Southeast Bankruptcy Workshop

# Case Law Update

**Hon. Benjamin A. Kahn**
U.S. Bankruptcy Court (M.D.N.C.) | Greensboro

**Hon. Sage M. Sigler**
U.S. Bankruptcy Court (N.D. Ga.) | Atlanta

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PLENARY SESSION

2022

# Case Law and Issues Update

**ABI Southeast Bankruptcy Workshop**

**July 24, 2022**

Hon. Sage M. Sigler, U.S. Bankruptcy Court (N.D. Ga.)

Hon. Benjamin A. Kahn, U.S. Bankruptcy Court (M.D.N.C.)

Prof. Lindsey D. Simon, University of Georgia School of Law

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# Subchapter V Cases

## Subchapter V – Discharge Issues

- *Cantwell-Cleary Co. v. Cleary Packaging, LLC (In re Cleary Packaging, LLC)*, No. 21-1981, 2022 U.S. App. LEXIS 15627 (4th Cir. June 7, 2022).
- *Gaske v. Satellie Rests, Inc. (In re Satellite Rests, Inc.)*, 626 B.R. 871 (Bankr. D. Md. 2021).

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## Subchapter V – Eligibility Issues

- *In re Port Arthur Steam Energy, L.P.*, 629 B.R. 233 (Bankr. S.D. Tex. 2021).
- *In re Tibbens*, No. BR 19-80964, 2021 Bankr. LEXIS 654 (Bankr. M.D.N.C. Mar. 19, 2021).
- *In re Vertical Mac Constr., LLC*, No. 6:21-bk-05120-LVV, 2021 WL 3668037, 2021 Bankr. LEXIS 2285 (Bankr. M.D. Fla. July 23, 2021).
- *In re Blue*, 630 B.R. 179 (Bankr. M.D.N.C. 2021).
- *Nat'l Loan Invs., L.P. v. Rickerson (In re Rickerson)*, ___ B.R. ___, 2021 Bankr. LEXIS 3403 (Bankr. W.D. Pa. Dec. 14, 2021).

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- *In re Walker*, 628 B.R. 9 (Bankr. E.D. Penn. 2021).
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## *Taggart* and its Progeny

- *Harker v. Eastport Holdings, LLC (In re GYPC, Inc.)*, 634 B.R. 983 (Bankr. S.D. Ohio 2021).
- *Beckhart v. Newrez LLC*, Case No. 21-1838, 31 F.4th 274 (4th Cir. April 15, 2022).
- *White-Lett v. Bank of N.Y. Mellon Corp (In re Lett)*, 635 B.R. 713 (Bankr. N.D. Ga. 2022).

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- *In re Purdue Pharma, L.P.,* 635 B.R. 26 (S.D.N.Y. 2021).
- *McAdams v. Robinson*, 26 F.4th 149 (4th Cir. 2022).
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## Attorney Issues

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## Supreme Court Cases

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# Automatic Stay Issues

## Automatic Stay Issues

- *Portuesi, et al. V. Bank of N.Y. Mellon (In re Portuesi*), Nos. 19-11275, 20-2018, 2022 Bankr. LEXIS 1104 (Bankr. M.D.N.C. Apr. 22, 2022).
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- *Houck v. Lifestore Bank*, No. 21-1280, 2022 WL 2813066, ___ F.4th ___ (4th Cir. July 19, 2022).

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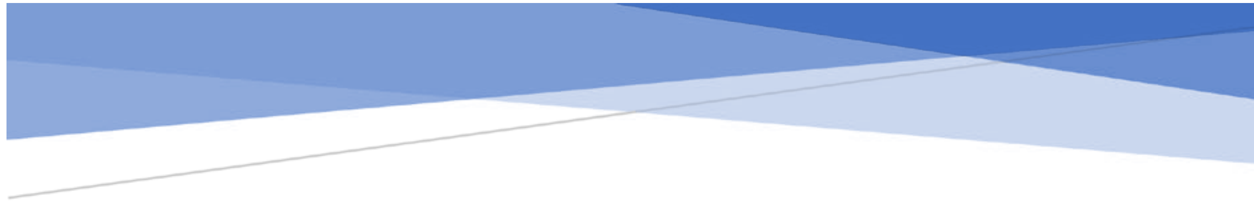

# ABI SOUTHEAST 2022 CONFERENCE

## Case Update

The Honorable Benjamin A. Kahn

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# I. Automatic Stay

## A. Defeo v. Winyah Surgical Specialists, P.A. (*In re* Defeo), 635 B.R. 253 (Bankr. D.S.C. 2022)

**Mistakenly sending an invoice constituted willful stay violation.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 2-3 (2022).

## B. Harker v. Eastport Holdings, LLC (*In re* GYPC, Inc.), 634 B.R. 983 (Bankr. S.D. Ohio 2021)

***Taggart* standard applies to contempt actions for willful stay violations in non-individual debtor cases.** *See* Richard Levin*, Recent Developments in Bankruptcy Law January 2022*, 1 (2022).

## C. *In re* Madsen, No. 22-20157-E-13, 2022 WL 1272583, 2022 Bankr. LEXIS 1148 (Bankr. E.D. Cal. Apr. 27, 2022)

**Stay does not terminate entirely on the thirtieth day after the petition date in second case brought after dismissal of a case pending within a year of the petition date.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported April 1 to June 30, 2022*, 2 (2022).

## D. Diocese of Rochester v. AB 100 Doe (*In re* Diocese of Rochester), Adv. P. No. 22-02075-PRW, 2022 WL 1638966, 2022 Bankr. LEXIS 1469 (Bankr. W.D.N.Y. May 23, 2022)

**Lack of chapter 11 plan feasibility may lead to denial of an extension of the automatic stay to non-debtor third-party entities.** This case involved sexual abuse claimants suing non-debtor Catholic institutions, such as schools and parishes. Debtor moved to extend the stay to these non-debtor entities after eleven extensions of a mutual "standstill agreement," which halted the sexual abuse litigation against the other Catholic entities. The court held that §362(a)(1) and (a)(6) do not apply to the other Catholic entities because the language of § 362 specifies "proceedings against the debtor" rather than proceedings related to the debtor's interests. Further, under §362(a)(3), debtor failed to show how allowing the proceedings to go forward would affect property of the estate. Finally, application of an injunction was unwarranted because injunctions require

analysis of the "likelihood of success," with "success" meaning successful reorganization. Because the case had been pending for three years and the debtor was now threatening cram down if the stay was not applied to the non-debtor entities, the court held that while it was not impossible to confirm a plan, it was highly unlikely and therefore denied imposition of the stay to the non-debtor entities.

### E. *In re* Dougherty-Kelsay, 636 B.R. 889, 899 (B.A.P. 6th Cir. 2022)

**Under § 362(b), there are very specific exceptions to the automatic stay that relate to child support and domestic support obligations.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 2 (2022).

### F. Portuesi, et al. v. Bank of N.Y. Mellon (In re Portuesi), Nos. 19-11275, 20-2018, 2022 Bankr. LEXIS 1104 (Bankr. M.D.N.C. Apr. 22, 2022)

**Based on the circumstances of this case, a creditor did not violate the codebtor stay by recoding a deed of trust on .** Debtor's mother granted the debtor a one half interest in property by gift deed, but the deed was recorded in the wrong jurisdiction. Debtor and his mother thereafter executed a promissory note and deed of trust in favor of lender, and the lender similarly recorded the deed of trust in the incorrect jurisdiction. Debtor's mother filed bankruptcy and received a chapter 7 discharge. Debtor filed a petition under chapter 13, objected to the creditor's secured claim, and the court disallowed the secured claim because the deed of trust was improperly recorded. Without seeking relief from the automatic stay or the codebtor stay, the mortgage servicer re-recorded the deed of trust in the correct jurisdiction. Debtor, unaware of the re-recording, completed his chapter 13 plan, and received a chapter 13 discharge of his personal liability under the note.

Debtor's mother thereafter properly transferred the property to the debtor and recorded the transfer in the appropriate county. Debtor then commenced a second chapter 13 case, and commenced an adversary proceeding with the chapter 13 trustee as co-plaintiff alleging that the recording of the deed of trust during debtor's first bankruptcy case violated the codebtor stay, was void, and the trustee could avoid the (therefore) unrecorded lien. Both parties filed motions for summary judgment. The court granted Defendant's motion and denied Plaintiffs' motion. The issue is whether the Bankruptcy Code prohibits the perfection of a lien against a codebtor's property without lifting the codebtor stay. To determine whether recording any deed of trust is an act to collect debt, the court must examine the purpose for recording a deed of trust. The court held that

recording a lien against property that is not property of the estate is not necessarily an act to collect a debt, and therefore is not a per se violation of the codebtor stay.

Although perfection of a lien is not a per se violation of the coedebtor stay, recording a lien against a codebtor's property can constitute a violation of the codebtor stay if the act creates any direct or indirect pressure on the debtor to repay the loan. After the recoding of the lien, Defendant took no action to collect from Debtor. Both Debtor and his mother testified that they did not feel pressure to repay the loan. In fact, they did not discuss the loan or repayment of it. Thus, based on the circumstances, the recoding of the deed of trust was not a violation of the codebtor stay.

**G. State Farm Fla. Ins. Co. v. Carapella (In re Gaime), 17 F.4th 1349 (11th Cir. 2021)**

**The automatic stay provision precluded the insurer's motion to intervene. Debtor was sued for wrongful death and bodily injury by the Rotells in state court.** Debtor was insured by State Farm, so she tendered her defense to State Farm. State Farm filed separate declaratory judgment and the state court ruled in State Farm's favor as State Farm did not have duty to defend Debtor. A jury verdict came in favor of the Rotells for $505 million. The Rotells petitioned the bankruptcy court for involuntary chapter 7 bankruptcy. With no response from Debtor, the bankruptcy court entered an order subjecting debtors' assets to its control. State Farm filed to intervene in Rotells' wrongful death action. Before doing so, State Farm requested relief from the automatic stay. The bankruptcy court denied the motion, and State Farm appealed. First, the court held that the plain language of § 362(a)'s is clear that the automatic stay applies to State Farm's motion to intervene because State Farm has an action against Debtor. Second, State Farm has not been deprived of due process because they had the opportunity to be heard when they filed the wrongful death action and voluntarily withdrew it. Finally, the court held that cause did not exist to lift the stay because there is no unfairness to State Farm.

## II. Jurisdiction

### A. Law Offices of Francis J. O'Reilly v. Selene Finance, L.P. (In re DiBattista), 33 F.4th 698, 700 (2d Cir. 2022).

Bankruptcy court's authority to award appellate fees in connection with contempt sanctions. The debtor reopened its chapter 7 case to file contempt proceedings against a mortgage servicer that attempted to collect delinquent mortgage payments in violation of the discharge order. The bankruptcy court awarded damages and fees for the debtor, and on appeal the district court vacated the award and remanded for clarification on whether the damages were actual or punitive. The bankruptcy court reinstated the original damage award, clarifying that the damages were compensatory, but rejected the debtor's request for additional fees incurred during the appeal because the bankruptcy court lacked authority to award such fees. The district court affirmed. On appeal the Second Circuit reversed both lower courts, concluding that the bankruptcy court's authority under § 105(a) extended to the award of appellate fees that were "caused by" the servicer's contempt.

### B. Byrnes v. Byrnes (*In re* Byrnes), 638 B.R. 821 (Bankr. D.N.M. 2022)

**Withdrawal of the reference unnecessary where the claims asserted were for defamation and emotional distress.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 3 (2022).

### C. LTL Mgmt., LLC v. San Diego Cnty. Emps. RET. Ass'n (*In re* LTL Mgmt., LLC), No. 21-30589 (MBK), 2022 WL 1295927, 2022 Bankr. LEXIS 1179 (Bankr. D.N.J. Apr. 29, 2022)

**Bankruptcy courts have the authority to extend the automatic stay to non-bankruptcy proceedings against non-debtor parties to protect the interests of the ongoing bankruptcy case.** *See* Richard Levin*, Recent Developments in Bankruptcy Law April 2022*, 3 (2022).

### D. VSP Labs, Inc. v. Hillair Capital Invs., L.P. (In re PFO Glob. Inc.), 26 F.4th 245, 254 (5th Cir. 2022)

**Relief from the automatic stay to liquidate claims in a state court action and to enable setoff was core, and the bankruptcy court had related to jurisdiction over the debtors claims**

**that were sold to a non-debtor. Therefore, the bankruptcy court could stop the non-debtor from amending its complaint against another nondebtor in the state court action.** In this case, VSP initiated a prepetition state court action against Debtor. After filing for bankruptcy, Debtor sold its counterclaims against VSP to Hillair. Hillair sought to sever the counterclaims from the state court action to proceed with liquidating the claims, and VSP sought relief from the stay to proceed with the state court claims so that it could liquidate its claim and assert its right to offset Debtor's claim. The parties provided the court with an order granting relief from the automatic stay. When VSP learned of conduct necessitating a claim against Hillair, the bankruptcy court enforced the previous order and disallowed VSP from amending its state court complaint to bring claims against Hillair. The relief from the automatic stay was a core matter, and the amended complaint was related to the bankruptcy case because successful claims against Hillair could reduce the amount of damages against debtor. The parties consented to the bankruptcy court's jurisdiction by offering the terms of the stay order, and the bankruptcy court had the jurisdiction to hear and enter appropriate orders relating to the state court proceeding between to non-debtors.

**E. Kreit v. Quinn (In re Cleveland Imaging & Surgical Hosp., LLC), 26 F.4th 285, 292 (5th Cir. 2022)**

**As an initial matter, a notice of appeal filed in the bankruptcy case will not operate as a notice of appeal in an adversary proceeding because these are distinct "judicial units." In addition, a notice of appeal must include the appropriate documents identified in Fed. R. Bankr. P. 8003(a)(3)(B) or else the appellate court's jurisdiction may be called into question. Aside from procedural requirements; after a liquidation trust terminates, the trustee retains an ongoing responsibility to protect the assets that he has yet to distribute to the beneficiaries. Therefore, a trustee retains an interest in defending decisions involving those assets when appealed.** *See* Richard Levin, *Recent Developments in Bankruptcy Law April 2022*, 8 (2022).

**F. Dean v. Seidel (In re Dean), 18 F.4th 842, 844 (5th Cir. 2021).**

**A chapter 7 Debtor does not have standing to appeal a bankruptcy order dealing with distribution of estate property where the order does not effect the discharge.** Debtor filed for chapter 7 bankruptcy and a trustee was appointed. The Trustee did not have sufficient unencumbered funds to retain counsel to pursue claims, so Trustee entered into a litigation financing agreement with one of Debtor's creditors. Debtor objected, claiming the agreement undermines the statutory ranking system for distribution of estate property. Standing to appeal a bankruptcy

order is a more exacting standard and requires the appellant to show that he is "directly, adversely, and financially impacted by a bankruptcy order." Where the discharge was not at issue, the debtor had no direct, adverse, nor financial interest in the order.

**G. NLG, LLC v. Horizon Hosp. Grp., LLC (In re Hazan), 10 F.4th 1244 (11th Cir. 2021)**

**The Rooker-Feldman doctrine did not apply to preclude the bankruptcy court from ruling on issues in adversary proceedings.** NLG, LLC sold a home ("Property") to Debtor and received a purchase money note and mortgage on the Property. Disputes arose with the Property between Debtor, NLF, and Selective Advisors Group, LLC ("Selective"). All of NLG's rights and claims against Debtor were assigned to Selective. By a court order, NLG was awarded $1.6 million. The day before the foreclosure of the Property, Debtor filed for relief under Chapter 11, and NLG filed a proof of claim. Debtor and Selective filed an adversary proceeding against NLG. Debtor filed an amended plan and did not include NLG's claim. The plan was approved on June 11, 2018. On August 8, NLF moved the court to stay the proceedings until the appeal in the adversary proceeding. The bankruptcy court denied the motion. On October 17, NLF appealed. The district court concluded that the Rooker-Feldman doctrine was inapplicable and dismissed NLG's claims because the claims are moot. NLG appealed to this court.

First, the Rooker-Feldman does not apply because Selective was not party to the state court and the issues in the bankruptcy court were different from the state court foreclosure proceeding. Second, the court held that the district court properly dismissed the appeal for equitable mootness because the factors of this case weigh in favor of equitable mootness. There was no stay in place for NLG, and there was substantial delay when NLG asked for relief.

**H. Reynolds v. Servisfirst Bank (In re Stanford), 17 F.4th 116 (11th Cir. 2021)**

**Mootness under section 363(m) applies to all authorizations and the inquiry included examining whether the buyer acted in good faith. Also, a complete sale order cannot be reversed by the court since the appeal is moot.** *See* Richard Levin, *Recent Developments in Bankruptcy Law January 2022*, 7 (2022).

## III. Case Commencement/ Eligibility

### A. *In re* Eht Us1, 630 B.R. 410 (Bankr. D. Del. 2021)

**Singapore law—not federal common law—applied for the purposes of determining debtor eligibility.** *See* Richard Levin, *Recent Developments in Bankruptcy Law July 2021*, 1 (2021).

### B. Visium Tech, Inc. v. Tarpon Bay P'ners, LLC (*In re* Visium Techs, Inc.), 635 B.R. 428 (Bankr. S.D. Fla. 2022)

**The term "petitioners" in § 303(i) does not include the principals, agents, or owners of entities filing an involuntary petition.** An involuntary chapter 7 petition was dismissed and the alleged debtor brought an adversary proceeding against the petitioners and their respective owners or principals for damages under §§ 303(i) and 105. The individual owners and principals for the petitioners each signed the involuntary petition on behalf of their respective entities. Section 303(i) permits a court to grant judgment "against the petitioners and in favor of the debtor." The issue on the individual defendants' motion to dismiss was whether they were "petitioners" within the meaning of § 303(i). The term is not defined in the Code. Looking to the plain text of § 303(i), the court found that the term "petitioners" only includes the entities signing the petition—not their principals, agents, or owners. This conclusion is bolstered by the definition of "creditor" under § 101(10)(A) as an "entity that has a claim against the debtor that arose at the time of or before the order of relief concerning a debtor." In an involuntary case, the order for relief is not entered until either the petition is not timely controverted or after a trial on a contested petition. Thus, use of the term "petitioner" in § 303(i) rather than "petitioning creditor" is meant to include entities whose claims have been determined invalid when assessing damages. Further, because § 303(i) is a fee-shifting statute, it should be construed strictly. As a result, the individuals' motion to dismiss was granted.

## IV. Bankruptcy Rules

### A. *In re* Cyber Litig., Inc., No. 20-12702, 2021 WL 5047512, 2021 Bankr. LEXIS 2966 (Bankr. D. Del. Oct. 28, 2021)

**Email notice of the bar date satisfied due process requirements but was insufficient under Rule 2002(a)(7).** *See* Richard Levin, *Recent Developments in Bankruptcy Law October 2021*, 3 (2021).

### B. Welt v. Bumshteyn (*In re* Bumshteyn), 637 B.R. 211 (Bankr. S.D. Fla. 2022)

**Failure to comply with local rule resulted in waiver of right to jury trial.** *See* Richard Levin, *Recent Developments in Bankruptcy Law April 2022*, 2 (2022).

### C. 5200 Enters. Ltd. v. City of N.Y., 22 F.4th 970 (11th Cir. 2022)

**Debtor's continuous trespass claim was barred by the New York statute of limitations. The Bankruptcy Abuse Prevention and Consumer Protection Act, 11 U.S.C. § 505(a)(2)(c), prohibited the bankruptcy court from redetermining any of the assessment, so Debtor's property tax challenge was foreclosed.** In 1986, 5200 Enterprises Limited (Debtor) bought a piece of property in Brooklyn. They City of New York was the owner of the Property around 1950s during which the Property was contaminated. Debtor failed to pay taxes and the taxes became liens on the property. In 2018, Debtor filed for Chapter 11 bankruptcy. Debtor filed an adversary proceeding against the City of New York and asserted that the city committed continuous trespass and sought declaratory judgment. The city filed a motion to dismiss the complaint for a failure to state a claim. The bankruptcy court granted the motion to dismiss.

First, the court found that Debtor's claim is barred by the statute of limitations of New York applicable law. Second, the court founds that the bankruptcy court was correct in dismissing the claim by holding that the Bankruptcy Abuse Prevention and Consumer Protection Act prohibited the court from redetermining any of the assessments. Applying BAPCPA to the pre-2005 taxes did not give the statute improper retroactive effect.

## V. Discharge Issues

### A. Loyle v. U.S. Dept. of Ed. (*In re* Loyle), Adv. No. 20-5073, 2022 WL 567724, 2022 Bankr. LEXIS 463 (Bankr. D. Kan. Feb. 24, 2022)

**Partial discharge of student loans permitted under *Brunner*.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 6 (2022).

### B. Gaske v. Satellite Rests, Inc. (*In re* Satellite Rests, Inc.), 626 B.R. 871 (Bankr. D. Md. 2021)

**Corporate debtors in subchapter V may discharge debts that would otherwise not be dischargeable under § 523(a).** *See* Richard Levin, *Recent Developments in Bankruptcy Law July 2021*, 4 (2021).

### C. Bach v. Office of Lawyer Regulation (*In re* Bach), No. 20-23343-KMP, 2022 WL 2068679, 2022 Bankr. LEXIS 1605 (Bankr. E.D. Wis. June 8, 2022)

**Debt arising from attorney disciplinary proceedings was non-dischargeable under § 523(a)(7).** Debtor was an attorney who brought an adversary proceeding to determine that the debt associated with her attorney disciplinary proceeding was discharged in her chapter 7 bankruptcy. The debt consisted of the costs of her disciplinary proceeding, which she was ordered to pay by the state supreme court. The court held that the costs were excepted from discharge under § 523(a)(7) because they constituted "a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss, other than a [particular] tax penalty." The state disciplinary rule required a finding of misconduct before an attorney in a disciplinary proceeding is assessed costs, thus such a cost assessment is a penalty within the meaning of § 523(a)(7). Further, under existing Seventh Circuit precedent, the penalty was not for "actual pecuniary loss" because the use of the Office of Legal Regulation's operating budget for investigative and disciplinary proceedings merely constituted "an expenditure by the government, part of the expense of governing" and was not undertaken with the expectation of creating a debtor-creditor relationship. As a result, the court granted defendant's motion for summary judgment and excepted the debt from discharge.

**D. Roth v. United States Dep't of Ed. (*In re* Roth), 638 B.R. 754 (Bankr. S.D. Ind. 2022)**

**Paying legal fees associated with aggressive litigation seeking a hardship discharge rather than attempting to repay student loan debt resulted in a finding of bad faith under *Brunner.*** Debtor brought an adversary proceeding seeking to discharge his federal student loan debt. The Department of Education moved for summary judgment. Debtor had previously engaged in costly litigation to reduce his private student loan debt, resulting in a monthly payment of $818 for legal fees. Applying the test from *Brunner v. New York State Higher Educ. Servs. Corp.,* 831 F.2d 395, 396 (2d Cir. 1987), the court found that defendant was entitled to summary judgment as to the second (additional exceptional circumstances exist making it improbably that the debtor will ever be able to repay the loans) and third prongs (good faith) of the *Brunner* test. Specifically, with respect to the third prong, the court concluded that debtor's decision to incur "hefty attorney fees" in the course of the private loan litigation and the dischargeability proceeding before it rendered it unable to conclude that he had made a good faith effort to repay his federal loans. The court was careful to note that it was not suggesting it was *per se* bad faith for debtors to incur legal fees in an effort to obtain a hardship discharge. But the amount of fees in this case was excessive. Debtor spent $42,500 in fees to discharge $80,00 in private student loans and $19,000 in fees for his litigation against the department of education, which resulted in debtor paying at times more than $1,000 per month in legal fees, an amount constituting one third of his net monthly income. The court took issue with debtor's arguments that he was wrongly dismissed from his pharmacy program—an argument that was costly to pursue in both sets of litigation. Finally, debtor elected to work a second job but never explained how his income from that job was spent. The court concluded that, while it would not require a debtor to work more than 40 hours a week to establish undue hardship, a debtor voluntarily doing so must explain why none of the additional income was spent servicing his student loan debt.

**E. Beckhart v. Newrez LLC, Case No. 21-1838, 31 F.4th 274, (4th Cir. 2022)**

**The standard adopted in <u>Taggart v. Lorenzen</u>, 139 S.Ct. 1795, which is the standard for holding a creditor in civil contempt for attempting to collect a debt discharged under Chapter 7, also applies when a court is considering whether to hold a creditor in civil contempt for violating a plan entered under Chapter 11.** *See* Richard Levin*, Recent Developments in Bankruptcy Law April 2022*, 6 (2022).

**D. Buckley v. Bartenwerfer (In re Bartenwerfer), 860 F. App'x 544, 545 (9th Cir. 2021), cert. granted sub nom. Bartenwerfer v. Buckley, No. 21-908, 2022 WL 1295707 (U.S. May 2, 2022).**

**Debtor is responsible for nondischargeable judgment debt arising out of imputed fraud of another, even without scienter.** A married couple filed a joint chapter 7 case that included among the debts a judgment against the husband for nondisclosure of material facts in connection with sale of real property. The couple had jointly purchased a home to renovate and sell, yet the wife had no involvement in or awareness of the condition of the property or the fraudulent representations made by the husband to the purchaser. The bankruptcy court determined that the debt was nondischargeable against the husband under § 523(a)(2)(A), but not against the wife who was innocent of the fraud. The Bankruptcy Appellate Panel affirmed the decision, but on appeal the Ninth Circuit reversed. The court joined a number of circuits that adopt a per se rule to § 523(a)(2)(A) that allows no exception for debtors without control or knowledge of the conduct triggering liability. This conflicts with other circuits that recognize the need for some level of scienter in imputing nondischargeability. The Supreme Court granted certiorari to address whether a debtor may be "subject to liability for the fraud of another that is barred from discharge in bankruptcy under . . . § 523(a)(2)(A), by imputation, without any act, omission, intent or knowledge of her own."

**E. Cutuli v. Elie (In re Cutuli), 13 F.4th 1342 (11th Cir. 2021)**

**The bankruptcy court did not abuse its discretion when it granted the motion to extend time for service.** *See* William Houston Brown, *Consumer Law Update, Cases reported from July 1, 2021 through September 15, 2021*, 6 (2021).

**F. Harris v. Jayo (In re Harris), 3 F.4th 1339 (11th Cir. 2021)**

**A general default judgment entered against Chapter 7 debtor in Florida state court action to recover for his fraudulent misrepresentation, negligent misrepresentation, investment fraud, and conspiracy to defraud could not be given collateral estoppel effect the claims were not identical to the elements under § 523(a)(2)(A).** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported from September 15, 2021 – December 31, 2021*, 4 (2021).

## VI. Claims and Priorities

### A. W. Wilmington Oil Feild v. Nabors Corp. Servs. (In re CJ Holding Co.), 27 F.4th 1105, 1108 (5th Cir. 2022).

**Whether to permit a late filed proof of claim is case specific, and in this case, there is no one factor that takes more weight.** *See* Richard Levin, *Recent Developments in Bankruptcy Law April 2022,* 2 (2022).

### B. Official Comm. of Unsecured Creditors v. PG&E Corp., Case No. 20-cv-4570-HSG, 2021 WL 2007145, 2021 U.S. Dist. LEXIS 96081 (N.D. Cal. May 20, 2021)

**Unimpaired, unsecured claims are entitled to receive interest payments at the federal judgment rate instead of the contract rate in solvent debtor cases**. *See* Richard Levin, *Recent Developments in Bankruptcy Law July 2021,* 3 (2021).

### C. Wells Fargo Bank, N.A. v Hertz Corp. (*In re* Hertz Corp.), 637 B.R. 781 (Bankr. D. Del. 2021)

**Make-whole premiums are allowed when they are not the economic equivalent of interest, which is a question of fact.** Wells Fargo sought a judgment requiring the debtor to pay a redemption premium to certain senior notes that were redeemed prior to maturity. In response, the debtor argued, in part, that the redemption premium is unmatured interest and must be disallowed under the Code. The court found that the make-wholes may be allowed only when they are not the economic equivalent of interest, which is based on the make-whole's terms and its relationship to the interest on the notes—all factual rather than legal questions. Further, disallowance of a claim under §502(b) does not render the class impaired, and therefore the notes were deemed unimpaired. Finding that the solvent debtor exception still applies in limited circumstances under §1129(a)(7) and §765(a)(5), the court applied it to the unimpaired notes, positing that there is no reason to treat impaired and unimpaired classes differently. Thus, the court held that when allowed, make-wholes are entitled to payment of post-petition interest at the federal judgement rate.

### D. *In re RGN-Grp. Holdings, LLC*, No. 20-11961 (BLS), 2022 WL 494154, 2022 Bankr. LEXIS 394 (Bankr. D. Del. Feb. 17, 2022)

**An objection to a proof of claim is a lawsuit and if a breach of contract suit arising**

**from a lease permits attorneys' fees, those fees may be allowed as part of the claim as long as the total claim falls below the §502(b)(6) cap.** The claim in question arose from debtor's breach of a lease. The creditor argued that it was contractually entitled to attorneys' fees resulting from the breach and debtor argued that there was no "suit" or "judgment" and that an allowed claim is merely a statement that a debt exists. The court disagreed, holding that an objection to a proof of claim, such as the one filed in this case by the debtor, is a lawsuit because it is a contested matter incorporating most of the rules applicable to adversary proceedings. Further, relying on Black's Law Dictionary, the court defined a "suit" as an ongoing dispute at any stage, and a "lawsuit" as a more formal proceeding in court, both of which fit the claim objection filed by the debtor in this case. Establishing that a suit or lawsuit did exist, the court then dealt with whether the attorneys' fees incurred by the creditor should be included in the allowed portion of the claim. Observing that the attorneys' fees cannot usually be collected in these cases as they would exceed the statutory cap in §502(b)(6), the court nevertheless concluded that the fees requested could be included in the claim because they fell below the statutory cap.

### E. *In re* Mullins, 633 B.R. 1 (Bankr. D. Mass. 2021)

**The "solvent debtor exception" requires payment at the federal judgment rate to rejecting classes under the "fair and equitable" analysis of §1129(b).** *See* Richard Levin, *Recent Developments in Bankruptcy Law April 2022,* 5 (2022).

### F. *In re* Verity Health Sys. of Cal., 633 B.R. 607 (Bankr. C.D. Cal. 2021)

**Pension underfunding claims are pre-petition debts not allowable as administrative expense claims.** *See* Richard Levin, *Recent Developments in Bankruptcy Law April 2022,* 5 (2022).

### G. *In re* Ditech Holding Corp., No. 19-10412 (JLG), 2022 WL 1750997, 2022 Bankr. LEXIS 1514 (Bankr. S.D.N.Y. May 28, 2022)

**Collateral attacks on an otherwise valid final state court decision cannot be relitigated in bankruptcy court as a claim against the debtor.** A *pro se* homeowner whose home was foreclosed upon prepetition filed a claim for the full value of the home after the claims bar date, alleging that the debtor had stolen his house. The court determined that the debtor had actual notice of the bar date and the claim was therefore time-barred. Further, applying the *Rooker-Feldman* doctrine, the court found it would be required to "look behind" the state court judgment and reject it for the claim to go forward, an action the doctrine states the bankruptcy court lacks the jurisdiction

to perform. Last, the doctrine of res judicata precluded the claimant from relitigating the claims against the debtor he previously brought in a state court action and also in a prior bankruptcy proceeding.

### H. Copley v. United States, 959 F.3d 118 (4th Cir. May 12, 2020)

**A debtor's interest in overpaid taxes is property of the estate, and § 553(a) overrides § 522(c) such that a debtor's exemptions cannot impair the IRS' right to offset unpaid taxes against previously overpaid taxes.** The Copleys' ("Debtors") listed a prepetition tax debt of $13,547.10 in their schedules but claimed as exempt $3,208.00 in overpaid 2013 taxes. After Debtors filed their 2013 tax returns, the IRS withheld the refund on the overpayment and explained that it was exercising its right to set-off under 26 U.S.C. § 6402(a). Debtors filed an adversary proceeding seeking to compel the government to remit the overpayment. The government response was that the overpayment was not property of the estate. Further, the government argued that it had a right to set-off the preexisting tax liability under § 6402(a). The bankruptcy court determined, and the district court affirmed, that the overpayment was property of the bankruptcy estate and that the government could not exercise its right to set-off

The bankruptcy estate is expansive and includes debtor's rights to bring legal claims. As § 542(b) states; "any entity that owes a debt that is property of the estate . . . shall pay such debt to . . . the trustee, except to the extent that such debt may be offset under § 553 of this title against a claim against the debtor." The court reasoned that until the defense was appropriately asserted, the legal claim retained value. Therefore, following this logic, the court determined that the bankruptcy estate captures Debtors' interest in the overpayment. Next, the court resolved what was perceived as conflicting statutes, 26 U.S.C. § 6402(a) and 11 U.S.C. § 522(c), by looking to § 553(a). Section 6402(a) allows the IRS to offset any overpayment against tax liabilities. Section 522(c) shields exempt property from being used to satisfy prepetition debt, save a few exceptions. While § 553(a) does not create a set-off right, it does provide that title 11 "[cannot] affect any right of a creditor to offset a mutual debt owing by such creditor to the debtor that arose before the commencement of the case under this title against a claim of such creditor against the debtor that arose before the commencement of the case." The court decided that the broad proscription in § 553(a) overrides the proscription identified in § 522(c). As such, Debtors' exemption did not affect the government's right to offset its tax liability claims.

## VII. Executory Contracts

### A. FERC v. Ultra Res., Inc. (In re Ultra Petro. Corp.), 28 F.4th 629, 639 (5th Cir. 2022)

**A bankruptcy court may authorize the rejection of a filed-rate contract that falls under FERC's umbrella so long as rejection is not a collateral attack on the rate, or an veiled attempt to renegotiate a lower rate. The bankruptcy court must employ a standard above the normal business judgment standard and consider the public interest when approving the rejection.** Debtor is a natural gas company that contracted with a pipeline company to reserve space in its pipelines. Under the Natural Gas Act, Debtor and the pipeline company filed the rate-contract with FERC. The rate could not be modified without FERC approval. After entering the contract, Debtor ceased drilling operations and filed for bankruptcy. Debtor sought to reject the contract, and FERC objected based on it having the exclusive authority to amend rates. After the bankruptcy court approved the rejection, the Fifth Circuit was presented with the potential conflict between the bankruptcy code and the Natural Gas Act. The Fifth Circuit looked to its past precedent in Mirant Corp. to resolve the issue and to explain its ruling. Rejecting a rate-contract is different from a rate change. Any potential creditor retains their right to sue on the contract breach. In this light, FERC does not have exclusive authority over rate-contract breaches. Therefore, the bankruptcy court had the power to authorize rejection of this rate-contract. Further, in explaining Mirant Corp., the Fifth Circuit said that it was not dicta when it decided courts can enforce the contract rejection, meaning that the bankruptcy court possessed the power to enjoin FERC from compelling a debtor to comply with the rate-contract. The Fifth Circuit affirmed the bankruptcy courts decision because it had considered the public interest, a step above the business judgment, when it granted Debtor's request. Further, because Debtor was ceasing drilling operations, Debtor was not attempting to renegotiate a rate change in bankruptcy.

### B. *In re* Brick House Props., LLC, 633 B.R. 410 (Bankr. Utah 2021)

**Entry of a specific performance order rendered a contract no longer executory.** A chapter 11 debtor moved to reject a real estate purchase contract with a creditor. The contract was contingent upon town approval of a subdivision. Debtor interfered with the purchaser's efforts to obtain town approval. Prior to the petition date, the creditor obtained an order of specific performance from the state court, limited to resolving a variance issue associated with the real estate purchase agreement. The court found that entry of the specific performance order rendered the contract no longer executory because it was intended to remove debtor's discretion as to performance under the contract. Further, under state law, an equitable conversion of title results

once a contract becomes subject to a specific performance order. Thus, the motion to reject was denied.

**C. *In re* Cornerstone Valve, LLC, No. 19-30869, 2021 WL 1731770, 2021 Bankr. LEXIS 1120 (Bankr. S.D. Tex. Apr. 27, 2021)**

**Contracts repudiated by debtors prior to bankruptcy are not considered executory.** *See* Richard Levin, *Recent Developments in Bankruptcy Law July 2021,* 4 (2021).

**D. *In re* Bennett Enters., 628 B.R. 481 (Bankr. D.N.J. 2021)**

**Contract no longer executory where specific performance order has been entered and the parties' obligations under the contract were all but complete.** *See* Richard Levin, *Recent Developments in Bankruptcy Law October 2021,* 7 (2021).

**E. *In re* Minesen Co., 635 B.R. 533 (Bankr. D. Haw. 2021)**

**Government can waive Anti-Assignment Act protections by limiting its power to reject assignments.** *See* Richard Levin, *Recent Developments in Bankruptcy Law April 2022,* 6 (2022).

**F. Highland Capital Mgmt., L.P. v. Dondero (*In re* Highland Capital Mgmt., L.P.), Case No. 19-34054-sgi11, WL 5769320, 2021 Bankr. LEXIS 3314 (Bankr. N.D. Tex. Dec. 3, 2021)**

**Rejecting an executory contract containing an arbitration provision also results in rejection of the arbitration agreement.** *See* Richard Levin, *Recent Developments in Bankruptcy Law January 2022,* 6 (2022).

## VIII. Trustees, Committees, Professionals

### A. Siegel v. Fitzgerald, 142 S. Ct. 1770 (2022).

**United States Trustee fees outlined in 28 U.S.C.A. § 1930(a)(B)(6) violates the uniformity requirement of the Bankruptcy Clause and is unconstitutional.** In 2017, Congress approved a temporary increase in fees to cover a shortfall in the UST Fund, which pays for the United States Trustee Program in every state except for Alabama and North Carolina. A chapter 11 debtor challenged the increase in quarterly fees it paid to the U.S. Trustee, claiming that the increase (which did not apply in the two states that have Bankruptcy Administrators instead of U.S. Trustees) was unconstitutional. The bankruptcy court found that the increased fees were unconstitutional, but did not address whether the debtor could be reimbursed for overpayments. On appeal, the Fourth Circuit reversed, holding that the increase was not a violation of the uniformity requirement because the funds benefitted only states that have U.S. Trustees, justifying the diusparity. The Supreme Court reversed the Fourth Circuit and held that the statute was unconstitutional. It first rejected the assertion that the fee increase was not subject to the uniformity clause because it was about the administration of the bankruptcy system and not substantive bankruptcy law. The uniformity clause applies equally to substantive and administrative bankruptcy law. The Court next held that the 2017 Act caused an impermissible disparity across geographic regions that stemmed from Congress' actions in creating two systems with different funding mechanisms. Importantly, the Court did not address how to provide a remedy to aggrieved debtors, and remanded to the Fourth Circuit for consideration of that issue.

### B. Official Comm. of Unsecured Creditors v. CIT Grp (*In re* Jevic Holding Corp.), Adv. Pro. No. 08-51903(BLS), 2021 WL 1812665, 2021 Bankr. LEXIS 1203 (Bankr. D. Del. May 5, 2021)

**Waiver of claims against creditors in a DIP financing order binds a subsequently appointed chapter 7 trustee.** *See* Richard Levin, *Recent Developments in Bankruptcy Law July 2021,* 5 (2021).

### C. *In re* Paragon Offshore, PLC, 629 B.R. 227 (Bankr. D. Del. 2021).

**Payments to beneficiaries of a liquidating trust created under a confirmed plan do not constitute "disbursements" for the purpose of calculating US Trustee fees.** *See* Richard Levin, *Recent Developments in Bankruptcy Law July 2021,* 7 (2021).

**D. *In* re Summit Fin., Inc., 634 B.R. 376 (Bankr. C.D. Cal. 2021)**

**Borrowing boilerplate language used in other filings that contravenes the duties of the DIP may lead to sanctions.** *See* Richard Levin, *Recent Developments in Bankruptcy Law January 2022,* 8 (2022).

**E. *In re* 218 Jackson LLC, 631 B.R. 937 (Bankr. M.D. Fla. 2021)**

**A subchapter V trustee is not disinterested when the trustee possesses a materially adverse interest to the single individual who is the principal of the debtor.** *See* Richard Levin, *Recent Developments in Bankruptcy Law January 2022,* 7 (2022).

**F. In re Boy Scouts of Am., 35 F.4th 149, 154 (3d Cir. 2022).**

**Bankruptcy court properly reviewed retention application under Section 327 without examining the Rules of Professional Conduct.** The debtors moved to retain a law firm as restructuring counsel that had previously represented an affiliate of one of the debtors' insurers in seeking backup coverage from reinsurers. The affiliate had issued policies to the debtor that were assets of the estate. The law firm initially asked for a conflict waiver from the insurer, but after the insurer refused to grant a waiver and challenged the retention the law firm withdrew from representation of the insurer's affiliate. The insurer objected to the retention application, alleging the law firm had an actual conflict that would prejudice the insurer. The bankruptcy court approved the retention under § 327(a), noting the possibility of a conflict but finding nothing that rendered the law firm unable to represent the debtor. The bankruptcy court also evaluated potential violations of Rules of Professional Conduct 1.9 and 1.7, but concluded that disqualification was inappropriate. The court noted that the law firm had put an ethical screen in place between its restructuring and insurance teams, and there was no evidence that confidential information was passed between the teams. The district court affirmed solely on the basis of § 327(a) without addressing Rules 1.7 or 1.9. On appeal, the Third Circuit held that the bankruptcy court had not abused its discretion in evaluating the law firm's retention. The court rejected the idea that a bankrupty court must consider the professional rules in retention decisions. While reliance on such standards may be necessary in some cases, this case could be decided by looking to § 327(a) alone. The court declined to address whether the "hot potato" doctrine requiring application of more stringent Rule of Professional Conduct 1.7 applies when a debtor stops representing a client to eliminate conflicts allowing representation of a more lucrative client.

### G. Anderson v. Morgan Keegan & Co. (In re Infinity Bus. Grp., Inc.), 31 F.4th 294 (4th Cir. 2022)

**As a representative of the estate, the Trustee can assert the causes of action possessed by the debtor, § 541, or possessed by a hypothetical lien creditor. §544(a)(1)). However, this is a double-edged sword. Under § 541, Trustee is subject to any defenses that the Debtor may have been subject to, including the defense of *in pari delicto*. Under § 544(a)(1), which looks to state law to define the rights of a hypothetical judgment lien creditor, the same logic applies.** Debtor's business was collecting bad checks, but its CEO and Board of Directors employed techniques to inflate its accounts receivables past reality. Many of those that participated in the accounting had already been held responsible, but the Trustee wished to pursue actions against a contractor that had assisted in soliciting investments. Notably, the contractor had previously flagged the relevant accounting practices as problematic. The Trustee, who had been appointed by the bankruptcy court, brought common law fraud and breach of fiduciary duty actions under South Carolina law (where Infinity's operations center was located) and an aiding and abetting breach of fiduciary duty action under Nevada law (where Infinity was incorporated). After a bench trial, the bankruptcy court found that Trustee failed to prove any of the elements of the claims and that the Trustee was subject to the affirmative defense of *in pari delicto*, which bars recovery by a plaintiff who bears equal or greater fault in the alleged tortious conduct. On appeal to the Fourth Circuit, the Trustee did not dispute the factual findings but instead challenged whether the affirmative defense of *in pari delicto* applies. While it was settled that a Trustee was subject to such a defense under § 541, Trustee argued that he had taken on the role of an innocent hypothetical judgment lien creditor under § 544(a)(1). The court's analysis focused on the rightss available under state law. In Nevada, judgment creditors may pursue those claims that the judgment debtor has the power to assign. Therefore, the court reasoned that the Trustee would be subject to the same defenses of a debtor, and that the court was under the same logic it had relied on under § 541.

### H. Skyline Restoration, Inc. v. Church Mut. Ins. Co., 20 F.4th 825 (4th Cir. 2021)

**Under § 108, the power to toll a statute of limitations is not available to an assignee who may collect on the claim.** In this case, Debtor contracted with a repair company to rebuild a damaged church. As payment, the Debtor assigned any right to insurance proceeds. Debtor then filed for bankruptcy and resolved the claims against the contractor by assigning them "any and all claims against any policies of insurance that may provide payments for work performed by [Contractor]." The insurance agency disputed coverage and the contractor stopped work, later

bringing an action to recover the value of services rendered. The district court dismissed the claim, finding that it was barred by the applicable North Carolina statute of limitations. North Carolina provides a three-year statute of limitations for claims seeking recovery from an insurance agency. Here, the contractor was outside the window but attempted to use the tolling provisions under § 108(a). The Fourth Circuit made clear that the "position as an assignee is notably different from the role of a trustee or a debtor-in-possession." The assignee does not owe a fiduciary duty to the bankrupt's creditors and instead may act in their own self-interest, which can serve to the detriment of the other creditors. Therefore, the benefits under § 108 are not available to the self-interested party.

### I. Bear Creek Trail, LLC v. BOKF, N.A. (In re Bear Creek Trail, LLC), 35 F.4th 1277 (10th Cir. 2022).

**Only the chapter 7 trustee—and not the debtor's former management—has authority to challenge conversion from chapter 11 to chapter 7.** The debtor was owned by a number of entities that were created and administered by an individual manager. Due to a state law turnover proceeding against the manager, a receiver controlled the debtor and related entities. The receiver moved to convert the debtor's case to chapter 7, and upon conversion a trustee was appointed to administer the estate. The manager (on behalf of debtor) appealed the bankruptcy court's order converting the case, and the creditor and receiver moved to dismiss the appeal. The district court dismissed the appeal because the manager had no right to bring the debtor's appeal. The Tenth Circuit affirmed the judgment, rejecting the manager's argument that the conversion was nonconsensual and concluding that the trustee was the sole party with authority to appeal on behalf of the debtor after conversion.

## IX. Avoiding Powers

### A. Cook v. United States (*In re* Yahweh Ctr., Inc.), 2022 U.S. App. LEXIS 6014 (4th Cir. Mar. 8, 2022)

**Under the Bankruptcy Code and the North Carolina Uniform Voidable Transactions Act, tax penalty obligations are not voidable**. As a matter of first impression, the Fourth Circuit looked to whether tax penalties and payments can be avoided under § 544. As the court noted, the Sixth Circuit had addressed this issue in In re Southeast Waffles, LLC, 702 F.3d 850 (6th Cir. 2012), which held that tax penalty obligations were not avoidable under the Bankruptcy Code or the Tennessee fraudulent transfer statute. The Sixth Circuit reasoned that the "noncompensatory penalties assessed and collected by the IRS do not fit neatly into the fraudulent transfer context." Waffles, 702 F.3d at 859. Under § 544 of the Bankruptcy Code, a Chapter 11 trustee "may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim." For a transfer to be avoided, it must be "voidable under applicable law by a creditor holding an unsecured claim." 11 U.S.C. § 544 (b)(1). In this case, the applicable law was the North Carolina Uniform Voidable Transactions Act, which provides that debt obligations are voidable "if the debtor made the transfer or incurred the obligation without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation." N.C. Gen. Stat. § 39-23.5. The court drew parallels between Tennessee and North Carolina, finding that that tax penalties do not fit within the obligations contemplated by the Voidable Transactions Act. The Act requires an exchange, which "suggests that for an obligation to be incurred as contemplated by the Act, an oral or written agreement must take place." Cook, 2022 U.S. App. LEXIS at *11. In this case, Debtor and IRS did not orally agree on the tax penalties and there is no evidence of a written record of the penalties.

### B. Faulkner v. Ford Motor Credit Co., LLC (*In re* Reagor-Dykes Motors, LP), No. 18-50214-RLJ-11, 2022 WL 2046144, 2022 Bankr. LEXIS 1570 (Bankr. N.D. Tex. June 3, 2022)

**The Ponzi Scheme Presumption only applies to traditional Ponzi schemes, not "Ponzi-like" frauds.** Debtor was a series of affiliated car dealerships that generated significant revenue and was a top-performing dealership with hundreds of millions of dollars in revenue from car sales and servicing, selling parts, and collecting accounts receivable. But debtor was unprofitable and substantially undercapitalized due to excessive partner draws, employee compensation, and

overhead resulting in an inability to services its obligations due to a lack of liquidity for the two years leading to its filing. To cover debtor's shortfall, its CFO orchestrated several fraudulent acts. An FBI investigation led to multiple federal fraud and fraud-related charges against at least 15 employees, including the CFO, all of whom pleaded guilty.

The chapter 11 trustee appointed under debtor's confirmed plan brought a fraudulent transfer claim against debtor's largest unsecured creditor to recover fraudulent and preferential transfers made to it. The Ponzi Scheme Presumption contained in § 548(a)(1)(A) relieves a plaintiff from having to establish fraudulent intent for each allegedly fraudulent transfer. Conceding that debtor did not operate a classic Ponzi scheme, the trustee nevertheless argued the Ponzi scheme presumption applied to his fraudulent transfer claim because debtor engaged in "Ponzi-like" frauds. The court found that the Fifth Circuit has limited application of the Ponzi Scheme Presumption to true Ponzi schemes and further explained that even if expansion of the doctrine were supported by existing precedent, its application in this case would constitute a radical departure from the statute since the transferor was a business paying legitimate obligations. The court therefore granted the creditor's motion for summary judgment as to the application of the Ponzi Scheme Presumption.

**C. In re City Center Healthcare LLC, Case No. 21-50796, 2022 Bankr. LEXIS 1638 (Bankr. D. Del. June 13, 2022).**

**Without determining whether the amendments to § 547(b), that a "trustee may, based on reasonable due diligence in the circumstances of the case and taking into account a party's known or reasonably knowable affirmative defenses under subsection (c), avoid any transfer . . .," creates a new element to preference actions, a party pleads facts sufficient to survive a motion to dismiss if they reference activities taken in investigating affirmative defenses.** The details of this case are not as important as the procedural posture. Debtor brought a preference action to avoid prepetition payments totaling $853,284.00. The defendant brought a motion to dismiss, and relevant here, argued that the debtors had not pled enough facts to show their due diligence in considering affirmative defenses. The court noted a split as to whether the new amendment creates a separate condition precedent to bringing a claim. However, the court declined to decide this issue and instead decided that the facts as pled were sufficient even if it were to decide this is a separate element. More specifically, the court concluded that "there is no requirement that the Debtors plead how the affirmative defenses are not available; the Debtors must simply plead that they considered them." The complaint alleged that debtors considered the transfers and whether they were protected from avoidance by applicable defenses, and that they "sent Demand Letters to the Defendants inviting an exchange of information regarding any potential defenses."

**D. Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC, No. 08-01789 (CGM), 2022 WL 2015662, 2022 Bankr. LEXIS 1575 (Bankr. S.D.N.Y. June 6, 2022)**

**Fictitious profits of a Ponzi scheme recoverable from former customers.** The trustee for the Securities Investment Protection Act (SIPA) liquidation of Bernard L. Madoff Investment Securities ("BLMIS") sued to recover $350,000 in fictitious profits from the probate estate of a former customer. Avoidance of a fraudulent transfer under § 548(a)(1)(A) requires "(i) a transfer of an interest of the debtor in property; (ii) made within two years of the petition date, (iii) with 'actual intent to hinder, delay, or defraud' a creditor." The central issue was whether the transfers were "of an interest of the debtor in property." SIPA permits the recovery of "customer property," defined as "securities actually allocated to customer accounts" as well as cash and securities held, received, or acquired at any time for the securities account of a customer. The transfers the trustee sought to recover were funded by checks drawn from one of three accounts used by BLMIS for the investment advisory business. The trustee established that the account—held in the name of Bernard L. Madoff—along with all the assets and liabilities of the sole proprietorship, was transferred to BLMIS prior to the challenged transfers. The defendants were unable to rebut that evidence. Further, when the defendants invested their money, the deposits were placed into accounts and comingled with the Ponzi scheme victim's deposits. Thus, because the trustee only had to establish that the property sought was "customer" property prior to the transfer, he need not have shown that the accounts were transferred to BLMIS prior to the challenged transfers. As a result, the transfers were "of an interest of the debtor in property" and summary judgment was granted in favor of the trustee.

## X. Chapter 7 Issues

### A. Attorneys

1. **Matthews & Assocs v. Fitzgerald (*In re* Prophet), No. 4:21-CV-01081-JMC, 2022 WL 766390, 2022 U.S. Dist. LEXIS 44523 (D.S.C. Mar. 14, 2022)**

**Bifurcated fees approved as not violating local bankruptcy rule on continued representation.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 7-8 (2022).

2. **Sylvester v. Chaffe McCall, L.L.P. (In re Sylvester), 23 F.4th 543, 549 (5th Cir. 2022)**

**Under § 326(a), the Chapter 7 Trustee fees are treated as a commission and the bankruptcy court must review any additional compensation under §330(a). In this context, under § 330(a), compensation is limited to those services necessitating legal expertise. The bankruptcy court must carefully review the services to ensure they do not fall within the trustee's typical responsibilities, even when the case reaches a successful result.** *See* Richard Levin, *Recent Developments in Bankruptcy Law April 2022,* 10 (2022); William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 8 (2022).

### B. Reopening a Closed Case

1. ***In re* Ostrowski, 635 B.R. 181 (Bankr. M.D. Fla. 2022)**

**Reopening to allow filing of reaffirmation agreement was denied.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 8 (2022).

### C. Discharge Injunction

1. **White-Lett v. Bank of N.Y. Mellon Corp (*In re* Lett), 635 B.R. 713 (Bankr. N.D. Ga. 2022)**

**Discharge of personal liability subjected mortgage servicer to potential discharge injunction violation but *Taggart* standard applied.** *See* William Houston Brown, *Consumer Law*

*Update, Selected Cases Reported January 1 to March 31, 2022*, 9-10 (2022).

### D. Conversion from Chapter 7 to Chapter 13

#### 1. *In re* Mitchell, 638 B.R. 455 (Bankr. D. Idaho 2022)

**Chapter 7 trustee's compensation disallowed as an administrative expense in case converted from 7 to 13 when no distributions were made while the case was pending under chapter 7.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 10-11 (2022).

### E. Conversion to Chapter 7.

#### 1. Baroni v. Seror (In re Baroni), 36 F.4th 958 (9th Cir. 2022).

**Party seeking conversion to chapter 7 has initial burden of persuasion. Post confirmation, a secured creditor bank moved to convert the individual debtor's chapter 11 case for failure to make approved plan payments.** The bankruptcy court converted the case due to the debtor's material default of her payment obligations. The chapter 7 trustee moved for turnover of the debtor's rental property proceeds, which under the plan belonged to the estate. The debtor appealed both the conversion and the bankruptcy court's decision granting the turnover motion. On appeal, the Ninth Circuit held (in an issue of first impression) that a party seeking to convert a case to chapter 7 has the initial burden of persuasion to establish cause for conversion. The court concluded that the bank had satisfied its burden, and affirmed the bankruptcy court's decisions to convert the case and order turnover of estate assets.

## XI. Chapter 11 Issues

### A. Subchapter V Eligibility

#### 1. *In re* Port Arthur Steam Energy, L.P., 629 B.R. 233 (Bankr. S.D. Tex. 2021)

**Collection of accounts receivable and maintenance of physical assets during a wind down qualifies as "being engaged in commercial or business activities" for the purposes of determining subchapter V eligibility.** *See* Richard Levin, *Recent Developments in Bankruptcy Law July 2021,* 2 (2021).

#### 2. In re Tibbens, No. BR 19-80964, 2021 Bankr. LEXIS 654 (Bankr. M.D.N.C. Mar. 19, 2021)

**The "order for relief" used to calculate the deadlines in subchapter V is the original petition, not the order converting the case to subchapter V. However, in chapter 11, dismissal requires both the subjective bad faith and objectively futility. Confirming a plan is not objectively futile where a debtor fails to file a report under § 1188(a), if there is no status conference scheduled, and where the debtor fails to comply with the deadline to file a plan under § 1189(b).** Debtor commenced a chapter 13 case on December 29, 2019. Over the course of the Chapter 13 case, there were significant issues with a § 363(b) motion to sell real property free and clear of all liens. After several hearings on the matter, Trustee filed a motion to dismiss the case due to Debtor exceeding the debt limits under § 109(e). Debtor withdrew the Amended Sale Motion on and filed a Motion to Convert to a chapter 11 case on July 21, 2020. The Bankruptcy Administrator argued that Debtor could not meet the deadlines under §§ 1188 and 1189, nor fund a chapter 11 plan. On September 30, 2020, Debtor filed a motion to extend the deadlines to hold a status conference and file a plan. The court granted the Motion to Convert and denied the Motion to Extend Deadlines.

Both §§ 1188 and 1189 use the ubiquitous language "after the entry of the order for relief under this chapter" to work as a triggering point for deadlines. Section 348(a) states "conversion of a case from a case under one chapter of this title to a case under another chapter of this title constitutes an order for relief under the chapter to which the case is converted, but . . . does not effect a change in the date of the filing of the petition, the commencement of the case, or the order for relief." Section 348(b) provides a list of statutory provisions that require the court to construe the date of the order converting the case as the date of the order for relief. As the court noted, §§

1188 and 1189 do not appear on that list. As such, the starting point for the deadlines was the date of the petition.

In chapter 11, and under Fourth Circuit precedent, § 1112 limits dismissal or conversion to chapter 7 to instances where the petition was filed with subjective bad faith and where the court finds that any reorganization is objectively futile. The court determined that the subchapter V filing deadlines, which had not been extended, would not render a reorganization objectively futile and, therefore, the court had limited discretion in dismissing the case. First, the court decided § 1188(b) does not apply unless the court already set the status conference. Section 1188(a) required that the court hold a status conference "not later than 60 days after the entry of the order for relief under this chapter[.]" Under § 1188(c), debtor would have had to report his efforts in reaching a consensual plan within 14 days of the status conference. The code placed the deadline to hold a status conference on the court. Debtor could not be late in reporting until after the clock started running. Second, juxtaposing the difference between small business cases and subchapter V, the court decided that failure to file a timely plan, standing alone, is not fatal to confirmation. Under § 1189(b), the Debtor had to file a plan "not later than 90 days after the order for relief under this chapter[.]" Therefore, the question arose whether conversion would be objectively futile since Debtor missed the 90-day window. The court noted that while § 1112(b)(4)(J) does list failure to file a timely plan as cause to dismiss or convert the case, § 1112(b)(2) prohibits dismissal under certain circumstances and creates a safe-harbor. Unlike the "unforgiv[ing]" small business deadlines in § 1121(e), made mandatory under §1112(b)(2)(A), the court determined that the safe harbor available to subchapter V debtors would be incongruent if the extant cause required dismissal or conversion. Further, the court noted that the safe harbor in § 1112(b)(2)(B) did not exclude those debtors who had failed to file or confirm a plan within the deadline from its protections as it did when cause to dismiss or convert arises under § 1112(b)(4)(A) as a result of a substantial or continuing loss or diminution to the estate. Finally, the court explained that §§ 1129(a)(1) & (a)(2) would not necessitate strict adherence to the deadlines in §1189 to achieve a confirmable plan. Rather, these provisions primarily apply to the contents of the plan and the solicitation and disclosure requirements, respectively, and cannot be used to prevent confirmation for any technical failure. Therefore, the court determined that Debtor's failure to adhere to § 1189, standing alone, would not bar confirmation and thus not result in an objectively futile plan.

3. ***In re* Vertical Mac Constr., LLC, No. 6:21-bk-05120-LVV, 2021 WL 3668037, 2021 Bankr. LEXIS 2285 (Bankr. M.D. Fla. July 23, 2021)**

**Maintaining bank accounts, actively working with insurance companies to resolve**

**outstanding claims, and preparing itself for a sale of assets constitute business activities for the purposes of determining subchapter V eligibility.** *See* Richard Levin, *Recent Developments in Bankruptcy Law October 2021,* 3 (2021).

4. ***In re* Blue, 630 B.R. 179 (Bankr. M.D.N.C. 2021)**

**There need not be a nexus between a debtor's current business activities and the business debt she is using to qualify as a debtor under subchapter V.** Debtor was formerly the sole owner and president of an entity that ceased operations prior to the petition date and had no assets as of the petition date. At the time of filing, debtor was a W-2 employee and also worked as an independent contractor for two other entities. She filed a voluntary petition for relief under chapter 11 and elected to proceed under subchapter V. The Bankruptcy Administrator objected to the subchapter V election, arguing among other things, that debtor was not a person "engaged in business or commercial activities." The court adopted the definition of a person "engaged in commercial or business activities" as a person that "participates in the purchasing or 'selling of economic goods or services for a profit'" and found that the debtor must presently be participating in business or commercial activities as of the petition date. Debtor's independent contract work qualified as commercial or business activities. Further, debtor's business debt need not be related to her current business activities since the intent of subchapter V was is to address debts arising from both defunct and non-defunct business activities. Finally, nothing in the statute required a nexus between qualifying debts and the debtor's current business or commercial activities and requiring such a nexus could disqualify small business debtors for having significant debts from former operations.

## B. Officers and Administration

1. **Springfield Hosp., Inc. v. Guzman (In re Springfield), 28 F.4th 403, 407 (2d Cir. 2022).**

**Debtors' ineligibility for CARES Act relief does not violate the Bankruptcy Code's antidiscrimination provision.** Debtor hospital filed an adversary proceeding against the Small Business Administration ("SBA") alleging discrimination in violation of § 525(a) due to its policy that debtors are ineligible for the Paycheck Protection Program ("PPP"). The bankruptcy court granted summary judgment for the debtor and permanently enjoined the SBA from denying the debtor's PPP application. The Second Circuit reversed, holding that § 525(a) does not apply to the PPP, which is a loan guaranty program and not an "other similar grant." The court's ruling

acknowledged that the SBA's sole reason for denying the debtor's application for benefits was its bankrupt status, but looking to the Code's plain meaning it concluded that loans were not covered under § 525(a). The court did not resolve whether the bankruptcy court's injunction violated the SBA's sovereign immunity granted by 15 U.S.C. § 634(b)(1), but vacated the injunction in light of its holding on § 525(a) and remanded the case for further proceedings.

2. **Official Comm. v. Walker Cty. Hosp. Dist. (In re Walker Cty. Hosp. Corp.), 3 F.4th 230, 231-32 (5th Cir. 2021).**

**This case offers another cautionary tale that an objecting party must seek a stay immediately upon deciding it will appeal a sale order.** In this case, a small rural hospital filed for chapter 11 bankruptcy and had hopes to sell a number of its assets. After a long search, it settled on a stalking horse bidder. However, the committee was not as supportive. Eventually, the Debtor, buyers, and committee reached a consensus on the sale and a sale order was entered. Over the course of the following due diligence period, issues arose that put the sale in jeopardy. At the same time, the buyers had financed some of the Debtor's operations to keep the hospital running. Eventually, Debtor filed an emergency motion seeking to amend the original sale order. The change substantively effected the amount available to unsecured creditors. The Debtors asked for the approval on an emergency basis and for the court to waive the 14-day stay. While the Committee received the Motion and apparently called the court to indicate it objected to the sale order, no objection was filed and the motion was granted the following day. This order indicated that an objecting party would need to pursue an appeal and stay within the closing window. The sale closed within 24-hours of the order. The Committee appealed, arguing that their procedural due process rights had been violated and that the sale did not follow with the bankruptcy rules. The Fifth Circuit spoke to the importance of finality in bankruptcy sales. Under Rule 363(m), a reversal or modification of an authorization to sell does not affect the validity of a sale or lease to a good faith purchaser, unless the authorization was stayed pending appeal. The Fifth Circuit enforced this provision, highlighting the unyielding aspects of a bankruptcy sale. The Committee had not sought a stay pending appeal and, therefore, any appeal would not affect the validity of the sale.

3. ***In re* Developers, Civil Action No. 1:20-cv-3491-RWS, 2021 WL 4516367, 2021 U.S. Dist. LEXIS 193398 (N.D. Ga. Sep. 30, 2021)**

**Insiders lending money to the debtor will not be granted administrative expense**

**priority status when the money was loaned without pre-approval from the bankruptcy court and the insider loan negatively effects non-insider creditors.** This case was on appeal to the district court following the bankruptcy court's denial of *nunc pro tunc* approval of administrative expense status for a postpetition loan to the debtor. The debtor in this case had sold a property but retained an option to repurchase, which ripened in 2018. The debtor did not possess the requisite cash on hand to repurchase the property, so debtor took on a loan from a company whose directors were all insiders of the debtor and another company without approval from the bankruptcy court. The bankruptcy court only learned of the repurchase of the property with these loans because it was mentioned in another pleading. The insider-lender moved for *nunc pro tunc* approval of the postpetition financing and treatment as an administrative expense, which the bankruptcy court denied. On appeal, the district court upheld the bankruptcy court's analysis in full. As allowance of the administrative expense priority for the insider's claim would have been a detriment to the estate and the claims of other "true" creditors, the bankruptcy court correctly denied classification of the debt as an administrative priority claim.

4. **Brock v. Cohen *(In re* Richard D. Van Lunen Charitable Trust), Civil Action No. 21-cv-1727-LTB, 2022 WL 1261453, 2022 U.S. Dist. LEXIS 78419 (D. Colo. Apr. 18, 2022)**

**Mere denial of receipt of the bar date notice does not rebut the mailbox rule and failure to timely file a final application for compensation lead to fee disgorgement.** This case was on appeal to the district court after the law firm plaintiff appealed the bankruptcy court's order of disgorgement of fees for failure to file their final application for compensation by the bar date. The question on appeal was whether the firm received adequate notice of the final claims bar date and whether disgorgement was too severe a punishment for failure to timely file its application for compensation. The firm argued that the bankruptcy court improperly applied the mailbox rule presumption that mailed documents were received and had abused its discretion in ordering fee disgorgement. The firm provided an affidavit saying that they did not receive notice of the bar date, despite it being mailed to the correct address as reflected on the filed certificate of service. The district court held that mere denial of receipt of a document does not rebut the presumption of delivery. Such a holding would defeat the purpose of deadlines and notice in the bankruptcy system. Thus, the firm was aware of the bar date and failed to file for compensation in time. Further, fee disgorgement was appropriate because ignorance of the fee application process is not grounds to support a four-month late application for compensation. The firm signed and submitted interim applications for compensation and the court held that they should have known that their full fee had not received final approval.

### C. Confirmation, Absolute Priority

**1. *In re* Walker, 628 B.R. 9 (Bankr. E.D. Penn. 2021)**

**Maintaining a luxurious lifestyle is permissible so long as debtor's proposed plan does not violate the requirements of the Code.** *See* Richard Levin, *Recent Developments in Bankruptcy Law July 2021,* 2 (2021).

**2. Jackson v. Le Ctr. on Fourth, LLC (In re Le Ctr. on Fourth, LLC), 17 F.4th 1326 (11th Cir. 2021)**

**Actual notice of the plan is sufficient to satisfy due process.** *See* Richard Levin*, Recent Developments in Bankruptcy Law January 2022*, 6 (2022).

### D. Dischargeability

***1. Cantwell-Cleary Co. v. Cleary Packaging, LLC (In re Cleary Packaging, LLC), No. 21-1981, 2022 U.S. App. LEXIS 15627 (4th Cir. June 7, 2022).***

**In a subchapter V case, a nonconsensual plan of reorganization cannot discharge the debts listed in § 523(a)(1) irrespective of whether debtor is an individual or corporation.** *See* Richard Levin*, Recent Developments in Bankruptcy Law October 2021*, 6 (2021).

***2. In re Nat'l Tractor Parts, Inc., No. 20 B 20833, 2022 WL 2070923, ___ B.R. ___ (Bankr. N.D. Ill. June 6, 2022)***

**A debtor can modify a consenually confirmed plan post confirmation before substantial consummation of the plan; but for the purposes of substantial consummation, commencement of distribution means even a de minimis distribution.** In this case, Debtor's subchapter V plan was confirmed and the class of unsecured creditors to receive distribution included the SBA. Post confirmation, Debtor learned of a loan program with the SBA that was available only if Debtor amended the SBA's treatment under the plan. Debtor sought to amend the confirmed plan under § 1193(b), which is permissible only before substantial consummation. Debtor and the U.S. Trustee agreed that the first two elements of substantial consummation under

§ 1101(2), transfer of substantially all of the property proposed by the plan to be transferred and assumption by the debtor of the business or of the management, had already occurred. However, Debtor and the U.S. Trustee disagreed on whether the last element, commencement of distribution, had occurred. Debtor argued that some classes had not yet received any funds and those that had received a distribution received a de minimis amount only. Basing its decision on the plan language of §1101(2), the court disagreed with the Eastern District of North Carolina's interpretation in *In re Dean Hardwoods, Inc.*, 431 B.R. 387 (Bankr. E.D.N.C. 2010)(commencement of distribution requires commencement to all or substantially all creditors) and decided that commencement of distribution means making "any payment to any creditor."

## E. Third Party Releases

### 1. *In re* Purdue Pharma, L.P., 635 B.R. 26 (S.D.N.Y. 2021)

**Bankruptcy courts lack authority to approve non-consensual third-party releases for liabilities associated with debtor's business operations.** *See* Richard Levin*, Recent Developments in Bankruptcy Law January 2022*, 4-5 (2022).

### 2. Patterson v. Mahwah Bergen Retail Grp., Inc., 636 B.R. 641 (E.D. Va. 2022)

**Bankruptcy courts cannot grant releases to non-debtor parties without the knowing and voluntary consent of the releasing parties.** *See* Richard Levin*, Recent Developments in Bankruptcy Law January 2022*, 7 (2022).

### 3. *In re* Mallinckrodt PLC, No. 20-12522 (JTD), 2022 WL 404323 (Bankr. D. Del. Feb. 8, 2022)

**Bankruptcy courts may issue non-consensual third-party releases that are integral to the plan's success in extraordinary cases.** *See* Richard Levin*, Recent Developments in Bankruptcy Law April 2022*, 6 (2022).

### 4. McAdams v. Robinson, 26 F.4th 149 (4th Cir. 2022)

**United States Magistrate Judge had authority to enter final judgment in class action suit. Non-named class members were not parties required to consent to the constitutional authority of the Article I judge to enter final judgment, and ample notice and ability to opt**

**out satisfied constitutional due process and authority concerns.** Class plaintiffs alleged that Nationstar Mortgage LLC ("Nationstar") violated consumer protection laws while servicing mortgage loans. An absent class member (i.e. a class member who was not named as a party to the lawsuit) objected to the settlement, arguing insufficient notice, unfair settlement, lack of consent to entry of final judgment by magistrate judge, and unconstitutionally overbroad release. A magistrate judge, acting on referral from the district court, overruled the objections, approved the settlement, and entered final judgment.

The Fourth Circuit recognized that a magistrate judge could not enter final judgment without the consent of the parties. The objecting absent class member argued that even absent class members constituted parties where the releases affected claims held by them. The Fourth Circuit observed that every other circuit to address this issue has concluded that absent class members are no parties for purposes of consent under 28 U.S.C. § 636(c), *id.* at 155-56 (citing *Koby v. ARS Nat'l Servs., Inc.*, 846 F.3d 1071, 1076 (9th Cir. 2017); *Day v. Persels & Assocs., LLC*, 729 F.3d 1309, 1316 (11th Cir. 2013); *Dewey v. Volkswagen Aktiengesellschaft*, 681 F.3d 170, 181 (3d Cir. 2012); *Williams v. Gen. Elec. Cap. Auto Lease, Inc.*, 159 F.3d 266, 269 (7th Cir. 1998), and joined the other circuits in this conclusion. In so holding, the court observed:

> Interpreting "parties" to include absent class members would prevent magistrate judges from entering judgment against absent class members who haven't given their explicit consent. That reading "would virtually eliminate § 636(c) referrals to magistrate judges" by hindering the judgment's preclusive effect.

*Id.* at 156 (quoting *Williams*, 159 F.3d at 269).

The court next considered the constitutional and procedural due process issues. The magistrate judge observed that the distribution of the class notice:

> was sufficient because over 97% of the nearly 350,000 class members received notice. He also found that class members "had information to make the necessary decisions and ... the ability to even get more information if they so desired. [citation omitted]. In support of that finding, the judge noted the low number of objectors (2), the low opt-out rate (.04%), and the high claims rate (13.8%).

*Id.* at 154. The magistrate judge approved three types of notice under Fed. R. Civ. P. 23, email, postcard, and longform, each of which permitted absent class members to opt out of the class, and

therefore the effect of the judgment and the releases. Only the longform explained the settlement in detail. The court held this was sufficient notice and consent to satisfy due process by absent class members.

## F. Dismissal

### 1. *In re Aronowitz Delaware 2 Family Limited Partnership, No. 21-50464, 2021 WL 4823520 (M.D.N.C. 2021)*

**When property is exclusively used for personal purposes and there are no business activities, there is no going concern and reorganization is objectively futile.** The Debtor was a limited partnership. Debtor's only asset was Banner Elk, North Carolina (the "Property"). The Property was used by Aronowitz as a summer home and vacation home for his family. The Property had never had any material business operations nor was it used for business purposes such as generating income. Disputes arose between the Aronowitz and another business entity that held a Note secured by a Deed of Trust on the property. The business entity commenced foreclosure proceedings, and Debtor filed the case during the last day in the upset bid period. The business entity moved for the court to dismiss or convert the case under § 1112(b).

Under § 1112(b)(1), absent limited exceptions, "'the court shall convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause . . .,' unless the court determines that appointment of a chapter 11 trustee is in the best interest of either creditors or the estate." The burden is on the movant to prove cause by a preponderance of the evidence. Section 1112(b)(4) provides a non-exhaustive list of examples that qualify as cause, but any single example would suffice. The Fourth Circuit has found that filing in bad faith is also cause to dismiss or convert the case. To dismiss a case for cause due to an absence of good faith in filing, a court must find both objective futility and subjective bad faith. Objective futility asks whether there is any going concern to preserve and whether there is hope of rehabilitation. While similar to objective futility, subjective bad faith asks whether the petitioner's real motivation is "to abuse the reorganization process" and "to . . . delay creditors . . . without an intent or ability to reorganize the debtor's financial affairs." In distinguishing why liquidation plans are not per se objectively futile, the court pointed out that rehabilitation and reorganization are not interchangeable. Liquidation plans focus on maximizing the value of a going concern. The court found that there was no going concern for which a liquidation plan could maximize. In addition, there was no hope of rehabilitating a business since there was no business to rehabilitate. The evidence demonstrated that the Property was used solely

for the personal use of Aronowitz and his family members. The Debtor conceded that the purpose of filing was to invoke the automatic stay to delay foreclosure with the hopes of prevailing in the New York litigation. The case represented nothing more than a state court dispute that attempted to use the automatic stay as a litigation tactic. The court determined that the case was filed with objective futility and subjective bad faith, and cause existed to dismiss or convert.

## XII. Chapter 13 Issues

### A. Property of the Estate

#### 1. TitleMax of Alabama, Inc. v. Hambright (*In re* Hambright), 635 B.R. 614 (Bankr. N.D. Ala. 2022)

**Under Alabama law, debtor retained an interest in a vehicle subject to title loan.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 12 (2022).

#### 2. TitleMax of Georgia, Inc. v. Snyder (*In re* Snyder), 635 B.R. 901 (Bankr. S.D. Ga. 2022)

**Under Georgia law, failure to redeem pawned property within the extended grace period results in an inability to modify the unredeemed title pawn contract in a chapter 13 plan.** Debtor entered into a 30-day pawn transaction, which extended her existing title pawn balance into a new contract. Prior to the maturity date of the new transaction, debtor filed her petition for relief under chapter 13. Debtor scheduled the vehicle as an asset and the title lender as a secured creditor. The title lender moved for stay relief, citing existing Eleventh Circuit precedent in *TitleMax v. Northington (In re Northington)*, 876 F.3d 1302 (11th Cir. 2017) for the proposition that the vehicle ceased being property of the estate once debtor failed to pay the debt in full by the end of the extended grace period. Analyzing Georgia's pawn law, the court found that pawn transactions, including for automobiles, are for 30-day periods, subject to extension for another 30 days, and failure to redeem the pawned property within the extended grace period results in the pawned vehicle not becoming property of the chapter 13 estate. Thus, the unredeemed title pawn contract could not be modified in a plan as a secured claim. The opinion analyzes Eleventh Circuit authority and the effect of § 541(b)(8).

### B. Debtor's Attorneys

#### 1. Smith v. Meredith (*In re* Smith), 637 B.R. 758 (Bankr. S.D. Ga. 2022)

***Nunc pro tunc* employment of personal injury attorney disallowed and fees disgorged where no showing of excusable neglect was made.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 15 (2022).

2. ***In re* Deighan Law, LLC, 637 B.R. 888 (Bankr. M.D. Ala. 2022)**

**National bankruptcy law firm engaged in the unlawful practice of law.** *See* William Houston Brown, *Consumer Law Update, Selected Cases Reported January 1 to March 31, 2022*, 16-17 (2022).

### C. Plans

1. ***In re* Mercer, No. BR 18-11913 EEB, 2022 WL 1836325, 2022 Bankr. LEXIS 1592 (Bankr. D. Colo. June 2, 2022)**

**Motions to modify confirmed chapter 13 plans to extend the term under CARES are effective when granted by the court, not when filed.** The CARES Act amended § 1329 to permit debtors impacted by the pandemic to propose up to a seven-year plan term. The amendment was originally slated to sunset in 2021 but was extended another year by the Consolidated Appropriations Act of 2021 and sunset on March 27, 2022. Debtors moved to modify their confirmed chapter 13 plans to exceed 60 months prior to the sunset date but did not obtain court approval of the modifications prior to the sunset date. There was no opposition to the motions. While active, amended § 1329(d) specified approval of the plan modification as an element. The court concluded this language was intended to render motions to modify effective only after they are approved, rather than when they are filed—a departure from § 1329(b)(2), which specifies that a modified plan "becomes the plan unless, after notice and a hearing, such modification is disapproved." In one of the cases before the court, debtors had previously obtained approval of a longer plan term prior to the sunset date. In another case, the court had approved a seven-year term with the initial modification, but debtors sought to adjust the payment amount while maintaining the term. The court concluded that: 1) the initial modification beyond 60 months previously approved should remain in effect but denied the motion to extend the term further; and 2) the seven-year term could remain in effect and the motion to modify the plan payment could be approved.

2. ***In re* Bohinski, No. 16-47598, 2022 WL 1435605, 2022 Bankr. LEXIS 1121 (Bankr. E.D. Mich. Apr. 25, 2022)**

**Approval of a modification extending a chapter 13 plan's term beyond 60 months impermissible after the sunset date of the CARES act, even though the motion to modify was filed prior to its expiration.** *See* William Houston Brown, *Consumer Law Update, Selected Cases*

*Reported April 1 to June 30, 2022*, 12 (2022).

## XIII. Chapter 15 Issues

### A. *In* re Talal Qais Abdulmunem Al Zawawi, 634 B.R. 11 (Bankr. M.D. Fla. 2021)

**A foreign debtor seeking Chapter 15 recognition need not meet the eligibility requirements for debtors under § 109(a).** *See* Richard Levin, *Recent Developments in Bankruptcy Law April 2022*, 13 (2022).

# CONSUMER LAW UPDATE

**Cases reported from July 1, 2021 through September 15, 2021**

**Prepared for Federal Judicial Center**

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**Appeals**

**Dismissal of Chapter 13 case rendered appeal moot.** The First Circuit held that debtor's appeal of order granting mortgage lender's motion for release of insurance proceeds was moot, because the voluntary dismissal of the Chapter 13 case triggered jurisdictional mootness. The trustee had released insurance-loss proceeds to the secured lender prior to the case dismissal, and the "revesting function of section 349 cannot reach out to grasp funds already distributed prior to the dismissal of a chapter 13 case." In re Sundaram, ___ F.4th ___, 2021 WL 3578339 (1st Cir. Aug 13, 2021). See also *In re Hazan,* ___ F.4th ___, 2021 WL 3907781 (11th Cir. Sept. 1, 2021) (In Chapter 11 case, equitable mootness barred mortgagee's appeal.).

**Automatic Stay**

**University's refusal to provide transcript was willful stay violation.** The Third Circuit considered its precedent, *In re University Medical Center,* 973 F.2d 1065 (3d Cir. 1992), concluding that it remained good law, notwithstanding subsequent amendment to § 362(k)**,** but California Coast University did not establish a willfulness defense under *University Medical Center.* California Coast had refused to provide a complete certified transcript to the former student, and the bankruptcy court found its refusal to be willful stay violation. Section 362(k)(2)'s good-faith defense to damages was held to be separate and distinct from the willfulness defense found in *University Medical Center,* but there is no conflict in the two defenses. This defendant did not argue good faith and failed to establish the willfulness defense, and the award of damages and attorney fees for the stay violation was affirmed. In re Aleckna, ___ F.4th ___, 2021 WL 4097155 (3d Cir. 2021).

**Avoidance**

**Insurance proceeds for fire damage to home not included in § 522(f) valuation.** The Eighth Circuit determined in valuation of the debtor's homestead, for purposes of judicial lien avoidance, that the appraised value of the damaged property as of the petition date was appropriate, and that the fire-loss insurance proceeds would not be included in that valuation. Applying the § 522(f)(2)(A) formula, the judicial lien impaired the exemption

and the lien was entirely avoidable. In re Sawyers, 2 F.4th 1133 (8th Cir. 2021). For other applications of § 522(f) avoidance, see In re Badalmenti, ___ B.R. ___, 2021 WL 3028186 (Bankr. M.D. Fla. July 15, 2021) (The Chapter 7 debtor could avoid a judgment lien under § 522(f), even though the lien attached during a period when the debtor was not residing in the subject home. The home was the debtor's residence when the Chapter 7 was filed, and the lien impaired exemption to which the debtor was entitled at that time.); In re Minkina, ___ B.R. ___, 2021 WL 3195806 (Bankr. D. Mass. July 28, 2021) (Application of § 522(f)(1)(A) in valuation of debtor's interest in tenancy by entirety property, with lien impairing exemption in debtor's interest.).

**Lis pendens filing date triggers avoidance periods.** Chapter 13 debtor filed avoidance complaint, alleging tax foreclosure judgment was either preference or fraudulent transfer, but the pre-judgment lis pendens filing was the date of transfer for purposes of both §§ 547 and 548. The lis pendens was filed outside of the relevant look-back periods, preventing the debtor's avoidance action. In re Azeglio, ___ B.R. ___, 2021 WL 3141279 (Bankr. D. N.J. July 23, 2021).

**Exemptions and Property of Estate**

**Meaning of "applicable nonbankruptcy law" in § 522(b)(3)(B).** the Chapter 7 debtor lived in Chicago but claimed exemption under § 522(b)(3)(B) in a Michigan condominium that was owned by debtor and spouse as tenants by entirety. The trustee objected, asserting that the debtor was resident of Illinois and could not claim exemption under Michigan law. Section 522(b)(3)(B)'s use of the term "applicable nonbankruptcy law" refers in this case to the law of Michigan, where the condominium is located, and Michigan did not limit its exemption for entireties property to homestead property. The Court concluded that "the better reading of section 522(b)(3) is that 'applicable nonbankruptcy law' has nothing to do with the debtor's domicile state;" rather, the applicable law is where the property is located. The Court found that most courts had so construed the statute. Illinois, the debtor's domicile state, had opted out of the § 522(b)(2) federal exemptions, permitting the debtor to choose § 522(b)(3) exemptions, including the § 522(b)(3)(B) tenancy by entirety exemption. The trustee's objection was overruled. In re Wheatley, ___ B.R. ___, 2021 WL 3214441 (Bankr. N.D. Ill. July 29, 2021).

**Workers' compensation payments were exempt under § 522(d)(10)(C).** Although the postpetition payments from workers' compensation benefits were property of the estate, those payments were disability, illness or unemployment benefits for purposes of § 522(d)(10)(C)'s exemption. The contingency fee paid to debtor's counsel in the workers' compensation settlement was also covered by the exemption, because it was a part of the workers' compensation claim rather than a separate, independent payment. In re Buffenmeyer, 629 B.R. 372 (Bankr. E.D. Pa. 2021).

**Allocation of income tax refund for property of estate.** The Chapter 7 case was filed in December, 2020, and prior to filing the debtor and non-debtor spouse filed their joint 2018 income tax return, showing a refund. The IRS sent the refund check to the trustee, and the parties disputed how the refund should be allocated between the non-filing spouse and estate. Reviewing the four primary approaches to allocation, found in *In re McInerney,* 609 B.R. 497 (Bankr. N.D. Ill. 2019), the Court adopted the "withholding rule," under which the refund is allocated between spouses in proportion to their respective tax withholdings for the relevant tax year. Here, during the 2018 tax year, all income was earned by the debtor and none by the non-filing spouse; therefore, the entire refund was attributed to the debtor's earnings and withholdings, and the refund was property of the estate. In re Culp, ___ B.R. ___, 2021 WL 3232569 (Bankr. E.D. Mich. July 29, 2021).

**Discharge**

**General default in state court action was not entitled to collateral estoppel effect.** The pre-bankruptcy Florida state court judgment was based on default in a multi-count complaint, and that judgment was not given collateral estoppel effect in the subsequent § 523(a)(2)(A) proceeding. In the Florida complaint, "each of the claims that could have satisfied the requirements of § 523(a)(2)(A) contained alternate factual allegations that did not do so. . . .In our view, when a complaint alleges several alternative (and inconsistent) factual grounds for a legal claim, and each of those grounds would be independently sufficient to establish the claim, it is impossible to tell which of the grounds a general default judgment was based on. And if one of those alternate grounds is insufficient to meet the elements of fraud under the Bankruptcy Code, the issues cannot be deemed identical." In re Harris, 3 F.4th 1339 (11th Cir. 2021). Compare In re

Adesanya, ___ B.R. ___, 2021 WL 2948433 (Bankr. E.D. Pa. July 14, 2021) (Federal district court judgment entitled to issue preclusive effect on § 523(a)(2)(B) claim.).

**Pro se plaintiff who failed to state claim under § 523(a)(2)(A) or a community property exception from discharge should have been given leave to amend.** The pro se creditor's complaint did not state a claim for exception from discharge under § 523(a)(2)(A) and the complaint did not allege that the debt was a community debt for purposes of § 524(a)(3). The opinion discusses the community property discharge provision in § 524(a)(3) and its exception when the community property ceases to exist. The complaint had been dismissed, but the pro se plaintiff should have been given leave to amend the complaint, with the concurring opinion urging the parties to obtain counsel. In re Lockhart-Johnson, ___ B.R. ___, 2021 WL 3186115 (B.A.P. 9th Cir. July 28, 2021).

**Distribution approach adopted for purposes of § 523(a)(3)(A).** In the Chapter 7 case, the original schedules did not list this creditor and there was no original proof of claim deadline, but subsequently a proof of claim deadline was issued.. After the debtors' discharge, an amendment to Schedule F was filed, listing this creditor who had obtained a prepetition judgment. The creditor filed a proof of claim, well past the deadline, but also a complaint under § 523(a)(3)(A), alleging that the claim was not scheduled for a year after the deadline to file a timely proof of claim, but the debtors responded that the estate was still open, pending recovery of assets, and that the proof of claim was filed in time for a distribution, if available. The issue was whether § 523(a)(3)(A) should be read in conjunction with § 726(a)(2)(C), and the Court adopted the distribution approach, following *In re Snyder,* 544 B.R. 905, 910 (Bankr. M.D. Fla. 2016), that the "determinative factor on timeliness must be whether the creditor filed a proof of claim in time to share in the distribution." Even though this proof of claim was tardy, it was filed in time to share in the distribution from this estate if assets were recovered. The timeliness requirement was satisfied for purposes of § 523(a)(3)(A), when read in conjunction with § 727(a)(2)(C). The debt was not excepted from discharge. In re Simmons, ___ B.R. ___, 2021 WL 3744890 (Bankr. M.D. Fla. Aug. 24, 2021).

**Attorney fees awarded in divorce proceeding were domestic support obligations.** Substantial attorney fees awarded by the divorce court to debtor's former spouse were clearly intended to be support and were nondischargeable under § 523(a)(5). The fees

were also entitled to priority under § 507(a)(1)(A). The debtor's argument that the fees were dischargeable under § 523(a)(15)'s pre-2005 balancing test was irrelevant, but if the fees were not domestic support in nature they would be nondischargeable under the current "catchall section 523(a)(15) for all other debts owed to a spouse incurred in the course of a divorce." In re Kalsi, ___ B.R. ___, 2021 WL 3922939 (Bankr. S.D. N.Y. Sept. 2, 2021).

**Bar fight injury was willful and malicious.** Affirming, the Bankruptcy Appellate Panel held that the injuries to a bar patron resulting from the debtor's instigation of a fight were willful, and the debtor's conduct was malicious. The opinion discusses the two prongs of § 523(a)(6). In re Judge, 630 B.R. 338 (B.A.P. 10th Cir. 2021).

**Private educational loan was not covered by § 523(a)(8)(A)(ii).** The Second Circuit held that the "direct-to-consumer Tuition Answer Loans" at issue were not excepted from the Chapter 7 discharge because they were not "an obligation to repay funds received as an educational benefit, scholarship, or stipend" under § 523(a)(8)(A)(ii). The other subsections of § 523(a)(8) were not at issue. Agreeing with the Tenth and Fifth Circuits, the Court construed the subsection's language to include "educational benefits. . .such as conditional grants," but not to include typical "loans." "'Educational benefit' is therefore best read to refer to conditional grant payments similar to scholarships and stipends," such as payments of tuition in exchange for the student's "promise to serve in the military after graduation or to practice medicine in an underserved region." In considering what Congress meant when it created § 523(a)(8)(A)(ii) in 2005, the opinion notes that "Congress used the word 'loan' several times in § 523(a)(8) but left it out of § 523(a)(8)(A)(ii), signaling that the omission was intentional." Homaidan v. Sallie Mae, Inc., et al., 3 F.4th 595 (2d Cir. 2021).

**Partial discharge of student loan debt.** Finding that it would be unreasonable for the 68-year old debtor "to further eliminate expenses or commit to working excessive overtime hours," the debtor had established it would be an undue hardship to pay the entire $190,000 student loan debt under the *Brunner* test. However, the debtor had ability to pay $12,000 of that debt over a ten-year period, accruing interest at the federal judgment rate. The Court agreed with those courts concluding that partial discharge was permissible, including *In re Alderete,* 412 F.3d 1200 (10th Cir. 2005), and *In re Clavell,*

611 B.R. 504 (Bankr. S.D. N.Y. 2020), and others cited at footnote 23. In re Randall, 628 B.R. 772 (Bankr. D. Maryland 2021).

**Pension benefit obtained by former spouse in violation of divorce decree was § 523(a)(15) debt.** The former (now deceased) spouse of the debtor had been awarded in the divorce decree all proceeds of his pension benefits, but upon his death, the debtor received those pension funds, and the decedent's estate sued for recovery and for exception from discharge. The Court held that the decedent's estate had standing to pursue the discharge action, because Rule 4007(a) gives "any creditor" standing, and the estate was a creditor. Further, the debt was incurred during the divorce proceeding and in connection with the divorce decree; therefore, it was a debt covered by § 523(a)(15), excepted from discharge in this Chapter 7 case. In re Jones-Peteet, 630 B.R. 61 (Bankr. S.D. Tex. 2021). See also In re Hunsucker, ___ B.R. ___, 2021 WL 3379352 (Bankr. N.D. Miss. Aug. 3, 2021) (Property settlement claim resulting from divorce was § 523(a)(15) debt, which is not an exception from discharge in Chapter 13 case.).

**Discharge Injunction**

**Jurisdiction in putative class action to consider violations of other courts' discharge orders.** Denying Discover Bank's motion to dismiss class action allegations based on the Court's lack of jurisdiction to consider alleged violations of the discharge orders entered by other bankruptcy courts, the Court did not rule on certification of a class, but rejected the argument that it would lack jurisdiction to consider the effects of discharge orders from other bankruptcy courts. The opinion reviews other relevant decisions, noting that the discharge injunction is statutory under § 524(a), with the discharge order generally accomplished by an Official Form. The Court recognized that the Fifth Circuit, in *In re Crocker*, 941 F.3d 206 (5th Cir. 2019), had held that "only the bankruptcy court issuing the discharge has authority to enforce the discharge injunction by contempt," but this Court concluded that it had jurisdiction because the claims at issue "arise under" the Bankruptcy Code. In re Golden, ___ B.R. ___, 2021 WL 3051896 (Bankr. E.D. N.Y. July 19, 2021).

**Reopening case denied when issue was alleged creditor's erroneous credit reporting.** The Chapter 7 debtor moved to reopen case to hold credit union in contempt

for violation of discharge injunction by its erroneous reporting that debt was charged off rather than discharged. Although erroneous credit reporting may be an attempt to coerce payment of discharged debt, under the circumstances, this credit union's reporting was not an act to collect the debt. The motion to reopen was denied as futile, because the debtor could not prevail on the contempt motion. In re Minech, ___ B.R. ___, 2021 WL 4071875 (Bankr. W.D. Pa. Sept. 7, 2021).

**Chapter 7 Issues**

**Dismissal**

**Debtor's motion to dismiss under § 707(a).** Although Chapter 7 debtor did not have absolute right to dismiss the case, the debtor had resolved one creditor's claim, leaving only a two-party dispute with a secured creditor on real property that the trustee had not begun to liquidate, and the debtor had agreed to pay the trustee's costs and legal fees incurred in the case as a condition of dismissal. Continuing litigation in the bankruptcy court would consume any equity in the real property, and the debtor-secured creditor dispute may be resolved outside of the bankruptcy court. The Court found cause to dismiss the case. In re Holmes, ___ B.R. ___, 2021 WL 3834168 (Bankr. D. S.C. Aug. 3, 2021).

**Chapter 13 Issues**

**Trustee Fees**

**Trustee is entitled to statutory fee upon receipt of each plan payment.** In an unpublished opinion that takes the minority position, the Ninth Circuit Bankruptcy Appellate Panel, with a dissent, held that the plain language of 28 U.S.C. § 586(e)(2) provided that "a standing trustee is entitled to collect the statutory fee upon receipt of each payment under the plan and is not required to disgorge the fee if the case is dismissed prior to confirmation." The opinion acknowledges that the majority of bankruptcy courts confronting the issue have held that § 586(e) in conjunction with § 1326(a)(2) require the trustee to hold the percentage fee until confirmation and to return

it to the debtor if the case is dismissed prior to confirmation. "The plain language interpretation is confirmed by the context of § 586(e)(2), related fee collection statutes, and the larger statutory scheme of the Bankruptcy Code. And logic dictates that once the trustee collects her fee 'from' each payment she receives, the fee is no longer part of the plan payments which must be retained by the trustee under § 1326(a)(2) and disbursed to creditors pursuant to the plan." The dissenting opinion agreed that the majority opinion was the "better" policy outcome, but disagreed with the interpretative approach taken by the majority. In re Harmon, 2021 WL 3087744 (B.A.P. 9th Cir. July 20, 2021).

**Disposable Income**

**Contributions to 401(k).** Distinguishing the facts in its prior decision, *In re Davis,* 960 F.3d 346 (6th Cir. 2020), in which the debtor had historically and regularly made prepetition contributions to a 401(k), the Sixth Circuit considered the situation in which a Chapter 13 debtor had historically contributed to a 401(k) plan but had been unable to do so in the six months leading up to the bankruptcy filing. The Court of Appeals ruled that these debtors could not exclude postpetition voluntary contributions to their 401(k) plan from calculation of their projected disposable income. The opinion reviews the history of decisions on the issue, including the prior decision *In re Seafort,* 669 F.3d 662 (6th Cir. 2012). In re Penfound, 7 F.4th 527 (6th Cir. 2021),

**Confirmation**

**Pawn loans current at commencement can be paid in plan.** In an unpublished decision, the Eleventh Circuit recognized a limitation to its prior *In re Northington,* 876 F.3d 1302 (11th Cir. 2017), holding that when the debtor was not in default under a pawn contract at the time of filing the Chapter 13, she had not lost her interest in the pawned vehicle and Title Max held a secured claim subject to modification and payment through the plan. In contrast to the debtor in *Northington,* the Alabama state-law redemption period had not been triggered because this debtor was not in default at filing. In re Womack, ___ Fed.Appx ____, 2021 WL 3856036 (11th Cir. Aug. 30, 2021).

**Effect of confirmation on property of estate and appreciated value.** Holding that confirmation vested property in the debtor, the estate may be replenished after

confirmation by new property but appreciated value of property vested in the debtor does not become property of the estate. The case was filed under Chapter 7 but then converted to 13, and the confirmed plan provided for unsecured creditors to be paid pro rata, with a total of $36,015 to be paid into the plan. Three years later the debtor moved to sell the residence, and the sale price indicated an increase in value ($129,000) since commencement of the case. The debtor proposed to pay off the balance of the plan from sale proceeds, but the trustee objected, asking that unsecured creditors be paid in full from the appreciated value and arguing that the appreciation was property of the estate. The opinion reviews the theories of vesting at confirmation, concluding that the "estate replenishment approach best harmonizes sections 1306(a) and 1327(b). . . .To allow the trustee to reach the asset that has vested in the debtor renders section 1327(c) moot." The Court then held that vesting of this property in the debtor caused that property to cease being property of the estate; therefore, proceeds of sale of that property did not become property of the estate. Its appreciated value did not accrue from property of the estate, and was vested in the debtor. If the debtor wishes to pay off the plan early, rather than continue confirmed monthly plan payments, the debtor must move to modify the plan. In re Larzelere, ___ B.R. ___, 2021 WL 3745428 (Bankr. D. N.J. Aug. 24, 2021).

**910 Car claim.** Affirming, the District Court held that a 910-claim is not subject to valuation process under § 506, because of the "hanging paragraph" in § 1322(a)(9). The creditor's purchase-money security interest also attached to the attorney fees provided for in the contract. Also, a plain reading of the confirmed plan provided that the actual amount of the creditor's claim could be determined post-confirmation when the creditor's claim was allowed, and the debtor was required to pay that claim in full. In re Laney, ___ B.R. ___, 2021 WL 4147994 (S.D. Ill. Sept. 13, 2021).

**Plan Modification**

**Modified plan could include postpetition mortgage arrearages.** Reviewing split of authority on whether a modified plan could include curing of postpetition mortgage arrearages, the Court agreed with Fifth and Eleventh Circuit decisions that such curing was permissible under §§ 1322, 1325 and 1329. The analysis included that a plain reading of § 1322(b)(5) expressly authorizes a timely cure of default whether it is pre- or

postpetition. The debtor had defaulted on postpetition mortgage payments because of her spouse's unemployment and COVID-19 impacts; as a result, the confirmed plan could be extended to 73 months to permit the cure, with the extension permitted under § 1329(d)(2). In re Smith, ___ WL 2628823 (Bankr. D. N.J. June 24, 2021).

**Best interest of creditors test in modification.** The Bankruptcy Judges in Kansas agreed on a holding that a postpetition personal injury settlement acquired by the debtor was not included in the calculation of the best interest of creditors test. The trustee had moved for inclusion of the settlement proceeds for payment of unsecured claims. The Court held that the proceeds were property of the estate under §§ 541 and 1306, and the opinion reviews the split of authority on whether postpetition property is included in the § 1325(a)(4) hypothetical liquidation analysis. The Court interpreted that Code section's "effective date of the plan" to refer to the original plan rather than the modified plan, following the leading case, *In re Barbosa,* 235 F.3d 31 (1st Cir. 2000), on that point, but § 348(f) controlled what property would be included in the hypothetical Chapter 7 liquidation. Assuming good faith, § 348(f) provides that property upon conversion is that property of the estate as of the filing of the petition if that property remains in the possession or control of the debtor, excluding § 1306 postpetition property. "The hypothetical liquidation calculated under the best interest test should be conducted assuming the same estate. That liquidation is determined by reference to what a Chapter 7 trustee would produce for unsecured creditors if the estate were liquidated at the time of the postconfirmation modification." The opinion observes that the majority view appears to be that postpetition windfall property is included in the best interest calculation, but the Court disagreed with that view. In re Taylor, ____ B.R. ____, 2021 WL 3118824 (Bankr. D. Kan. July 21, 2021).

**Rule 3002.1, Punitive Damages and Contempt**

**Punitive damages not allowed under Rule 3002.1** The Second Circuit Court of Appeals vacated a bankruptcy court's contempt and sanctions ruling, concluding that, even if PHH Mortgage Corp. improperly disclosed mortgage-related fees, such a violation of Rule 3002.1 could not "form the basis for contempt," in light of *Taggart v. Lorenzen*, 139 S. Ct. 1795 (2019), because "there is fair ground of doubt" as to whether its conduct

was expressly barred. The opinion did not make a distinction between *Taggart*'s discharge injunction context and this case's context of violation of the bankruptcy court's order that the mortgage was current. The majority panel went on to rule, in a matter of first impression among the circuits, that Rule 3002.1 does not authorize an award of punitive sanctions. There is a strong dissent, and a motion for en banc review is anticipated. PHH Mortgage Corp. v. Sensenich (In re Gravel), 6 F.4th 503 (2d Cir. 2021).

See also Newrez, LLC v. Beckhart*,* 2021 WL 3361707 (E.D.N.C. July 6, 2021), appeal filed, Beckhart v. Newrez, LLC (4th Cir. Aug. 2, 2021). The District Court rejected imposition of civil contempt sanctions for creditor's commencement of foreclosure in violation of a confirmation order. Sanctions had included monetary sanctions, lost wages, attorneys' fees and "loss of fresh start." A bankruptcy court has the power to hold someone in civil contempt and to impose sanctions; however, in light of evidence supporting "finding that appellants acted in good faith," the District Court reversed contempt finding.

**Discharge**

**Discharge could not be granted in case that exceeded 5 years.** The debtor failed to make some mortgage payments during the life of her 5-year plan, but she attempted to cure the default after the plan terminated and sought discharge. The Tenth Circuit affirmed the denial of request for discharge and dismissal of the case. The Circuit opinion viewed the attempted cure as an impermissible attempt to modify the plan, holding that plans were limited to five years and that modification could not be permitted after that term's expiration. The bankruptcy court had no discretion to grant a discharge when the debtor had not completed required payments during the plan term. The opinion concluded that § 1328(a)'s language "completion . . .of all payments under the plan" was ambiguous but nevertheless most naturally meant that a discharge is required only if payments "had been made during the existence of the plan." Congress "intended to strictly limit the time for payments under Chapter 13 plans." In re Kinney, 5 F.4th 1138 (10th Cir. 2021).

**Debtor with unpaid but "abated" plan payments not eligible for discharge.** After confirmation the debtor missed several plan payments, resulting in debtor's response to

trustee motions to dismiss with her motions to "abate" or suspend those missed payments. The debtor now moved for discharge under § 1328(a), contending that as a below-median debtor she had paid disposable income when it was available, while in some months no disposable income was available. The "abatement" of several scheduled plan payments did not eliminate that payments were required over a 36-month period. "While abatement allows a debtor to cure missed plan payments, it is not—at least as practiced in this Court—a formal modification of the plan pursuant to § 1329. Rather, abatement is the provision of a grace period in which a debtor may cure missed payments. Technically, when this Court grants a debtor's motion to abate missed payments, it is declining to dismiss the debtor's case for material default under § 1306(c)(6) so long as the debtor cures the missed payments within a reasonable period. The debtor's obligations under the plan, however, remain intact." The confirmed plan obligated this debtor to pay at least $300 monthly for at least three years, and the debtor must cure the missed payments before being eligible for plan-completion discharge. In re Nicksion, ___B.R. ___, 2021 WL 3855699 (Bankr. D. Kan. Aug. 11, 2021).

**Dismissal**

**Section 1307(b) dismissal is mandatory.** The Sixth Circuit held that § 1307(b) is clear in its mandatory "shall dismiss" language. Upon a Chapter 13 debtor's motion to dismiss the case, the bankruptcy court is required to dismiss. The Court noted that this right to dismiss is consistent with Chapter 13 providing only voluntary relief, and Congress had provided in section 1307(c) for circumstances in which the bankruptcy court "may" dismiss or convert a case. The opinion observed that the Fifth and Ninth Circuits had ruled that dismissal was not mandatory under section 1307(b), but those decisions predated *Law v. Siegel,* 571 U.S. 415 (2014), in which the Supreme Court rejected equitable authority as overruling clear statutory language. In re Smith*,* 999 F.3d 452 (6th Cir. 2021),

**Ninth Circuit agrees that § 1307(b) provides absolute right to dismiss.** Noting that its prior decision, *In re Rosson,* 545 F.3d 764 (9th Cir. 2008), "has been effectively overruled by *Law* and is no longer binding precedent in the Circuit," the Court now held that § 1307(b) is unambiguous and that the Chapter 13 debtors had an absolute right to dismiss, subject only to the single exception of a prior conversion. The Bankruptcy Code

provides “alternative tools for bankruptcy courts to address debtor misconduct.” In re Nichols, ___ F.4th ___, 2021 WL 3891571 (9th Cir. Sept. 1, 2021).

**Debtor’s voluntary dismissal did not shield against dismissal with prejudice.** The Ninth Circuit Bankruptcy Appellate Panel held that although the debtor had a right to dismiss under § 1307(b), dismissal did not provide “a get-out-of chapter-13-free card.” The opinion concluded that § 349(a) controlled all “roads to dismissal,” holding: “(1) every dismissal, including a § 1307(b) motion to dismiss, triggers the § 349(a) issue whether ‘cause’ exists to order that dismissal be with prejudice; (2) no particular procedure prescribes how or when to initiate a contest regarding § 349(a) ‘cause’ so long as there is due process notice appropriate for denial of discharge and a hearing; and (3) the proponent of a § 349(a) prejudice determination has the burden of persuasion.” Relying on the totality-of-circumstances factors in *In re Leavitt,* 171 F.3d 1219 (9th Cir. 1999), for application of § 349(a), the opinion provides a roadmap of the procedures, standards and burdens involved in dismissals with prejudice, and it identifies subsets of such dismissals, ranging from “weak form” to “strong form,” with the latter tantamount to denial of discharge under § 727. In re Duran, ___ B.R. ____, 2021 WL 3186117 (B.A.P. 9th Cir. July 27, 2021).

**Debtor’s Attorney**

**Fees benefitting Chapter 13 debtor allowed as administrative expense.** Attorney fees for representing the debtor in an adversary proceeding were objected to by the trustee, on the basis that the fees benefitted only the debtor and not the estate, but the Court held that Chapter 13 debtor’s attorney is entitled to allowance of fees under § 330(a)(4)(B) for work that is beneficial and necessary to the debtor and that proof of benefit or necessity to the estate or creditors is not required, assuming that the requested fees meet the reasonableness test. The requested fees were reasonable and allowed as administrative expense under § 503. In re Steen, ___ B.R. ___, 2021 WL 2877515 (Bankr. N.D. Tex. July 8, 2021).

**Disgorgement of unreasonable fees.** The U.S. Trustee moved for disgorgement of fees paid to Chapter 7 debtor’s attorney, on the basis that the attorney’s limited representation, failure to correct inaccuracies in the schedules, and other failures in

representation caused the fees to be unreasonable. Under § 329(b), the attorney has the burden to establish reasonableness, and the attorney put on no proof to support the fees. There was a lack of informed consent to the attorney's limited representation or advice as to the risk of filing Chapter 7 when real property at issue had substantial equity. Disgorgement was ordered. In re Mawson, 2021 WL 4073376 (Bankr. W.D. Mich. Sept. 7, 2021).

**Claims**

**Chapter 13 proof of claim deadline cannot be extended for excusable neglect.** Affirming, the First Circuit Bankruptcy Appellate Panel held that Rule 3002(c)'s deadline for timely filed proofs of claim could not be extended under Rule 9006(b) for excusable neglect, and even if such an extension were permissible, the illness of creditor's attorney was not a basis for finding excusable neglect under the facts in this case. In re Lopez, 629 B.R. 322 (B.A.P. 1st Cir. 2021).

# CONSUMER LAW UPDATE

**Selected Cases reported**
**September 15, 2021 – December 31, 2021**

**Prepared for Federal Judicial Center**
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United States Bankruptcy Judge, Retired
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**Appeal**

**Chapter 7 debtor lacked "person aggrieved" standing to appeal.** After a judicial foreclosure had been scheduled, the debtor filed Chapter 11 cases that were voluntarily dismissed, and after completion of sale the debtor filed a Chapter 13 that was converted to 7. The Chapter 7 trustee abandoned the debtor's purported interest in the foreclosed property, and the debtor appealed an order overruling his objection to the mortgage deficiency claim. The First Circuit affirmed the Bankruptcy Appellate Panel's dismissal of the appeal, holding that the Chapter 7 debtor did not establish appellate standing as a "person aggrieved." The challenged order had no direct or immediate impact on the debtor's pecuniary interest. In re Neira Rivera, 14 F.4th 60 (1st Cir. 2021). See also In re Levitt, 632 B.R. 527 (B.A.P. 8th Cir. 2021) (Chapter 7 debtors lacked standing as persons aggrieved to appeal trustee's fee.); In re Buscone, ___ B.R. ___, 2021 WL 6068131 (B.A.P. 1st Cir. Dec. 21, 2021) (Chapter 7 debtor lacked standing to appeal sanction against her attorney.); CitiMortgage, Inc. v. Davis, ___F.4th ___, 2021 WL 5856795 (7th Cir. Dec. 10, 2021) (Court of appeals lacked jurisdiction to review district court's affirmance of remand order.)

**Automatic Stay**

**Former spouse did not violate stay by seeking continuances and attending status conferences in state court litigation.** In prepetition action, the former spouse had sought state court order to require debtor's compliance with marital settlement agreement, and upon the Chapter 13 filing, the spouse continued the state court matter. Equating this type of continuance to postponement of a foreclosure sale, the Bankruptcy Appellate Panel declined to interpret § 362(a)(1)'s "continuation" of a judicial action to "include a 'continuance' or status hearing in a stayed nonbankruptcy proceeding." Such continuances in prepetition nonbankruptcy court matters are commonplace and do not constitute prosecution of the matter. In re Perryman, ___ B.R. ___, 2021 WL 4742673 (B.A.P. 9th Cir. Oct. 8, 2021 J. Brand). Compare In re Smith, 2021 WL 5441745 (Bankr. E.D. Tenn. Nov. 19, 2021 J. Whittenburg) (Former spouse's and attorney's continuation of civil contempt action in divorce court was a willful stay violation, and the non-support

debt was subject to discharge in the Chapter 13 case under § 523(a)(15).); see also In re Koeberer, 632 B.R. 680 (B.A.P. 9th Cir. 2021, J. Faris) (The Bankruptcy Appellate Panel held § 362(k) provides that a willful violation of the stay "shall" result in recovery of actual damages, including costs and attorney fees; therefore, notwithstanding the violation being "technical," it was error to not consider an award of attorney fees. The creditor had failed to withdraw its notice of trial of a fraudulent conveyance against the debtors individually, although it had advised the state court that a stay was in effect as a result of the debtor's Chapter 7 filing. Denial of attorney fees to the debtors was remanded.); In re Mellem, 2021 WL 5542226 (9th Cir. Nov. 26, 2021, per curiam) (Affirming its Bankruptcy Appellate Panel, probate court's determination that an advance had been made on the debtor's inheritance was not a stay violation because it was not a determination of personal liability of the debtor.).

**Failure to vacate garnishment did not violate stay.** Applying *City of Chicago v. Fulton,* the Bankruptcy Appellate Panel held that the creditor maintained the status quo and did not violate the stay under § 362(a)(3) when it refused to release a prepetition garnishment. The opinion also observes that the creditor did not violate other subsections of § 362(a). The creditor had asked the state court to stay further actions in the case but otherwise maintained the status quo. In re Stuart, 632 B.R. 531 (B.A.P. 9th Cir. Nov. 10, 2021 J. Faris). See also In re Cordova, ___ B.R. ___, 2021 WL 5774400 (Bankr. N.D. Ill. Dec. 6, 2021 J. Barnes) (In putative class action against City of Chicago, the City's motion to dismiss was denied in part, concluding that *Fulton* was limited to § 362(a)(3). The plaintiffs sufficiently stated claims for potential relief under §§ 362(a)(4), (6) and § 542(a). but the City was immune from punitive damages under § 106(a)(3).).

**Chapter 13 debtor's attorney sanctioned for failure to investigate before filing proceeding alleging stay violation.** After the Chapter 13 filing, a medical provider mailed an invoice for $910 to the debtor for prepetition services, and the debtor's attorney called to advise that bankruptcy had been filed. The provider noted the account as subject to bankruptcy but then in error sent a second invoice. Without contacting the provider again, the debtor's attorneys filed a complaint seeking damages for stay violation, and the provider served a motion for sanctions against

the attorneys under Rule 9011(c)(1)(A) for failure to conduct a reasonable investigation before suing. Although the complaint was filed for reasonable purpose of enforcing debtor's rights under the Code, the "prominent placement of a demand for $50,000 in actual and punitive damages on the front page of the complaint and extreme characterization of Defendant's conduct" was indicative of the attorneys' desire to "threaten and intimidate the Defendant by increasing the perceived financial risk to Defendant." Sanctions were appropriate under Rule 9011(b)(3), with the Court finding a failure of counsel to perform a reasonable investigation of the factual basis for the debtor's claim prior to filing the complaint. Appropriate sanction was $!0,000 reasonable attorney fees to the defendant creditor. In re Defeo, 632 B.R. 44 (Bankr. D. S.C. 2021 J. Waites).

**Lessor's postpetition action to terminate residential lease required stay relief.** At the time of Chapter 13 filing, the debtor was current on month-to-month residential lease, and the lessor's attempts to terminate the lease without first obtaining stay relief were ineffective. Although month-to-month leases may be subject to termination, the tenancy was property of the bankruptcy estate and subject to protections of the automatic stay. In re Myers, 633 B.R. 286 (Bankr. D. S.C. 2021 J. Waites).

**Avoidance and Exemptions**

**Section 522(h) does not authorize debtors to avoid lien resulting from IRS's penalty claim.** The prior decision *In re DeMarah,* 62 F.3d 1248 (9th Cir. 1995) held that because § 522(c)(2)(B) provides that otherwise exempt property remains subject to a properly filed tax lien; therefore, the Chapter 7 debtors could not invoke § 522(h) to avoid a properly filed tax lien, even if that lien could have been avoided by the trustee under § 724(a). Here the trustee did avoid the tax lien to extent the lien secured the penalties claim, and that avoided lien was preserved for the benefit of the estate. Section 522(c)(2) makes it clear that a debtor's exemption power cannot overcome a tax lien, regardless of whether the trustee avoided the lien. In re Hutchinson, 15 F.4th 1229 (9th Cir. 2021).

**Avoidance under § 522(f)(3).** Interpreting § 522(f)(3)'s restrictions on avoidance rights, the debtor's claim of exemptions under applicable Wisconsin law satisfied § 522(f)(3)(A) because Wisconsin had opted out of the federal bankruptcy exemptions. Subpart (B) restricts avoidance if the applicable state law satisfies one of the alternatives concerning consensual liens, either that the state law permits a claim of exemption without limitation in amount, except as to consensual liens, or prohibits avoidance of consensual liens. There are "competing interpretations of the statute…[that] highlight its poor drafting," and the Court concluded that Wisconsin law did not prohibit avoidance of consensual liens. Thus subpart (B) was not satisfied, and the debtors were able to avoid the consensual lien to the extent of available exemption in tools of trade under Wisconsin's statute. In re Klug, ___ B.R. ___, 2021 WL 4237307 (Bankr. W.D. Wisc. Sept. 16, 2021 J. Furay).

**Converting nonexempt assets to exempt was not fraudulent.** Overruling objections to the Chapter 7 debtor's claim of exemptions, the Court reviewed authority on pre-bankruptcy conversion of nonexempt assets to exempt, concluding that both Wisconsin and Federal law "align in endorsing the following key principle: a debtor does not defraud his creditors when he does no more than convert assets from non-exemptible to exemptible forms before a bankruptcy case or efforts to collect by attachment, execution, or other process, even if he does so intending to put his property beyond the reach of his creditors." In re Galesky, ___ B.R. ___, 2021 WL 4704805 (Bankr. E.D. Wisc. Sept. 29, 2021 J. Halfenger).

**Post-foreclosure deficiency judgment impaired homestead exemption.** The creditor argued that its deficiency judgment lien after foreclosing on non-homestead property was not avoidable under § 522(f)(2)(C), but the Court found a split of authority on interpretation of the statute, with an "overwhelming majority of courts hold[ing] that mortgage deficiency liens are not judgments that arise out of a mortgage foreclosure and are therefore avoidable under § 522(f)." Relying on *In re Hart,* 328 F.3d 45 (1st Cir. 2003), the Court agreed with the majority view, concluding that § 522(f)(2)(C) "does not preclude avoidance of a mortgage deficiency judgment lien." In re Le, ___ B.R. ___, 2021 WL 5028962 (Bankr. M.D. Fla. Oct. 29, 2021 J. Jennemann).

**Annuity exemption under § 522(d)(10)(E).** Overruling the Chapter 7 trustee's objection to the debtors' claim of annuity exemption, the Court analyzed whether factors identified in *In re Anderson,* 259 B.R. 687 (B.A.P. 8th Cir. 2001) were still relevant in light of *Rousey v. Jacoway,* 544 U.S. 320 (2005), concluding that the annuity at issue satisfied critical requirements for exemption. In re Wainer, ___ B.R. ___, 2021 WL 5343921 (Bankr. E.D. Pa. Nov. 16, 2021 J. Frank).

**Tenancy by entirety property interest.** Applying North Carolina law that recognized tenancy by entirety property ownership, the Chapter 7 debtor had an interest in such property at commencement of the case, but the other tenant did not file bankruptcy. The debtor's interest became property of the estate, subject to exemption but also subject to the trustee's right to administer the property interest for the benefit of creditors holding joint claims against both tenants. Although the spouses divorced post-bankruptcy and the tenancy by entirety would be terminated by the divorce, that termination did not itself bring the debtor's new interest as tenant in common into the bankruptcy estate. Rather, the debtor's interest in an equitable distribution from the property became property of the bankruptcy estate at filing and remained in the estate after termination of the tenancy by entirety. The debtor's motion to force the trustee to abandon the interest was denied. In re Gifford, ___ B.R. ___, 2021 WL 5286301 (Bankr. D. N.C. Nov. 12, 2021 J. Kahn).

**Discharge**

**Bankruptcy court had discretion to extend time to effect service of nondischargeability complaint.** The bankruptcy court had extended time to effect service of process. Rule Civil P. 4(m) does not set a time limit, and the abuse of discretion standard requires examination of the reasons for extension. Here, the extension was tied to litigation and appeals over whether the complaint should have been dismissed on other grounds. Moreover, dismissal now for failure to serve more promptly would amount to dismissal with prejudice. In re Cutuli, 13 F.4th 1342 (11th Cir. 2021).

**User error caused complaint to be untimely.** Affirming the bankruptcy court's finding that a dischargeability complaint was untimely and that the creditor's attorney's user error caused the untimeliness, rather than CMECF system malfunction. The complaint was properly dismissed. State Bank of Southern Utah v. Beal, ___ B.R. ___, 2021 WL 4245105 (D. Utah Sept. 16, 2021).

**Plaintiffs' implied consent to final judgment.** In § 727(a) proceeding, when debtor moved for dismissal and the plaintiffs' response stated that they did not consent to entry of final order or judgment, the Court examined whether those parties had consented by their prior actions. In their amended complaint, the plaintiffs demanded judgment for $100,000 against the defendant debtor, and such judgment would not be possible without consent to final judgment. Moreover, the conduct of the plaintiffs supported a finding that they had given implied consent to final judgment by the bankruptcy court under the standard established by *Roell v. Withrow,* 538 U.S. 580 (2003). In re Pritchard, ___ B.R. ___, 2021 WL 4483417 (Bankr. E.D. Tenn. Sept. 30, 2021 J. Rucker).

**Stipulated judgment given preclusive effect.** The Chapter 7 debtor had consented to a stipulated judgment in state court for fraudulent concealment, and that judgment was entitled under California law to preclusive effect in a § 523(a)(2)(A) complaint. In re Italiane, 632 B.R. 662 (B.A.P. 9th Cir. Oct. 4, 2021 J. Spraker).

**Shotgun pleading requires more definite statement.** Quoting Winston Churchill's plea for brevity, the Court found the "shotgun pleading" approach to the dischargeability complaint to be in violation of Rule of Civil Procedure 8(a)(2), 9(b) and 10(b). An amended complaint was required, with more definite statements of the grounds for relief under §§ 523(a)(2), (4) and (6). In re Ozcelebi, 2021 WL 6140249 (Bankr. S.D. Tex. Dec. 29, 2021 J. Rodriguez).

**Tax debt derived from State's "report" requirement was excepted from discharge.** Adopting the opinion of its Bankruptcy Appellate Panel at 619 B.R. 397 (B.A.P. 9th Cir. 2020), except for a footnote, § 523(a)(1)(B) excepts from discharge taxes with respect to which a "return, or equivalent report or notice" was not filed. The California statute requires the taxpayer to file a "report" to the Franchise Tax

Board if the taxpayer receives notice of changes or corrections to the federal tax return, and the Court held that this "report" requirement was equivalent to a "return" for purposes of § 523(a)(1)(B). In re Berkovich, 15 F.4th 997 (9th Cir. 2021). See also In re Sienega, 18 F.4th 1164 (9th Cir. 2021) (Faxes notifying state taxing authority of changes in Federal return were not "return" within meaning of § 523(a)(1)(B).).

**Basis for state-court judgment was unclear and creditor/plaintiff was not collaterally estopped from asserting § 523(a)(4) complaint.** The Sixth Circuit remanded, after finding that the prepetition state-court judgment was unclear in the basis for its relief. The bankruptcy and district courts had found that judgment to be based on a breach of contract claim, but the state-court complaint sufficiently alleged larceny and defalcation, with the judgment unclear as to whether it was based only on breach of contract. Under applicable Tennessee law, the judgment did not prevent the plaintiff/creditor from litigating dischargeability in the bankruptcy case. In re Piercy, ___ F.4th ___, 2021 WL 6133173 (6th Cir. Dec. 29, 2021).

**Student loan debt and its purpose.** In a dispute over which subsection of 523(a)(8) applied, the debtor argued that the claims were not for "educational loans because a portion exceeded the cost of attendance, and some loans were used to attend an unaccredited for-profit institution. "Courts have held that the purpose, and not the actual use of the funds, determines whether the loan is 'educational' under § 523(a)(8)(A)," with the Sixth Circuit looking to the "initial purpose." The Court reviewed the loan applications and promissory notes to determine the purpose, finding that the loans at issue fell within the educational loan scope of § 523(a)(8)(A). In re Latson, ___ B.R. ___, 2021 WL 4484022 (Bankr. N.D. Ohio Sept. 30, 2021 J. Gustafson).

## Chapter 7 Issues

### Eligibility

**Power of attorney authorized spouse to act as debtor's attorney in fact.** Applying Missouri law, the power of attorney that debtor executed prepetition was a valid power of attorney, authorizing the debtor/wife to act as husband's attorney in

fact in Chapter 7 case. The power of attorney included powers related to bankruptcy. There were grounds to support waiver of the husband's requirement for prepetition credit counseling. In re Sugg, 632 B.R. 779 (Bankr. E.D. Mo. 2021 J. Clair).

**Abandonment**

**Abandonment requires asset to be included in schedules, and disclosure in statement of financial affairs was insufficient.** Affirming its BAP, the Ninth Circuit held that the Chapter 7 debtors' cause of action had not been abandoned by the trustee, even though the pending lawsuit was discussed by the debtors with the trustee and the cause of action was disclosed in the statement of financial affairs. To satisfy § 554(c), abandonment requires that property be "scheduled under section 521(a)(1)," and the Circuit as a matter of first impression held that this requires that "property must be scheduled on a schedule, not just listed on the SOFA." In re Stevens, 15 F.4th 1214 (9th Cir. 2021). See also Litton Loan Servicing, L.P. v. Schubert, ___ B.R. ___, 2021 WL 4304280 (N.D. Ohio Sept. 22, 2021) (Bankruptcy court did not abuse discretion in granting Chapter 13 debtors' request for abandonment of their breach of contract counterclaims against mortgage servicer.).

**Trustee's counsel**

**Trustee could employ litigation counsel nunc pro tunc.** The Court interpreted the Supreme Court's holding in *Acevedo,* 140 S.Ct. 696 (2020), "as limited to a prohibition on creating facts that never were before the court. The Court further finds persuasive other courts' reasoning that *Acevedo* does not prohibit retroactive employment of professionals." The trustee's application here to employ litigation counsel nunc pro tunc comports with Rule 2014, and the creditor objecting to employment was not prejudiced because it knew of a prior employment allowing the trustee's counsel to employ co-counsel. In re Ramirez, 633 B.R. 297 (Bankr. W.D. Tex. 2021 J. Gargotta).

**Conversion and Dismissal**

**Conversion to Chapter 13 over objection of Chapter 7 trustee.** After entry of Chapter 7 discharge, the Chapter 7 trustee initiated sale of the debtors' home and the debtors moved to covert to Chapter 13 under § 706(a), but the trustee objected on grounds of bad faith. Reviewing the facts and circumstances in light of *Marrama,* 569 U.S. 365 (2007), the Court found the debtors to be eligible for Chapter 13 relief under § 109(e) and conversion was not in bad faith. The bad faith determination is made under a total of circumstances using seven factors found in *In re Gier,* 986 F.2d 1326 (10th Cir. 1993). In re Johnson, ___ B.R. ___, 2021 WL 6053832 (Bankr. D. Colo. Dec. 15, 2021 J. McNamara).

**Dismissal of case involving two-party dispute.** Finding authority to dismiss a Chapter 7 case under § 707(a) when it is an abuse of the bankruptcy process, the case was a battle between two parties who had litigation pending in another forum, with the non-debtor party holding over 99% of potential claims in the case. The Court had authority to dismiss, for cause, *sua sponte.* In re Goden, 2021 WL 5286364 (Bankr. D. Maryland Nov. 12, 2021 J. Alquist).

**Reaffirmation**

**Reaffirmation and ride-through.** Discussing reaffirmation when the debtor's attorney had signed the certification under threat from the creditor that it would repossess the mobile home if the attorney did not certify, the Court considered the effects of failure of certification on a debtor's potential "ride-through" option. This debtor, unlike the debtor in *In re Dumont,* 581 F.3d 1104 (9th Cir. 2009), had complied with §§ 521(a)(2), (6) and 362(h), by stating her intent to reaffirm and entering into a reaffirmation agreement. Under the majority view, adopted by this Court, "ride-though is not affected whether the agreement is certified," and "nothing in the plain, but very specific language of §§ 521(a)(6) and 362(h), requires a reaffirmation agreement be certified or otherwise enforceable to preserve the ride-through option. Those statutes also do not require that a reaffirmation agreement be enforceable in order to protect the debtor from an *ipso facto* clause." In this case, although debtor's counsel withdrew certification at the hearing, resulting in the

reaffirmation being unenforceable, the debtor "was nonetheless protected from the loss of ride-through because she otherwise complied with the statutory requirements." In addition, the creditor's failure to file a proof of claim preserved the debtor's ride-through, because the creditor did not have an "allowed" claim for purposes of 521(a)(6)'s remedies. The Court also discussed the difficulty of reaffirmation choices when the collateral is a mobile home, because issues arise whether the collateral is attached to real property, and §§ 521(a)(6), 521(d) and 362(h) only pertain to personal property collateral. In summary, this debtor's "timely compliances with §§ 521(a)(2), 521(a)(6) and 362(h) provided her the benefit of ride-through and protection from the *ipso facto* clause under § 521(d)." In re Rhodes, ___ B.R. ___, 2021 WL 5863383 (Bankr. S.D. Cal. Dec. 9, 2021 J. Mann).

**Chapter 13 Issues**

**Confirmation**

**No interest required in plan paying creditors 100%.** Although the plan proposed to pay unsecured claims 100%, it did not commit all disposable income and did not propose payment of interest on those claims. A judgment creditor objected to confirmation, arguing that § 1325(b)(1) required payment of interest when the debtor was not committing all disposable income. The Court concluded that section's subparts are written in disjunctive, requiring compliance with only one subpart, and part (A) provides that confirmation may be based on the payment of the full amount of the claim. The Court found the majority of court decisions holding that an above-median debtor is not required to devote all disposable income if the plan pays allowed unsecured creditors in full within 60 months. The Court also found that courts have disagreed whether subsection (A) requires payment of interest, concluding that § 1325(b)(1)'s phrase "as of the effective date of the plan" refers to *when* the court determines what is being paid to unsecured creditors and does not require payment of interest. In other Code sections that phrase follows the word "value," and in those instances the phrase modifies that word, requiring payment of interest as part of value determination. The opinion agreed with the *Collier* interpretation and disagreed with the interpretations found in *Norton* and *Lundin on*

*Chapter 13.* In re Moore, ___ B.R. ____, 2021 WL 5711785 (Bankr. D. S.C. Nov. 23, 2021 J. Waites).

**TitleMax held secured claim that could be treated in plan.** Examining Alabama law on whether TitleMax held a secured claim or whether the debtor's and estate's interests in a vehicle had been forfeited to TitleMax, the Court determined under Alabama's Pawnship Act that "a good that secured a pawn, but that the pawnbroker allows to remain in the possession of the pawnor until the pawnbroker elects to exercise its post-default right to take possession, is not a pledged good" under the Act. Only "pledged goods" are subject to that Act's statutory possessory lien and automatic forfeiture provision. The estate retained an interest in this vehicle, and the debtor could provide plan treatment of TitleMax's secured claim. In re Hambright, ___ B.R. ___, 2021 WL 5441074 (Bankr. N.D. Ala. Nov. 19, 2021 J. Henderson).

**Best interests test and preferences.** The debtor disclosed payment of $8,000 to family members within one year of bankruptcy filing, and the trustee objected to confirmation, asserting that the best interests test required adding repayment of the $8,000 preference to the plan payments. The Court found that the best interests test would require $8,000 recovery in hypothetical Chapter 7, but that amount would be reduced by Chapter 7 administrative costs and also by the amount of priority claims, rejecting the trustee's argument that the preference amount should be in addition to a hypothetical distribution. The amount offered by debtor's plan exceeded requirements of best interests test and projected disposable income. Also, the plan met good-faith requirement for confirmation. In re Law, 2021 WL 6140248 (Bankr. S.D. Ill. Dec. 29, 2021 J. Altenberger).

**Modification**

**Base plan would require modification to increase payments to creditors.** Following approval of the debtor's motion to sell real property, the issue was whether net sale proceeds should be distributed to unsecured creditors, and the confirmed plan was a "base or pot" plan providing for creditors to share in a specific amount. "To increase the payment to creditors beyond the base amount, the confirmed plan

must be modified," and although the debtor voluntarily proposed paying the net sale proceeds to creditors, a plan modification motion is required under Rule 3015(h). In re Anderson, ___ B.R. ___, 2021 WL 5772522 (Bankr. D. S.C. Nov. 10, 2021 J. Waites).

**Dismissal**

**Dismissal with 3-year bar to refiling.** The trustee had sought dismissal of the debtor's case with prejudice and a 5-year bar to refiling, based on her abuse of the bankruptcy process, and the Court found that the debtor in two prior Chapter 13 cases had "displayed a penchant for vexatious, frivolous litigation designed to bog down the respective courts with innumerable pleadings and appeals in an apparent effort to hinder the payment of her creditors." The same tactics existed in this third case. Section 1307 authorizes dismissal for cause, and although not included in § 1307(c)'s nonexclusive list of cause, lack of good faith constitutes grounds for dismissal. There was overwhelming evidence of the debtor's misuse of the Bankruptcy Code, but a 5-year bar to refiling was "an extreme remedy for a pro se debtor." The Court found that dismissal with prejudice and a 3-year bar was appropriate. In re Parson, 632 B.R. 613 (Bankr. N.D. Tex. 2021 J. Larson). See also In re Minogue, 632 B.R. 287 (Bankr. D. S.C. 2021 J. Waites) (Discussing split of authority on whether debtor has right to dismiss in response to a motion to convert to Chapter 7, under *Law v. Siegel* there is "no reason to conclude that a Chapter 13 debtor may be precluded from voluntarily dismissing his or her Chapter 13 case in the face of a pending motion to convert," but that did not prevent the bankruptcy court from using other powers under §§ 109(g) or 349(a) to condition the dismissal. In light of evidence of bad faith conduct, the dismissal was granted with a bar to any voluntary filing for two years.).

**Trustee**

**Trustee could not retain fee on amounts collected in unconfirmed case.** Disagreeing with the bankruptcy court, the district court held that § 1326(a)(2) controlled over 28 U.S.C. § 586(e). Moreover, § 1326(a)(2) does not provide

specifically for the trustee to retain a fee in unconfirmed cases, in contrast to § 1226(a)(2). In re Doll, 2021 WL 5768991 (D. Colo. Dec. 6, 2021).

**Creditor's motion for removal of trustee denied.** Among other issues raised by a creditor, the Court denied the motion to remove the trustee. As a part of its objections to confirmation, the creditor alleged that the trustee had breached fiduciary duties and did not preserve business equipment for benefit of creditors, but the creditor did not establish basis for removal by preponderance of evidence. In re Gutierrez, ___ B.R. ___, 2021 WL 4715693 (Bankr. S.D. Tex. Oct. 8, 2021 J. Rodriguez).

**Claims**

**Plan provision for State's claim under § 507(a)(1)(B) did not prevent subsequent claim objection.** Although the Chapter 13 plan provided for the treatment of the claim of the State Department of Children and Families to be priority under § 507(a)(1)(B), the debtors subsequently objected to the claim. The plan provided for 60 months of payments and further provided that the State's claim would be paid less than the full amount under § 1322(a)(4). Subsequent to confirmation, the Seventh Circuit's *In re Dennis,* 927 F.3d 1015 (7th Cir. 2019), held that a claim for overpayment of public assistance benefits was not entitled to priority under § 507(a)(1)(B). Finding no statutory or rule deadline for claim objections, the plan provision for the claim was not preclusive. Rule 3012(a)(2) permits the court to determine the amount of a claim entitled to priority, and Rule 3012(b) authorizes this objection. The *Dennis* decision "militates against applying law of the case" from the confirmation order. In re Terrell, ___ B.R. ___, 2021 WL 4304839 (Bankr. E.D. Wisc. Sept. 21, 2021 J. Halfenger). In subsequent decision, 2021 WL 5179214 (Bankr. E.D. Wisc. Nov. 3, 2021), over the State Department's objection, the debtors were allowed to modify the plan to shorten the term from 5 to 3 years. The State has filed appeal on November 4, 2021, to the Seventh Circuit.

**Remedies for violation of Rule 3002.1(c)(2).** The reverse mortgage holder did not file a proof of claim, and the debtor's attorney filed one on behalf of the creditor, but the creditor did not comply with Rule 3002.1's requirement of disclosing post-petition

advances and expenses for taxes and insurance. The Court determined that appropriate remedies under Rule 3002.1(i) included prohibiting the creditor from asserting the undisclosed advances during the bankruptcy case as a basis for plan objection, stay relief or in any other contested matter or adversary proceeding. Non-payment of the undisclosed advance could not be used as an act of default under the reverse mortgage. The creditor's non-compliance with the Rule also justified an award of attorney fees to the debtor. In re Legare-Doctor, ___ B.R. ___, 2021 WL 5712149 (Bankr. D. S.C. Dec. 1, 2021 J. Waites).

**IRS claim for shared responsibility payments entitled to priority.** Under the Affordable Care Act, individuals failing to maintain qualified health insurance or to qualify for exemption from the requirement are subject to a "shared responsibility payment" for those months they lack health insurance coverage. The liability is subject to priority treatment under § 507(a)(8)(A) because the shared responsibility payment is measured by income. The obligation must be provided priority treatment in a Chapter 13 plan. In re Miller, ___ B.R. ___, 2021 WL 4994424 (Bankr. M.D. Ga. Oct. 26, 2021 J. Laney).

**Sufficiency of notice of bar date.** Construing Rule 3002(c)(6)(A), notice to attorney who represented creditor in collection litigation was sufficient for purposes of applying bar date for timely proof of claim. The creditor moving for extension of bar date must show that it received insufficient notice of the proof of claim deadline. The general rule is that notice to a party's attorney satisfies requirement of notice to the party, and although the collection attorney had not been engaged to represent the creditor in the Chapter 13 case, the attorney had given actual notice to the creditor of the bankruptcy filing. The debtor's objection to the untimely claim was sustained. In re Vrusho, ___ B.R. ___, 2021 WL 5762941 (Bankr. D. N.H. Dec. 3, 2021 J. Harwood).

# Recent Developments in Bankruptcy Law, July 2021

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## 1. AUTOMATIC STAY

### 1.1 Covered Activities

### 1.2 Effect of Stay

### 1.3 Remedies

1.3.a **Court denies retroactive stay relief that would validate default judgment.** The debtor did not notify a tort claimant of his chapter 11 filing. The claimant filed an action against the debtor after the bankruptcy filing. The debtor did not respond, and the claimant obtained a default judgment. The debtor's case was dismissed for failure to prosecute. Later, the debtor filed a second chapter 11 case, which was converted to chapter 7. The claimant sought retroactive stay relief to validate the prior default judgment. An act taken in violation of the automatic stay is void. However, section 362(d) permits annulment or retroactive stay relief, which would validate a prior action taken in violation of the stay. A court should not grant retroactive relief to validate a default judgment. The debtor may justifiably rely on the stay to be automatic and to relieve the debtor from any obligation to respond to a post-bankruptcy complaint. Therefore, the court grants prospective relief to permit the filing of a new action but denies retroactive relief. *Garcia v. Sklar (In re Sklar)*, 626 B.R. 750 (Bankr. S.D.N.Y. 2021).

## 2. AVOIDING POWERS

### 2.1 Fraudulent Transfers

### 2.2 Preferences

### 2.3 Postpetition Transfers

### 2.4 Setoff

### 2.5 Statutory Liens

### 2.6 Strong-arm Power

### 2.7 Recovery

## 3. BANKRUPTCY RULES

## 4. CASE COMMENCEMENT AND ELIGIBILITY

### 4.1 Eligibility

4.1.a **Nonbankruptcy law governs characterization of a business trust.** An indebted Singapore trust that owned real estate filed a chapter 11 case. Lenders filed a motion to dismiss on the ground that the debtor was not eligible to be a debtor under the Bankruptcy Code. Only a person may be a debtor under chapter 11. A trust that is not a business trust is not a person. Many prior decisions applied federal common law to determine whether a trust was a business trust. However, the Bankruptcy Code applies state law to determine legal rights and liabilities unless some federal interest or Code provision provides otherwise. There is no federal interest in determining eligibility. Therefore, the court must look to the nonbankruptcy law creating an artificial entity to determine the entity's nature, rights, and capacity to take specific legal action. Applying Singapore law, the court determines the debtor is a business trust and denies the motion to dismiss the case. *In re EHT US1, Inc.*, ___ B.R. ___, 2021 Bankr. LEXIS 1477 (Bankr. D. Del. June 1, 2021).

4.1.b **Wind-down activities constitute commercial or business activities for subchapter V eligibility purposes.** The debtor operated a flue gas energy recovery facility, selling steam and electricity to its customers. A dispute with the energy supplier resulted in the termination of the debtor's operation and in litigation against the supplier to recover damages. The debtor filed a chapter 11 petition and elected to proceed under subchapter V. As of the petition date, in addition to pursuing the litigation, the debtor was actively maintaining and preserving its physical assets and working on a sale of the assets. A debtor is eligible to proceed under subchapter V if the debtor is engaged in commercial or business activities. Commercial activities involve "the exchange or buying and selling;" business activities involve dealing or transactions of an economic nature. Subchapter V does not require that the commercial or business activities be the same as the debtor's core or historic operations. Nor does it require the case to result in reorganization of such operations or business, as it permits a plan that may include selling all assets. Because the debtor's activities as of the petition date qualified as commercial or business activities, the court denies a motion to dismiss the case or void the subchapter V election. *In re Port Arthur Steam Energy, L.P.*, ___ B.R. ___, 2021 Bankr. LEXIS 1793 (Bankr. S.D. Tex. July 1, 2021).

### 4.2 Involuntary Petitions

### 4.3 Dismissal

## 5. CHAPTER 11

### 5.1 Officers and Administration

5.1.a **Board-elected officers are not eligible for a KERP.** The debtor in possession adopted a key employee retention plan for about 190 employees, including six employees who were elected as officers by the board of directors. Section 503(c) severely limits KERP payments to insiders. The definition of "insider" includes officer, but the Code does not define "officer." Objective criteria should govern whether an employee is an officer. Under nonbankruptcy law, someone elected to an officer position by the board is an officer and should be treated as such for Bankruptcy Code purposes, whatever the scope of the individual's duties and authority. Therefore, the six employees are not eligible to participate in the KERP. *Harrington v. LSC Comm'ns (In re LSC Comm'ns)*, ___ B.R. ___, case no. 20-CV-5006 (JPO) (S.D.N.Y. July 9, 2021).

### 5.2 Exclusivity

### 5.3 Classification

### 5.4 Disclosure Statement and Voting

### 5.5 Confirmation, Absolute Priority

5.5.a **In an individual subchapter V case, good faith does not require best efforts.** The debtor was a high income individual. He proposed a plan that would pay unsecured claims 7.5% over three years. The class of unsecured claims accepted the plan, but one creditor objected to confirmation on good faith grounds. Section 1129(a)(3) requires as a condition to confirmation that the plan be proposed in good faith. Good faith includes pursuing a result that is consistent with the Code's objective and purposes, including preserving going concern value, maximizing property available to creditors, the fresh start, deterring misconduct, expeditious resolution, and achieving fundamental fairness and justice. Thus, courts analyze good faith based on the totality of the circumstances but construe the requirement narrowly to prevent the requirement from importing a judge's subjective moral judgments into the force of law. Confirmation denial should be reserved for egregious cases. The class's acceptance of the plan is important in evaluating good faith. Here, though the debtor might have been able to pay more, the debtor was not taking advantage of the system and did not go overboard in his lifestyle. Given that creditors accepted the plan, the court finds it was proposed in good faith. *In re Walker*, 628 B.R. 9 (Bankr. E.D. Pa. 2021).

## 6. CLAIMS AND PRIORITIES

### 6.1 Claims

6.1.a **Unimpaired unsecured claims are entitled to postpetition interest at the federal judgment rate.** The plan provided that the class of unsecured claims was unimpaired. Creditors with a claim must pursue their rights in federal court, subject to federal law. A claim as of the petition date is similar to a federal judgment, whose payment depends on completion of the bankruptcy process, making postpetition interest analogous to post-judgment interest, which is payable at the federal judgment rate. The Code and federal law impose the limitation to the federal judgment rate; the plan is not the source of the limitation. Therefore, use of the federal judgment rate rather than the contract rate does not impair the class under section 1124 for. *Official Comm. v. PG&E Corp.*, 2021 U.S. Dist. LEXIS 96081 (N.D. Cal. May 20, 2021).

### 6.2 Priorities

6.2.a **Claims for the purchase price of a private flight service membership are entitled to priority.** The debtor provided private flights to its "members." To become a member, a consumer was required to pay the debtor a fixed amount, which would entitle the consumer to a certain number of flight hours. The debtor maintained a ledger recording the amount paid and the deductions for flight hours used. The payments were nonrefundable unless the debtor terminated the agreement with the consumer. Section 507(a)(7) grants priority to a claim "arising from the deposit … of money in connection with the purchase … of property or … services … that were not delivered or provided." A "deposit" is the giving of money to another who promises in exchange to return goods or services. Where a membership is part of a dependent, open transaction for future services and contains no independent value, the membership purchase price is a deposit for future services, not a completed purchase of a membership. Therefore, the claims are entitled to priority. *In re Superior Air Charter, LLC*, 627 B.R. 241 (Bankr. D. Del. Apr. 9, 2021).

## 7. CRIMES

## 8. DISCHARGE

### 8.1 General

### 8.2 Third-Party Releases

### 8.3 Environmental and Mass Tort Liabilities

## 9. EXECUTORY CONTRACTS

9.1.a **Specific performance order renders a contract non-executory.** The debtor contracted to sell land, subject to town approval of a subdivision. The debtor interfered with the buyer's efforts to obtain town approval. The buyer sued in state court, obtaining a specific performance order requiring the debtor to obtain the zoning variance necessary to gain subdivision approval. The debtor filed a chapter 11 petition and moved to reject the contract. A specific performance judgment cannot be an "executory contract," because the order transforms the parties' unperformed obligations into non-material or ministerial acts to follow the court's order. Here, the order did not require conveyance of title only because title could not be conveyed until the variance and the subdivision approval were obtained. The order implied a requirement to convey title once those conditions were satisfied. Moreover, an obligation to convey title does not render a contract executory, because state law results in an equitable conversion of title once a contract becomes subject to a specific performance order. Therefore, the court denies the debtor's motion

to reject the contract. *In re Brick House Props., LLC*, 2021 Bankr. LEXIS 1585 (Bankr. D. Utah June 11, 2021).

9.1.b **Prepetition contract repudiation renders contract not executory.** Six months before bankruptcy, the debtor cancelled the remaining open purchase orders under a supply contract, claiming the supplier had provided parts that did not comply with contract specifications. The supplier disputed the debtor's claim and right to cancel the remaining purchase orders, but the parties did no further business after the cancellation. An executory contract is one under which some performance remains due on both sides. Where a party clearly repudiates a contract, the other party is relieved of any remaining performance obligation. Therefore, the contract is no longer executory. *In re Cornerstone Valve LLC*, 2021 Bankr. LEXIS 1120 (Bankr. S.D. Tex. April 27, 2021).

## 10. INDIVIDUAL DEBTORS

### 10.1 Chapter 13

### 10.2 Dischargeability

10.2.a **Section 523 discharge exceptions do not apply in a non-individual subchapter V case.** A corporate subchapter V debtor confirmed a plan under section 1191(b), the subchapter V cram-down provision. Creditors brought a nondischargeablity complaint. Section 1192 provides that if the plan is confirmed under section 1191(b), "the court shall grant the debtor a discharge of all debts … except any debt … of the kind specified in section 523(a)." Section 523(a) provides that a "discharge under section … 1192 … does not discharge an individual debtor from any debt" listed in the subsection. Because section 523(a) applies only to individual debtors, the reference to it in section 1192 does not apply to non-individual debtors. The court therefore dismisses the dischargeability complaint. *Gaske v. Satellite Rests. Inc. (In re Satellite Rests. Inc.)*, 626 B.R. 871 (Bankr. D. Md. 2021).

### 10.3 Exemptions

### 10.4 Reaffirmations and Redemption

## 11. JURISDICTION AND POWERS OF THE COURT

### 11.1 Jurisdiction

### 11.2 Sanctions

### 11.3 Appeals

### 11.4 Sovereign Immunity

11.4.a **Sovereign immunity does not bar post-effective date action against a state.** During bankruptcy, the debtor in possession agreed to lease the state some estate property. Separately, the state also filed a proof of claim for environmental damage. The plan created a liquidating trust, which assumed all the property of the estate and was to make distributions to creditors. After a dispute arose about the lease, the state took over the leased facility without paying rent, relying on its police power to protect the environment and public safety. The take-over persisted after the effective date. The liquidating trustee sued the state to recover for the inverse condemnation of the leased facility, both before and after the effective date. A state generally has sovereign immunity against suit in the federal courts, but immunity in bankruptcy cases is limited, because in the Constitution, the states waived their immunity in certain bankruptcy proceedings. In sum, "States cannot assert a defense of sovereign immunity in proceedings that further a bankruptcy court's *in rem* jurisdiction no matter the technical classification of that proceeding," including the court's exercise of *in rem* jurisdiction over the debtor's property, the equitable

distribution of property, and the discharge. A proceeding's function, not its form, governs. Here, the trustee's action against the state furthers the court's jurisdiction over the debtor's and the estate's property and over equitable distribution, in that it prevents the state from recovering on its proof of claim without answering to the trustee's claim. The post-effective date source of a portion of the trustee's claim does not matter to the immunity waiver, because the property to be recovered was in compensation for the trust's assets and furthers the equitable distribution of the estate among creditors. *Davis v. Calif.(In re Venoco LLC)*, 998 F.3d 94 (3d Cir. 2021).

## 12. PROPERTY OF THE ESTATE

### 12.1 Property of the Estate

12.1.a **Litigation funder's lien on personal injury action proceeds did not survive bankruptcy.** Before bankruptcy, the debtor obtained financing to pursue a personal injury tort action. Under New York law, a personal injury action is not assignable, but proceeds are. The debtor assigned and granted a security interest in the proceeds of the action to the financier. The debtor filed a chapter 7 petition before obtaining a judgment in the action. The financier filed a proof of secured claim. The trustee settled the action, and the financier claimed the proceeds. Property of the estate includes all the debtor's interests in property, notwithstanding applicable nonbankruptcy law to the contrary, so the action became property of the estate. Under section 541(a)(6), proceeds of the action became property of the estate only when received. Before that, the proceeds did not exist. The assignment of future proceeds operates only as a future lien and does not relate back to the assignment date. Therefore, the debtor's prepetition assignment and grant of a security interest in the action's proceeds was ineffective to vest in the financier any rights that survived the filing of a bankruptcy petition, and the proceeds became property of the estate, unencumbered by the financier's claimed interests. *In re Reviss*, 628 B.R. 386 (Bankr. E.D.N.Y. 2021).

### 12.2 Turnover

### 12.3 Sales

## 13. TRUSTEES, COMMITTEES, AND PROFESSIONALS

### 13.1 Trustees

13.1.a **Chapter 7 trustee does not succeed to committee's right to bring estate action against prepetition lenders.** The debtor in possession's financing agreement stipulated to the validity of the debtor's prepetition LBO financing and waived all claims of the debtor and the estate against the lender but permitted the unsecured creditors committee or "any party-in-interest, including a … trustee appointed or elected during the [75-day] Investigation Period" to challenge the validity of the prepetition financing. The committee brought a fraudulent transfer action against the prepetition lenders. Later, the case converted to chapter 7. Upon conversion, the committee ceased to exist. The trustee sought to substitute for the committee in the action. Because the trustee did not bring an action within the Investigation Period, the trustee may not assert a challenge to the financing. The committee's right to bring the action is not transferrable. The committee's claims are derivative of the DIP's, because the DIP granted the rights to the committee. But because the DIP barred itself from bringing those claims, the trustee, who succeeds only to such rights as the debtor and the estate had, could not. *Official Committee v. The CIT Group/Business Credit, Inc. (n re Jevic Holding Corp.)*, 2021 Bankr. LEXIS 1203 (Bank. D. Del. May 5, 2021).

13.1.b **Trustee's appellate standing does not depend on a pecuniary interest.** The bankruptcy court awarded counsel for the debtor in possession fees for services performed before the chapter 11 trustee was appointed. Two creditors objected and appealed. During the appeal, the creditors

settled with counsel but not with the trustee and sought to dismiss the appeal, arguing the appeal was moot and the trustee did not have standing to appeal. Ordinarily, for standing to appeal, a party must show a direct and adverse pecuniary interest that the order affected. However, trustees can never show they were pecuniarily affected, because they have no pecuniary interests in the cases they administer. Their standing arises from their duty to enforce the bankruptcy law in the public interest. Here, the trustee was responsible for paying the fees if they were awarded and therefore had an interest in determining whether they were proper. The court finds the trustee has standing and affirms the fee award on the merits. *Edwards Family P'ship v. Johnson (In re Cmty. Home Fin. Servs.)*, 990 F.3d 422 (5th Cir. 2021).

13.1.c ***Barton*** **doctrine does not apply after a receivership concludes.** After the conclusion of a state court receivership, the plaintiff, whose property the receiver administered, sued the receiver and others under a conspiracy theory. Under *Barton v. Barbour*, 104 U.S. 126 (1881), a court lacks jurisdiction over an action against a federal court receiver unless the appointing court has given permission for the action. The doctrine arises from the *in rem* nature of a receivership and the resulting protection of property that is subject to the receivership and is *in custodia legis*. Once the receivership concludes, there is no longer a receivership estate to protect, so *Barton* protection ends. However, a receiver and counsel are entitled to judicial immunity for acts within the scope of the receiver's authority, even if their acts were "in error, malicious, or … in excess of[the appointing court's ] jurisdiction." *Chua v. Ekonomou*, ___ F.3d ___, 2021 U.S. App. LEXIS 17755 (11th Cir. June 15, 2021).

### 13.2 Attorneys

13.2.a **An adequate ethical screen defeats a disqualification motion.** A partner at the defendant's law firm, who billed 300 hours to an adversary proceeding over three years, left the firm to join the firm representing the plaintiff. Her new firm immediately implemented an ethical screen that prohibited her from sharing any information she learned in the representation, from accessing any information in the new firm's files about the litigation, from discussing the matter with anyone at her new firm, and from sharing in any part of the fee from the litigation. Model Rule 1.10(a)(2) permits a screen to protect an attorney's duty of confidentiality to prevent disqualification, which should be granted only in exceptional circumstances. Here, there was no indication that the attorney or her new firm would not abide fully with the screen. Her limited involvement in this major litigation indicated that she was not a critical part of the trial team that would make this an exceptional case. Therefore, the court denies the defendant's disqualification motion. *Maxus Liquidating Trust v. YPF S.A. (In re Maxus Energy Corp.)*, 626 B.R. 249 (Bankr. D. Del. 2021).

### 13.3 Committees

### 13.4 Other Professionals

### 13.5 United States Trustee

13.5.a **2017 U.S. Trustee fee increase is constitutional and applies to pending cases.** In 2017, Congress amended 28 U.S C. § 1930(a)(6) to increase U.S. Trustee fees, effective January 1, 2018, including to then-pending chapter 11 cases. The fees are entitled to priority as an administrative expense. At the time, section 1930(a)(7) authorized but did not require the Judicial Conference to charge the same fees in chapter 11 cases pending in Bankruptcy Administrator district. The Judicial Conference increased fees effective October 1, 2018, but not for then-pending cases. The debtor filed its chapter 11 case in 2008. Under its confirmed plan, a liquidating trustee administered the case. The trustee brought an action to recover the difference in fees it paid compared to the fees it would have paid in a Bankruptcy Administrator district. Laws on the subject of bankruptcies must apply uniformly to a defined class of debtors and be geographically uniform. The uniformity requirement does not prohibit a law that addresses regionally isolated problems. Here, the U.S. Trustee program suffered budgetary pressures, while the Bankruptcy Administrator program did not. Because the fee increase was directed to addressing the budget problems in the U.S. Trustee districts, it qualified as a law that addressed

only a regionally isolated problem. *Siegel v. Fitzgerald (In re Circuit City Stores, Inc.)*, 996 F.3d 156 (4th Cir. 2021).

13.5.b **2017 U.S. Trustee fee increase is unconstitutional.** In 2017, Congress amended 28 U.S C. § 1930(a)(6) to increase U.S. Trustee fees, effective January 1, 2018, including to then-pending chapter 11 cases. The fees are entitled to priority as an administrative expense. At the time, section 1930(a)(7) authorized but did not require the Judicial Conference to charge the same fees in chapter 11 cases pending in Bankruptcy Administrator district. The Judicial Conference increased fees effective October 1, 2018, but not for then-pending cases. In 2020, Congress amended section 1930(a)(7) to require the Judicial Conference to charge the same fees, although the Judicial Conference has not yet implemented the change with respect to cases that were pending on October 1, 2018. The debtor filed its chapter 11 case in December 2017. It later brought an action to recover the difference in fees it paid compared to the fees it would have paid in a Bankruptcy Administrator district. A law imposing fees on bankruptcy estates is a law on the subject of bankruptcies, because it affects the recoveries of creditors, who may receive payment only after payment of the U.S. Trustee fees. Therefore, it must comply with the Constitution's uniformity requirement. The treatment of estates in U.S. Trustee districts differs from their treatment in Bankruptcy Administrator districts and is therefore non-uniform. Non-uniformity may be justified by a geographically isolated problem. However, in this case, the difference between the U.S. Trustee districts and the Bankruptcy Administrator districts, though geographically isolated, is based on a geographical distinction Congress created, which cannot then be used to justify additional geographical differences. Therefore, the fee increase is unconstitutional, and the debtor in possession is entitled to the refund. *Clinton Nurseries, Inc. v. Harrington (In re Clinton Nurseries, Inc.)*, 998 F.3d 56 (2d Cir. 2021).

13.5.c **Litigation trust disbursements are not subject to U.S. Trustee fees.** On the debtor's plan effective date, the estate transferred claims against a third party to a litigation trust for the benefit of creditors. The transfer to the trust was in consideration of the releases of claims against the debtor, and for tax reasons, the parties were required to treat the transfer as a transfer directly to the trust beneficiaries, followed by a contribution by the beneficiaries to the trust. Upon the transfer, the debtors and their estates had no further interests in the trust assets or the trust. During the calendar quarter in which the trust transfer was made, the estate paid U.S. Trustee fees under 28 U.S.C. § 1930(a), based on the amounts included in the transfer. Later, the trust settled the litigation against the third party and received a payment, which it distributed to the trust beneficiaries. Section 1930(a)(6) requires payment of U.S. Trustee fees each quarter in every chapter 11 case based on the amount of "disbursements" until the case is closed or dismissed. Courts have interpreted "disbursements" to mean those made by or on behalf of a debtor or its estate and those in which the debtor or estate had some interest in or control over the money disbursed. Because the debtor and the estate had no interest in the litigation proceeds, the transfer to the trust was actually to and for the benefit of the trust beneficiaries, and the estates had paid a U.S. Trustee fee based on the distribution to the trust, the disbursement of litigation proceeds were not by or on behalf of the debtor and were not subject to the U.S. Trustee fee. *In re Paragon Offshore, PLC*, Case no. 16-10386-CSS (Bankr. D. Del. June 28, 2021).

## 14. TAXES

## 15. CHAPTER 15—CROSS-BORDER INSOLVENCIES

15.1.a **Chapter 15 filing as a tactic to stay U.S. litigation does not constitute bad faith warranting refusal of recognition.** Minority shareholders derivatively sued a Bermuda company in New York over a refinancing and a large dividend. After the court dismissed the action and before the time for appeal had run, the company entered a members voluntary liquidation in Bermuda. After many more years of litigation and the depletion of most of the assets of the Bermuda company, leaving it insolvent, the liquidators initiated a Bermuda court-supervised liquidation proceeding.

The liquidators then sought an anti-suit injunction from the Bermuda court. In response, the New York plaintiffs sought a TRO to enjoin the anti-suit action. After a stand-still on those matters, the liquidators sought recognition of the Bermuda liquidation as a foreign main proceeding under chapter 15 to ensure the Bermuda proceedings would be binding and enforceable in the United States so as to preclude the New York plaintiffs, under the automatic stay, from continuing the New York action. The recognition petition met all the requirements for recognition under chapter 15, but the New York plaintiffs argued that the court should deny recognition because the petition was filed in bad faith as a litigation tactic. Section 1506 permits the court to refuse to take an action that would be manifestly contrary to U.S. public policy. Courts generally do not apply this section to prohibit recognition where the debtor has engaged in bad faith. However, though the liquidators clearly sought recognition as a litigation strategy and their action might constitute bad faith under a different Bankruptcy Code chapter, in chapter 15, section 1506 does not examine whether the debtor's actions violate public policy but whether the foreign court's procedures and protections do not comport with U.S. public policy. Here, the Bermuda court's do, so the liquidators' motivation in filing the chapter 15 petition does not warrant denial of recognition. *In re Culligan Ltd.*, 2021 Bankr. LEXIS 1783 (Bankr. S.D.N.Y. July 2, 2021).

# Recent Developments in Bankruptcy Law, October 2021

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## 1. AUTOMATIC STAY

### 1.1 Covered Activities

### 1.2 Effect of Stay

### 1.3 Remedies

## 2. AVOIDING POWERS

### 2.1 Fraudulent Transfers

2.1.a **Trustee may avoid transfer as actual fraudulent transfer only if ultimate decision-maker has fraudulent intent.** Before entering into a two-step LBO transaction, the debtor formed a special board committee of independent directors, which hired professional advisers. Each step required separate financing. It sought solvency opinions for each step of the transaction. The opinions were based on management projections, but before the issuance of the first opinion, management had concluded the company would not make the projections, yet the opining firm was not advised of this new information. The transaction's first step closed using borrowed money, and major shareholders, who were represented on the board, sold their shares. Before the second step, management revised its projections again. The opining firm, based on management misrepresentations, ultimately issued a second solvency opinion. Although two other advisers did not agree with the opinion, they did not try to stop the transaction, which then closed. The company failed one year later. The liquidating trustee sued to avoid the transactions as actual fraudulent transfers. A corporation can act only through individuals; state law determines who has authority to act for the corporation—in this case, the board of directors—which delegated its authority to the special committee. Actual fraudulent intent can be established only through the intent of the individuals who have the authority to control the transfer. Here, the management projections may have misled the special committee and the advisers, but there was no allegation that the board itself intended to hinder, delay, or defraud creditors. Moreover, it is "unreasonable to assume actual fraudulent intent whenever the members of a board [stand] to profit from a transaction they recommended or approved." Therefore, the complaint fails to allege actual fraudulent intent adequately, and the court dismisses the complaint. *In re Tribune Co. Fraudulent Conveyance Litigation*, 10 F. 4th 147 (2d Cir. 2021).

### 2.2 Preferences

2.2.a **Critical vendor order does not vitiate preference liability.** Early in the chapter 11 case, the debtor in possession was authorized but not required to pay certain amounts to critical customers to be able to continue to receive necessary services from the customers. The liquidating trustee under the confirmed chapter 11 plan sued one customer to avoid and recover a preference. The customer order does not vitiate the trustee's preference claim. The debtor made the payments before the customer order and so, absent specific protection, could not have been protected by authorization to make future payments. Moreover, the order was permissive, not mandatory, and did not specifically identify the customer or require that its claims be paid. Therefore, the order does not protect the prepetition payments from preference attack. *Insys Liquidation Trust v. McKesson Corp. (In re Insys Therapeutics, Inc.)*, ___ B.R. ___, 2021 Bankr. LEXIS 1923 (Bankr. D. Del. July 21, 2021).

### 2.3 Postpetition Transfers

### 2.4 Setoff

### 2.5 Statutory Liens

### 2.6 Strong-arm Power

2.6.a **Trustee may not avoid unrecorded mortgage that does not transfer an interest in property.** The bank failed to record the Puerto Rico mortgage. Under Puerto Rico law, recording a mortgage is a "constitutive act," and an unrecorded mortgage does not transfer any interest in the mortgaged property but gives the mortgagee only an unsecured claim. Under section 544(a)(3), a trustee may avoid "a transfer of property of the debtor … that is voidable" by a bona fide purchaser. Because the failure to record the mortgage prevented the transfer of any interest in the property, there was no transfer for the trustee to avoid. The court does not address the consequence, which would appear to be that the real property becomes unencumbered property of the estate, the same as if the mortgage had been avoided. *Miranda v. Banco Popular de Puerto Rico (In re Lopez Cancel)*, 7 F.4th 23 (1st Cir. 2021).

### 2.7 Recovery

2.7.a **Good faith under sections 548(c) and 550(b)(1) is measured by an inquiry notice standard.** The broker-dealer debtor ran a Ponzi scheme and was liquidated under the Securities Investor Protection Act. The SIPA trustee sued under section 550(a) to recover customer property from subsequent transferees of the debtor's account holders who withdrew funds within two years before the liquidation. A SIPA trustee has the same avoiding powers as a bankruptcy trustee. Section 550(a) authorizes the trustee to recover an avoided transfer from the initial transferee or from subsequent transferees, but section 550(b) prohibits a trustee from recovering from a subsequent transferee who took for value, in good faith, and without knowledge of the voidability of the transfer. "Good faith" is based on inquiry notice, that is, what the transferee should have known, even in a SIPA stockbroker case. However, the test is not purely objective or a negligence standard. "[W]hat the transferee should have known depends on what it actually knew, and not what it was charged with knowing on a theory of constructive notice." The test requires a three-step analysis: what did the transferee actually know; do those "facts put the transferee on inquiry notice of the fraudulent purpose behind a transaction—that is, whether the facts … would have led a reasonable person in the transferee's position to conduct further inquiry into possible fraud," and if so, whether "diligent inquiry would have discovered the fraudulent purpose." *Picard v. Citibank, N.A. (In re Bernard L. Madoff Inv. Secs. LLC)*, 12 F.4th 171 (2d Cir. 2021).

## 3. BANKRUPTCY RULES

3.1.a **Bankruptcy Rule 3002.1 does not authorize punitive sanctions.** The mortgagee added additional charges to the debtor's account statement without compliance with Bankruptcy Rule 2002.1, which requires a mortgagee to provide notice of any such charges to the trustee and the debtor. The mortgagee ignored the trustee's requests to delete the charges, after which the trustee brought a motion for contempt and sanctions. The mortgagee then removed the charges and opposed the sanctions motion. Rule 3002.1 provides remedies for noncompliance. If the creditor fails to give the required notice, the court may preclude the creditor from presenting evidence in support of the charge and "award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure." "Other appropriate relief" should be construed consistent with the other terms in the same provision. Expenses and fees are compensatory, suggesting that other relief is limited to non-punitive sanctions. *PHH Mortgage Corp. v. Sensenich (In re Gravel)*, 6 F.4th 503 (2d Cir. 2021).

3.1.b **Bankruptcy Rules apply in a related-to action in the district court.** A tort plaintiff sued a defendant that it claimed was responsible with the debtor for the plaintiff's injuries. The state court action was removed to federal district court on the ground that it was related to the debtor's bankruptcy case and transferred to the district where the debtor's case was pending. Among other reasons, because the case was a personal injury tort claim, the district court did not refer it to the bankruptcy court. The defendant moved to dismiss on jurisdictional grounds. The court granted the motion. The plaintiff moved for reconsideration 28 days later. The court denied

reconsideration, and the plaintiff appealed. Bankruptcy Rule 1001 provides that the Rules "govern procedure in cases under title 11." Although the phrase is ambiguous as to whether it includes related-to proceedings, practicalities require it to be read that way. Otherwise, a district court handling both core and non-core proceedings in a single case would have to apply two different sets of Rules. Bankruptcy Rule 9023 requires that a motion for reconsideration be filed within 14 days after the order or judgment. It applies here. Therefore, the filing 28 days after the order was late. Under Rule 9023, a timely-filed motion tolls the time period for filing a notice of appeal. Because the motion did not toll the time period for filing a notice of appeal, the notice of appeal was late, and the court of appeals lacks jurisdiction to hear it. *Roy v. Canadian Pac. Ry. Co. (In re Lac-Mégantic Derailment Litig.)*, 999 F.3d 72 (1st Cir. 2021).

3.1.c **Email service of a bar date notice is not adequate.** The claims agent mailed the bar date notice to the creditor's address shown on the schedules, which the parties stipulated was not the creditor's last known address. It also emailed the notice to the creditor's email address, which the creditor regularly used, including for communications relating to the case. The parties stipulated that the creditor did not receive the mail notice, and the creditor claimed he did not see the email notice. Due process requires at a minimum notice reasonably calculated to inform. While due process is necessary, it might not be sufficient. Bankruptcy Rule 2002(a)(7) requires that notice of a bar date be sent by mail. Because the parties stipulated that the address to which the notice was sent was not the creditor's last known address, the notice did not comply with Rule 2002(a)(7). Bankruptcy Rule 9005 incorporates Fed. R. Civ. P. 61, which requires the court to disregard errors and defects that do not affect substantial rights—the harmless error doctrine. To show harmless error here in the absence of properly mailed notice, the debtor would have to show the creditor had actual knowledge of the bar date. Because the debtor could not show that, the court denies the bar date objection to the claim. *In re Cyber Litigation Inc.*, ___ B.R. ___ (Bankr. D. Del. Oct. 21, 2021).

## 4. CASE COMMENCEMENT AND ELIGIBILITY

### 4.1 Eligibility

4.1.a **Subchapter V eligibility does not require business operations, only activities.** The debtor ceased operations in October 2020 and filed a subchapter V petition in April 2021 to liquidate assets valued at about $300,000 and disburse sale proceeds to creditors. At the filing date, the debtor maintained business bank accounts, had accounts receivable, worked with insurance adjusters and insurers to address prepetition insurance claims, and was preparing assets for sale. Subchapter V eligibility is limited to a "person engaged in commercial or business activities." "Engaged" is tested as of the petition date. "Commercial or business" means dealings or transaction of an economic nature. "Activities" requires behavior, actions, or acts. Under these definitions, the debtor's conduct on the petition date included commercial or business activities and is therefore eligible for subchapter V. Operations are not required. *In re Vertical Mac Construction, LLC*, ___ B.R. ___ (Bankr. M.D. Fla. July 23, 2021); *accord In re Blue*, 630 B.R. 179 (M.D.N. Car. 2021).

4.1.b **Debtor's eligibility is determined based on its law of formation.** A REIT formed in Singapore under Singapore law filed a chapter 11 case. Only a person is eligible to file a chapter 11 case. "Person" is defined to include a business trust. Under the principles of *Butner v. United* States, bankruptcy courts should apply nonbankruptcy law unless there is a bankruptcy-based reason for not doing so. Thus, determination of whether an entity is a business trust that is a qualified debtor should be based on the entity's law of formation, not on federal common law. Breaking with the majority of courts to address this issue, the court looks to Singapore law to determine the debtor's status as a business trust and its eligibility for chapter 11. *In re Eht Us1*, 630 B.R. 410 (Bankr. D. Del. 2021).

### 4.2 Involuntary Petitions

4.2.a **Official Form 105 contains adequate allegations to withstand a motion to dismiss.** The petitioning creditor filed an involuntary petition using Official Form 105, checking the boxes on that form to allege the debtor is eligible for involuntary relief, the creditor is eligible to file the petition, and the debtor is generally not paying his debts as they become due, unless subject to a bona fide dispute as to liability or amount. In response to an additional question on the form, the petitioner also listed the amount of the petitioner's claim and asserted it was matured and unpaid. A debtor may respond to an involuntary petition with a motion to dismiss for failure to state a claim under Rule 12(b)(6). Rule 9009(a) requires that Official Forms be used without alteration, which establishes the legal sufficiency of the form. Therefore, absent some defect in use of the form or in the information provided with the form, the court should deny a motion to dismiss under Rule 12(b)(6). The better approach is to hold a prompt trial on the merits. *In re Haymond*, ___ B.R. ___ (Bankr. S.D. Tex. Sept. 28, 2021).

### 4.3 Dismissal

## 5. CHAPTER 11

### 5.1 Officers and Administration

5.1.a **Court permits structured dismissal.** The debtor in possession sold all its assets and had a pot of cash and some administrative claims, as well as its general unsecured claims. However, it did not have enough to pay all administrative claims and the cost of preparing, soliciting, and confirming a plan. It moved for a dismissal, contingent upon payment of all administrative claims (including US trustee fees) and a small payment on unsecured claims, with the court retaining jurisdiction over a pending adversary proceeding and an exception to the default rule in section 349 so that all orders issued during the case would remain in force. Section 349 permits dismissal of a case and provides that unless the court orders otherwise, dismissal vacates all orders entered during the case, among other things. Although the Supreme Court limited structured dismissals in *Czyzewski v. Jevic Holding Corp. (In re Jevic Holding Corp.)*, 137 S. Ct. 973, 197 L. Ed. 2d 398 (2017), where the dismissal violated bankruptcy priorities, it did not prohibit them. Because the estate has limited remaining assets and no real alternatives, a structured dismissal is appropriate. The court has discretion to permit retention of jurisdiction of an adversary proceeding, which it does here, and to leave orders entered during the case in place, so as, among other things, to preserve the sale authorization. *In re KG Winddown, LLC*, 628 B.R. 739 (Bankr. S.D.N.Y. 2021).

5.1.b **Court subordinates to general unsecured claims an unauthorized postpetition loan.** During its chapter 11 case, without court approval under section 364, the debtor borrowed from an insider to acquire real property. The lender asserted an administrative claim for the loan amount. Section 503(b) allows claims for actual amounts necessary to the preservation of the estate and grants them priority over prepetition claims. Section 364 permits the court to authorize postpetition loans with administrative expense priority. Failure to obtain prior approval defeats a claim for administrative expense priority. Section 503(b)(3) allows an administrative expenses claim of a creditor and certain other specified entities for making a substantial contribution to the case. An insider lender is not among the specified entities and so may not rely on the substantial contribution provision. A court may grant administrative expense priority to an unauthorized postpetition loan on equitable principles. To do so, the court must find that the court would have granted approval of the loan before it was made, the loan would not impair creditor interests, and the property acquired with the loan proceeds would provide a substantial distribution to creditors, all measured as of the time the loan was made. None of those factors was present here. Therefore, the court denies administrative expense priority to the loan. The court may disallow the claim in its entirety, but here, the court allowed it and subordinated it to the claims of general unsecured creditors based on the insider's inequitable conduct. *Norcross Hospitality, LLC v. Glass (In re Nilhan Devs., LLC)*, ___ B.R. ___ (N.D. Ga. Sept. 30, 2021).

**5.2 Exclusivity**

**5.3 Classification**

**5.4 Disclosure Statement and Voting**

**5.5 Confirmation, Absolute Priority**

## 6. CLAIMS AND PRIORITIES

### 6.1 Claims

6.1.a **Court may set bar date for, and plan may discharge, claims arising between confirmation and effective date.** The debtor confirmed a chapter 11 plan, which provided for discharge of all claims arising before the effective date. In the long period between confirmation and the effective date, the debtor in possession discharged an employee, who sued for age discrimination in federal court after the effective date. The employee had notice of the general bar date and the administrative claims bar date, which was 30 days after the effective date, but did not file a proof of claim or request for payment of an administrative expense. Section 503(b) provides that the actual, necessary expenses of preserving the estate are administrative expenses, which are entitled to priority. The estate lasts until the plan effective date, so claims arising between confirmation and the effective date may qualify as administrative expenses. Although a tort or similar claim is not necessary to preserving the estate, *Reading Co. v. Brown*, 391 U.S. 471 (1968), held that such claims are administrative expenses. By referring to timely filed claims, section 503 authorizes the bankruptcy court to set a bar date for the filing of requests for payment of administrative expenses and to bar unfiled claims from sharing in any distribution under a plan. Section 1141(d) discharges all claims that arose before confirmation, except as otherwise provided in the plan. The plan may modify not only the kinds of claims excepted from discharge, but also the effective date of the discharge. Therefore, the unfiled employment discrimination claim was barred by the bar date and discharged by the plan. *Ellis v. Westinghouse Electric Co., LLC*, 11 F.4th 221 (3d Cir. 2021).

6.1.b **Guaranteed creditor may waive setoff rights before guarantor pays creditor in full.** The debtor owed the United States, supported by a surety bond, and was entitled to a tax refund from the United States. The United States and the trustee settled: the United States' claim was allowed, and the United States waived the right to offset the tax refund. The surety had acknowledged its obligation to pay the United States but had not yet completed payment by the time the United States and the trustee settled. As subrogee to the debtor's rights against the United States, the surety claimed the right to the tax refund, which the United States had waived in the settlement. Section 509 subrogates a surety to the creditor's rights to the extent of payment but subordinates the surety's claim to the principal creditor's claim until the creditor's claim is paid in full. Because the surety had not paid the United States in full by the time of the settlement, its rights were subordinated, and the United States could use its setoff rights to protect its own interests without the surety's approval. *Giuliano v. Ins. Co. of Penn. (In re LTC Holdings, Inc.)*, 10 F.4th 177 (3d Cir. 2021).

### 6.2 Priorities

6.2.a **Employee benefit priority applies separately to multiple employee benefit plans.** Under a collective bargaining agreement, the debtor funded three employee benefit plans. When the debtor filed bankruptcy, each of the plans filed a proof of claim. Section 507(a)(6) grants priority to a claim of an employee benefit plan for services rendered within 180 days before the petition date "for each such plan, to the extent of the number of employees covered by each such plan multiplied by $12,850." Because the statute uses the term "each such plan," the priority amount is set separately for each plan. The plans are not required to share the priority. *Algozine Masonry Restoration, Inc. v. Local 52 (In re Algozine Masonry Restoration, Inc.)*, 5 F.4th 827 (7th. Cir. 2021).

## 7. CRIMES

## 8. DISCHARGE

### 8.1 General

8.1.a **Section 523(a) exceptions to discharge do not apply to a nonconsensual subchapter V plan.** The creditor obtained a prepetition judgment against the corporate subchapter V debtor, which the creditor sought to except from discharge. Section 523(a) excepts certain debts from the discharge of an individual debtor under section 1192. Section 1192(2) excepts from discharge under a nonconsensual subchapter V plan any debt "of the kind specified in section 523(a)." The reference to section 1192 in section 523(a) means that the limitation of the exceptions to discharge in section 523(a) applies to individual debtors and that the exceptions do not apply to a corporate debtor. *Cantell-Cleary Co. v. Cleary Packaging LLC (In re Cleary Packaging LLC)*, 630 B.R. 466 (Bankr. D. Md. 2021).

8.1.b **Signing of guaranty creates dischargeable contingent debt.** The debtor personally guaranteed his company's debts to a supplier. He did not list the supplier as a creditor in his schedules. After his no-asset bankruptcy and discharge, his company continued to purchase from the guaranteed supplier but later failed to pay the supplier for those purchases. A discharge applies to all debts that arose prepetition. Under controlling circuit precedent, when a debt arises is based on the conduct test, not the state-law focused accrual test. Conduct is measured by the existence of a prepetition relationship. Here, the signing of the guarantee, rather than the making of the guaranteed loan, established the relationship and was the conduct under which the contingent claim arose, so the claim was potentially dischargeable. However, under section 523(a)(3)(A), the claim of a creditor who did not receive timely notice of the bankruptcy is not discharged, except in a no-asset case. Therefore, the lack of notice to the supplier does not except the debt from discharge. *Reinhart FoodService L.L.C. v. Schlundt (In re Schlundt)*, ___ B.R. ___, 2021 Bankr. LEXIS 2577 (Bankr. E.D. Wis. Aug. 19, 2021).

### 8.2 Third-Party Releases

### 8.3 Environmental and Mass Tort Liabilities

8.3.a **CERCLA response cost claim arises when the debtor deposited waste.** The debtor contributed waste to a hazardous waste site in the 1950s and 1960s. It filed chapter 11 in 1992 and confirmed a plan, which provided for discharge of all claims that arose before the effective date. In 2017, the EPA issued a decision and decree for remedial action at the site against a group of settling defendants. The settling defendants brought an action for contribution against potentially responsible parties, including the debtor. A claim for contribution lies only when the plaintiff and the defendant are both liable on the same claim, in this case, to the United States. If the United States' claim against the debtor arose before the plan effective date, it was discharged, and a contribution claim would not lie. Under the "underlying acts" approach the Fourth Circuit has adopted, a claim arises when the acts underlying the claim occurred. Here, the underlying acts were the deposit of waste in the hazardous waste site in the 1950s and 1960s. The claim arose then, which was before the plan's effective date, and therefore was discharged. *68thSt. Site Work Group v. Airgas, Inc.*, ___ B.R. ___, 2021 U.S. Dist. LEXIS 199088 (D. Md. Oct. 15, 2021).

## 9. EXECUTORY CONTRACTS

9.1.a **Remaining covenants that do not go to a contract's essence do not make the contract executory.** The debtor contracted with a movie producer to produce a film, which the producer did. The contract provided for contingent consideration based on the film's profits over time. However, the debtor was not obligated to pay the contingent compensation if the producer was in

breach of its continuing obligations not to interfere with the debtor's intellectual property in the film, indemnify the debtor for breach of reps and warranties, and limit assignment of the contract. Six years later, the debtor filed a chapter 11 petition. Under its plan, it sold its business, including the contract with the producer, to a buyer, who refused to pay the producer any arrearages owing under the contract. An executory contract is one under which a party's material breach would excuse the other party's remaining performance. If a party has substantially performed the essence of the contract, that party's future breach is not material. Here, the producer substantially performed the contract obligations by producing and delivering the film. Although the parties can contract around the rule by designating certain obligations as material and providing for termination upon breach, the producer's remaining obligations did not go to the essence of the contract, and their breach would not excuse the debtor's remaining performance. They were merely covenants or conditions precedent to continued payment of contingent consideration. Therefore, the contract was not executory, and the buyer was not required to cure the unpaid prepetition amounts the debtor owed. *Spyglass Media Grp., LLC v. Bruce Cohen Prods. (In re Weinstein Co. Holdings, LLC)*, 997 F.3d 497 (3d Cir. 2021).

9.1.b **A surety bond is not an executory contract.** Before bankruptcy, the debtor obtained surety bonds to guarantee performance of its obligations to mineral rights lessors. The surety's obligations to the lessors were irrevocable, but once it issued the bonds, it had no further obligations to the debtor. In connection with obtaining the bonds, the debtor entered into indemnification agreements with the surety, obligating the debtor to pay the surety or provide collateral under certain circumstances. Under its chapter 11 plan, the debtor assumed all contracts not rejected. The surety bonds were not among the contracts listed for rejection. After the effective date, the reorganized debtor defaulted on some of the leases, the lessors demanded payment from the surety, and the surety demanded the reorganized debtor reimburse it or post collateral. An executory contract is one under which "performance remains due to some extent on both sides and … if the failure of either party to complete performance would constitute a material breach." Here, the surety had no remaining performance obligation to the debtor, and because the bonds are irrevocable, the debtor's failure to perform under the indemnity agreement would not constitute a breach excusing the surety's performance to the lessors. Therefore, the contract is not executory, it was not assumed under the plan, and the surety may not enforce any obligations under the indemnity agreement against the reorganized debtor. *Argonaut Ins. Co. v. Falcon V, L.L.C.*, ___ B.R. ___, 2021 U.S. Dist. LEXIS 188686 (M.D. La. Sept. 29, 2021).

9.1.c **Court order enforcing contract makes the contract not executory.** The debtor contracted to sell a liquor license. The sale required city council approval, which the contract required the debtor to request. The buyer put the purchase price in escrow, to be released on closing. The debtor breached. The buyer obtained a state court order requiring the debtor to cooperate with the buyer in obtaining approval, make the request to the council, and close the sale upon approval. The debtor made the request but filed a chapter 11 petition three days before the approval hearing and moved for approval to reject the contract. A contract is executory if performance remains on both sides, failure of which would constitute a material breach that would relieve the other party of further performance. When a court orders performance of a contract, any remaining performance obligation of the party is ministerial, because the court may enforce the order and cause the performance. Therefore, a contract obligation that has been reduced to judgment is no longer executory. In addition, applying a purchase price to a contract where the only remaining contingency to doing so is not within the parties' control is a ministerial act. Therefore, the contract itself, regardless of the court order, is not executory. The court denies the rejection motion. *In re Bennett Enters.*, 628 B.R. 481 (Bankr. D.N.J. 2021).

9.1.d **Rejection terminates granted rights that are useful solely in contract performance.** The debtor contracted with a pipeline company to use a pipeline the company was constructing to deliver oil and gas to a collection point. Under the contract, the debtor exclusively dedicated, granted, and committed to the performance of the contract all the debtor's interests in specified mineral leases, all gas and water produced or delivered from the leases, and all the debtor's future interests in certain wells, and agreed not to deliver any gas from those properties to any

other pipeline company. Upon filing chapter 11, the debtor in possession moved for court approval to reject the contract. The pipeline company claimed the dedication survived rejection. Under *Mission Product Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 1652 (2019), rejection operates only as a breach and not as a rescission or avoiding power that allows a debtor in possession to recapture rights already granted to the contract counterparty. Here, the contract counterparty cannot use the dedicated and granted rights unless the debtor continues to perform under the contract. Rejection relieves the debtor of future performance, rendering the dedicated rights useless to the counterparty, except as a way to enforce the contract's exclusivity provision, which rejection relieves the debtor from performing. Therefore, the counterparty may not retain the dedicated and granted interests after rejection. *Caliber N. Dak., LLC v. Nine Point Energy Holdings, Inc. (Nine Point Energy Holdings, Inc.)*, ___ B.R. ___ (D. Del. July 30, 2021).

## 10. INDIVIDUAL DEBTORS

### 10.1 Chapter 13

### 10.2 Dischargeability

### 10.3 Exemptions

### 10.4 Reaffirmations and Redemption

## 11. JURISDICTION AND POWERS OF THE COURT

### 11.1 Jurisdiction

### 11.2 Sanctions

### 11.3 Appeals

11.3.a **Eighth Circuit severely limits equitable mootness doctrine.** The preferred shareholder appealed the chapter 11 confirmation order. Before the appeal was heard, the plan sponsor funded the plan, all equity interests were canceled, the secured creditor received payment, unsecured creditors received partial payment, and the plan sponsor released its DIP financing claim and a prepetition claim. The equitable mootness doctrine is based on common sense or equitable considerations to justify declining to decide a case on the merits. In a case of first impression, the Eighth Circuit declines to adopt a specific multi-factor test, deferring instead to whether the court can grant effective relief without undermining the plan and thereby affecting third parties. Most important are whether the plan has been substantially consummated and what effects reversal might have on third parties. Seeking or obtaining a stay is not determinative. Therefore, the appellate court must undertake a preliminary review of the merits to determine the strength of the appeal and the time required to resolve it, as well as of the remedies available, so as not to undermine the plan and harm third parties. Therefore, dismissal for equitable mootness should be extremely rare. Here, because the district court did not undertake this review, the court of appeals remands, noting that the plan sponsor and the supportive secured creditors are not true third parties the doctrine is meant to protect. *FishDish, LLP v. VeroBlue Farms USA, Inc. (In re VeroBlue Farms USA, Inc.)*, 6 F.4th 880 (8th Cir. 2021).

11.3.b **Rule 8002 time limit is mandatory but not jurisdictional.** The court overruled a preferred shareholder's objection to the secured creditor's claim. The shareholder appealed 18 days after the order. Rule 8002 requires that a notice of appeal be filed "within 14 days after entry of the judgment, order, or decree being appealed." Section 158(a) of title 28 permits appeals of final judgments and of interlocutory orders. Section 158(c)(2) requires an appeal under subsection (a) to be taken "in the time provided by Rule 8002 of the Bankruptcy Rules." Only a statute may specify a court's jurisdiction. Because the Rules may be amended without Congressional action to change the time period for filing a notice of appeal, the Rule is not jurisdictional, despite the reference to the Rule in the statute. However, the deadline is mandatory, and the court dismisses

the appeal. *FishDish, LLP v. VeroBlue Farms USA, Inc. (In re VeroBlue Farms USA, Inc.)*, 6 F.4th 880 (8th Cir. 2021).

11.3.c **Chapter 13 dismissal moots appeal from order directing funds disbursement.** The court ordered the chapter 13 trustee to disburse to the secured lender insurance proceeds resulting from damage to the chapter 13 debtor's house. The debtor moved to dismiss her case, which the court granted. The debtor appealed the disbursement order. An appeal is jurisdictionally moot when the case or controversy it concerns is no longer live. Section 349(b)(3) provides that property of the estate revests in the entity in which the property was vested immediately before the petition. Once the trustee disbursed the funds, they were no longer property of the estate, and section 349(b)(3) does not authorize the court to recover funds that were already disbursed. Therefore, the court may not grant relief, and the appeal is moot. *Sundaram v. Briry, LLC (In re Sundaram)*, 9 F.4th 16 (1st Cir. 2021).

### 11.4 Sovereign Immunity

## 12. PROPERTY OF THE ESTATE

### 12.1 Property of the Estate

12.1.a **Court explains proper disposition of unclaimed creditor distribution.** The bank failed to record the mortgage but filed a proof of claim. The trustee avoided the unrecorded mortgage and sold the real property. The trustee issued a check to the mortgagee, but the mortgagee never cashed it. After 90 days, the trustee stopped payment under section 347(a) and deposited the funds into court. After five years, the clerk, under 28 U.S.C. 2041, deposited the funds with the U.S. Treasurer in the name and to the credit of the court. The debtor then sought recovery of the unclaimed funds. In a status of custodial escheat, the funds are not abandoned property under section 554 and remain property of the estate. Section 2041 provides that moneys paid into court may be paid to "the rightful owners." Section 2042 prohibits money deposited under section 2041 to be withdrawn except by court order and permits payment to a claimant "entitled thereto" upon "full proof of the right thereto." Although the funds remained property of the estate, the mortgagee is not deemed to have abandoned its claim. The survival of the mortgagee's claim prevents the case from being a surplus case, with funds being paid to the debtor under section 726(a)(6). Therefore, upon the mortgagee's proper proof of entitlement to the funds, the trustee will be required to pay them to the mortgagee. *In re Pickett*, ___ B.R. ___, 2021 Bankr. LEXIS 2203 (Bankr. E.D. Cal. Aug. 11, 2021).

12.1.b **Bank may force management change if authorized under the loan agreement.** The debtor defaulted on its loans. The bank agreed to amendments, but required a personal guarantee from the principal and the installation of a CRO. After further defaults, the debtor and guarantor handed the CRO full authority over the business. Yet the borrowers remained in default. A forbearance agreement then reaffirmed the validity of the debt, confirmed there were no valid defenses to enforcement, and waived all claims against the bank. After still more defaults, the lenders accelerated and foreclosed and called the guaranty. Ratification recognizes a contract as valid, having knowledge of all relevant facts. A guaranty that has been ratified cannot be avoided due to duress or fraudulent inducement. Duress exists only upon a threat to do something without a legal right, an illegal exaction or fraud, and an imminent restraint that destroys fee agency. The bank had the right to take action, including demanding management change, under the loan agreements, the amendments, and the forbearance agreement. Therefore, it did not act illegally in exercising its leverage and in enforcing the guarantee. *Lockwood Int'l, Inc. v. Wells Fargo, N.A.*, ___ Fed. Appx. ___, 2021 U.S. App. LEXIS 24385 (5th Cir. Aug. 16, 2021).

### 12.2 Turnover

### 12.3 Sales

## 13. TRUSTEES, COMMITTEES, AND PROFESSIONALS

### 13.1 Trustees

### 13.2 Attorneys

### 13.3 Committees

### 13.4 Other Professionals

### 13.5 United States Trustee

13.5.a **2018 U.S. Trustee fee increase is unconstitutional as applied to then-pending chapter 11 cases.** The debtors filed their cases in 2016. In 2017, Congress amended section 1930(a) of title 28, which governs U.S. trustee fees for chapter 11 cases, to increase the fees effective January 2018 for each case for disbursements made in each quarter after the effective date. The fee increase did not apply in Bankruptcy Administrator districts, where chapter 11 fees are set by the Judicial Conference under a statute that then authorized, but did not require, that the Judicial Conference set BA district fees to be equal to UST district fees. Courts apply a presumption against retroactive application of a new statute to avoid notice and other issues, first determining what the statute expressly provides and second whether the statute would impair a party's rights, increase liability for past conduct, or impose new duties regarding completed transactions. If it would, then the statute would not apply retroactively unless it expressly provided otherwise. Here, the statute is sufficiently clear that it applies to disbursements in each quarter starting in January 2018, without excluding pending cases, and so applies to the debtors' cases. Moreover, it applies only to post-enactment disbursements, so it does not apply to past conduct or completed transactions. The Constitution authorizes Congress to enact "uniform Laws on the subject of Bankruptcies throughout the United States," which requires geographic uniformity. Because the statute imposes a fee that estates must pay before paying creditors and therefore affects the relation between a debtor and its creditors, it is a law on the subject of bankruptcies. Uniformity requires that a bankruptcy law apply uniformly to a defined class of debtors, not based on their geographic location. The fee increase applies based on location and therefore violates the Uniformity Clause. *John Q. Hammons Fall 2006, LLC v. U.S. Trustee (In re John Q. Hammons Fall 2006, LLC)*, ___ F.4th ___, 2021 U.S. App. LEXIS 29917 (10th Cir. Oct. 5, 2021).

## 14. TAXES

## 15. CHAPTER 15—CROSS-BORDER INSOLVENCIES

15.1.a **Section 109 does not limit Chapter 15 eligibility.** The individual foreign debtor had no property in the United States. The foreign liquidators filed a chapter 15 petition to investigate the debtor's affairs in the United States, to recover any property they discovered, and to bring claims against third parties. Section 109(a) provides that only an entity with a domicile, residence, place of business, or property in the United States may be a debtor under the Bankruptcy Code. Section 1517 requires a court to recognize a foreign representative if the foreign proceeding is a foreign main proceeding or a foreign nonmain proceeding (as defined), the foreign representative is a person or body, and the petition meets section 1515's requirements. Section 1517 is mandatory and does not cross-reference section 109. The definition of "debtor" in chapter 15 ("entity that is the subject of a foreign proceeding") differs from the definition for section 109 (person "concerning which a case under this title has been commenced"). Section 109 specifies eligibility requirements only for other chapters, not chapter 15, and contains other eligibility requirements, such as credit counseling, that could not apply in a chapter 15 case. Chapter 15 permits commencement of an ordinary bankruptcy case against the debtor if the debtor has assets in the United States, implying that having assets in the United States is not a chapter 15 eligibility requirement. These provisions, taken as a whole, show that section 109 does not limit chapter 15

eligibility. *In re Abdulmunem al Zawawi*, ___ B.R. ___, 2021 Bankr. LEXIS 2367 (Bankr. M.D. Fla. Aug. 30, 2021).

# CONSUMER LAW UPDATE

**Selected Cases reported**
**January 1 to March 31, 2022**

**Prepared for Federal Judicial Center**
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**Automatic Stay**

**Denial of stay relief was final and appealable, although it was "without prejudice."** Deciding an issue not addressed in *Ritzen Grp., Inc. v. Jackson Masonry, LLC,* 140 S.Ct. 582 (2020), the Ninth Circuit concluded that the bankruptcy court's order denying stay relief was final and appealable, despite its "without prejudice" language, because the bankruptcy court's denial "conclusively resolved the request for stay relief." The record in this case "makes it clear that the court 'unreservedly denied relief,'" and the "bankruptcy court's statement that the denial of stay relief was without prejudice indicates that the court was willing to consider stay relief if sought for a different purpose, but not for the purpose of resolving" the state court litigation at issue in the motion that was denied. Harrington v. Mayer (In re Mayer), 28 F.4th 67 (9th Cir. 2022).

**Automatic stay and domestic support obligations.** A post-petition hearing in the Family Court that modified and established an additional family support obligation was not a violation of the stay, falling under § 362(b)(2)(A)(ii)'s exception, but the Family Court's judgment of civil contempt had the purpose of compelling the debtor to pay pre-petition child support arrearages under threat of sanction, and that contempt judgment was a stay violation and void. The interception of state and federal tax refunds for payment of child support arrearages was not a stay violation, falling within § 362(b)(2)(F)'s exception. In re Dougherty-Kelsay, ___ B.R. ___, 2022 WL 830907 (B.A.P. 6th Cir. Mar. 21, 2022).

**Omitted creditor willfully violated stay be sending second invoice after learning of the bankruptcy filing.** Chapter 13 debtor had inadvertently omitted a medical creditor from schedules, but when the debtor received an invoice, debtor's counsel notified the creditor of the bankruptcy, with the schedules and plan amended to add the creditor. Although a second invoice was sent because of human or computer error, the creditor willfully violated the stay. After amendments of schedules, the creditor was receiving notices about the bankruptcy case, and it had the burden to ensure that it did not violate the stay. Section 362(k) does not contain a specific intent requirement, and the violation was willful. The actual damages were small, but the debtor was entitled to reasonable attorney fees, with the $17,500 requested fee reduced to $2,500. Punitive damages were

not appropriate. In re Defeo, ___ B.R. ___, 2022 WL 154489 (Bankr. D. S.C. Jan. 14, 2022), Judge Waites.

**Jurisdiction**

**Under "narrow" interpretation of "personal injury tort," bankruptcy court could hear claims for defamation and intentional infliction of emotional distress.** Tort claims were filed by pro se plaintiff, who was Chapter 7 debtor's estranged spouse. State-law actions were removed to Bankruptcy Court and issue was whether that Court could hear the litigation or whether District Court should withdraw reference. Bankruptcy Court entered recommendation adopting the "narrow" interpretation of a personal injury tort for purposes of 28 U.S.C. § 157(b)(5). Under that view such a tort "requires a trauma or bodily injury or psychiatric impairment beyond mere shame or humiliation." Under this interpretation, the plaintiff's claims of defamation and intentional infliction of emotional distress were not personal injury torts, and the bankruptcy court could litigate those claims, with the Court recommending against withdrawal of the reference. In re Byrnes, ___ B.R. ___, 2022 WL 816378 (Bankr. D. N.M. Mar. 11, 2022), Judge Thuma.

**Property of Estate and Exemptions**

**Roth IRAs are excluded from estate under federal law.** The Chapter 7 debtor claimed exemption in IRA and 401(k) accounts and asserted that the IRAs were excluded from the bankruptcy estate under section 541(c)(2), with the issue on appeal whether Roth IRAs were excluded. The Eleventh Circuit held that Roth IRAs met requirements for exclusion under federal law, because they qualified as beneficial interest in a trust and had restriction on transfer that was enforceable under applicable Georgia law. There was no reason why Roth IRAs should be treated differently from traditional IRAs in the context of exclusion from the bankruptcy estate. In re Hoffman, 22 F.4th 1341 (11th Cir. 2022).

**State-law public assistance exemptions include earned income tax credit and child tax credit.** In unpublished decision, the Ninth Circuit Bankruptcy Appellate Panel affirmed the bankruptcy court's conclusion that Washington's "public assistance" exemption included federal earned income tax credits and additional child tax credits. The opinion refers to similar statutes in other states that have been construed broadly to include such credits as exempt, and the Washington Supreme Court had held that

exemptions were to be liberally construed. In re Moreno, 2021 WL 6140115 (B.A.P. 9th Cir. Dec. 23, 2021).

**Trustee did not establish equitable estoppel to prevent debtor's amendment of schedules and exemption.** Finding that the Chapter 7 trustee was aware of the debtor's ownership interest in property and the debtor's position that the property was held in resulting trust for the debtor's nephew, the trustee did not establish required elements of equitable estoppel that would prevent the debtor from amending schedules and wild card exemption. "Equitable estoppel is not a substitute for bad faith," and *Law v. Siegel* prevents denial of exemptions or amended exemptions on grounds of bad faith. In re Rizal Juco Guevarra, ___ B.R. ___, 2022 WL 884595 (B.A.P. 9th Cir. Mar. 25, 2022).

**Burdens of proof on homestead exemption under state law.** In Chapter 7 case in which debtor claimed state-law homestead exemption that was subject to increase due to non-filing spouse's disability, the parties disagreed on the burden of proof when the trustee objected to the increased homestead. The opinion reviews *Raleigh v. Ill. Dept. of Revenue*, 530 U.S. 15 (2000), which looked to state law for the burden related to an objection to claim. The *Raleigh* Court stated that Congress could preempt state law in the Bankruptcy Code, but the burden related to exemption objections is found in Rule 4003(c), and this opinion discusses the authority, including *In re Tallerico,* 532 B.R. 774 (Bankr. E.D. Cal. 2015), on whether the Rule is invalid when a debtor claims exemptions under state law assigning the burden. For reasons discussed in the opinion, this Court "concludes that Fed. R. Bankr. P. Rule 4003(c) remains valid," with the burden placed on the objecting trustee. The Court upheld the increased homestead, based on the spouse's disability. In re Hammond, ___ B.R. ___, 2022 WL 796249 (Bankr. C.D. Cal. Mar. 16, 2022). Judge Houle.

**No homestead in property owned by LLC and exemption in SEP lost by prohibited transactions.** The Chapter 7 debtor was not entitled to Ohio homestead exemption in property owned by LLC, and the debtor's SEP IRA lost its tax-exempt status as a result of transactions prohibited by the Internal Revenue Code. Ohio Code's "good-faith savings provision does not affect the exemptibility of the SEP IRA." In re Villavicencio, 635 B.R. 486 (Bankr. S.D. Ohio 2022), Judge Hoffman.

**Tenancy by entirety survivorship interest subject to levy under state law.** Examining New Jersey law on tenancy by entirety, each party's individual interest in right of survivorship is subject to levy. As a result, the debtor's claim of exemption under § 522(b)(3)(B) failed. The opinion discusses other opinions on the issues. In re Weiss, ___ B.R. ___, 2022 WL 789445 (Bankr. D. N.J. Mar. 15, 2022), Judge Meisel.

**Discharge Issues**

**Section 523(a)(5) and arbitration of property interests for unmarried parties.** Parties who had previously been married, divorced, lived together without remarrying and subsequently separated disputed their property interests, including one parties' retirement savings. Their dispute was submitted to binding arbitration, with the arbitrator awarding to the woman half of the increased value in the man's retirement account during their cohabitation. There was an appeal in state court that the man lost, and he then filed Chapter 13, with the Bankruptcy Court finding the arbitration had awarded the woman an interest in property that could not be discharged, but the District Court reversed. The Seventh Circuit upheld the District Court, noting that because the parties were not married, the woman "could not secure relief through the familiar channels of divorce law;" she had sued in state court instead on "equitable theories of express or implied contract, unjust enrichment, and *quantum meruit*." The dispute in the bankruptcy was found to be "whether the arbitrator had awarded Anne a money judgment or an interest in property." The Circuit opinion found that "the better reading of the arbitration award is that it awarded Anne a money judgment, not a property interest." The opinion also noted that the arbitrator's award stated that the judgment would not be dischargeable in bankruptcy, but the arbitrator had no authority to determine that conclusively. The Circuit opinion observed that the closest exception to discharge would be § 523(a)(5), but it was not applicable because the parties had stipulated that this was not a domestic support obligation, "for good reason; as a non-spouse Anne does not meet the statutory requirements" under § 101(14A)'s definition of domestic support obligation for purposes of § 523(a)(5). Because this was a Chapter 13 case, § 523(a)(15) was not discussed in the Circuit's opinion. In re Harshaw, 26 F.4th 768 (7th Cir. 2022).

**Lump sum alimony and debts incurred in connection with divorce were nondischargeable under §§ 523(a)(5) or (a)(15).** Unpaid balance of agreed lump sum alimony was domestic support obligation under § 523(a)(5), and employee severance owed to former spouse by debtor's business was incurred in course of divorce and therefore covered by § 523(a)(15). Although the debtor's business was the primary obligor for the severance, the debtor agreed that he was responsible for the debt if the business failed to pay. The former spouse's employment was terminated due to the divorce and the debtor's personal liability arose directly from the divorce. Section 523(a)(15) also covered obligations to pay the former spouse's cell phone charges and health insurance premiums. In re Burkhalter, 635 B.R. 284 (Bankr. N.D. Miss. 2022), Judge Woodard. See also In re Kalsi, ___ B.R. ___, 2022 WL 620033 (Bankr. S.D. N.Y. Mar. 3, 2022) (In Chapter 7 case, domestic support obligations were nondischargeable to extent not paid as priority for estate distributions, and state-court equitable distribution awards were excepted from discharge under § 523(a)(15) but they were not priority claims.).

**Cost of attorney disciplinary proceeding was penalty under § 523(a)(7).** Cost of the attorney debtor's pre-bankruptcy disciplinary proceedings, under the Wisconsin Supreme Court's cost order, was a "penalty" within the scope of § 523(a)(7), rather than "compensation for actual pecuniary loss." The costs were excepted from discharge. Attorney discipline "uniquely requires 'a finding of misconduct,'" and the cost order falls within the type that *Kelly v. Robinson,* 479 U.S. 36 (1986), identified as "punitive rather than compensatory." Osicka v. Office of Lawyer Regulation, 25 F.4th 501 (7th Cir. 2022).

**Partial student loan discharge.** Applying the *Brunner* standard, as adopted in the Tenth Circuit, there is authority to grant partial discharge of student loan debt to the extent the portion being discharged imposed undue hardship. This Chapter 7 debtor satisfied the three prongs of *Brunner* for the total debt exceeding $225,000, with the nondischargeable amount apportioned among three loans, and the nondischargeable amount will not bear interest. In re Loyle, ___ B.R. ___, 2022 WL 567724 (Bankr. D. Kan. Feb 24, 2022), Judge Herren.

**Chapter 7 Issues**

**Attorneys**

**Bifurcated fees approved by District Court as not violating local bankruptcy rule on continued representation.** In Chapter 7 cases in the District of South Carolina the debtors' attorney offered two payment options: prepayment of fees before filing the case or bifurcated fee agreements. Under the later, the engagement was split between pre-petition and post-petition services, with the clients then having the option to enter into post-filing fee agreements within ten days after the case was filed. The debtors were given other options of representing themselves post-filing or engaging other counsel if they chose not to enter into the post-filing agreements. The fee agreements specified pre-filing and post-filing services. If the debtor chose to pay in full before filing, the fixed fee was $2,350, including filing fee, but with potential hourly rates post-petition for specific services. If the debtor chose the bifurcated agreement, financing was through a third party, which charged fee for the service. The United States Trustee asserted that the bifurcated fee arrangements violated a local rule, and the Bankruptcy Court agreed. On appeal the District Court referred to the Eighth Circuit Bankruptcy Appellate Panel's comment that bifurcated fee agreements "are designed to change the attorney's fees into a post-petition, non-dischargeable debt that can be collected from the client without violating either the automatic stay or the discharge injunction," citing *In re Allen,* 628 B.R. 641, 644 (B.A.P. 8th Circ. 2021). Such bifurcated fee agreements require adequate disclosure about payments, and they must comply with state rules of professional conduct and any relevant local rules. The Bankruptcy Court had determined that its local rule required continued representation by the attorney throughout the case, and such a requirement did not permit bifurcated fee agreements that could lead to the filing attorney's withdrawal after filing. The District Court reviewed recent opinions from other courts and found no binding authority that bifurcated fee agreements were prohibited as a matter of law. Then, the Court found that such agreements did not violate that District's local bankruptcy rule, with the debtors' attorney agreeing that he was the attorney of record until the Bankruptcy Court allowed withdrawal. In the cases on appeal, the filing attorney did not attempt withdrawal, and the debtors were satisfied with the attorney's services and with the bifurcated fee arrangements. The Bankruptcy Court had not made

findings on the reasonableness of the attorney fees or other related matters; therefore, those issues were not before the District Court, which reversed on the basis that the fee agreements were not violative of the local rule but remanded for other determinations. In re Prophet, et al., 2022 WL 766390 (D. S.C. March 14, 2022).

**Trustee's attorney may only be compensated for legal services under § 330.** The Chapter 7 debtor appealed from order requiring debtor to compensate trustee's law firm for services performed on behalf of the trustee, and Fifth Circuit held that § 330(a) only allowed attorney compensation for services that required legal expertise and not for administrative services that were ordinarily performed by the trustee without attorney assistance. The law firm failed to carry the burden of showing that all its services were justified under the Code. In Matter of Sylvester, 23 F.4th 543 (5th Cir. 2022).

**Reopening closed case**

**Approaches to amending schedules after reopening.** The Chapter 7 debtor moved to reopen closed case to amend Schedule C exemptions and avoid judicial liens under § 522(f), and the Court explored whether there was "cause" to reopen under § 350(b) and amend schedules after a case has been closed. The United States Trustee argued that the doctrine of laches should apply because this case had been closed for eight years. First, the court found that § 350(b) provided "broad discretion to determine whether a movant has demonstrated 'good cause' to reopen a case." Such cause could include a need to amend schedules, and neither the Code section nor Rule 5010 "prescribe a period by which a motion to reopen must be brought." Although legislative history "suggests a defense based upon the equitable doctrine of laches may be asserted against a motion to reopen," the Court found no showing of prejudice to the two lienholders who would be impacted by reopening. Those lienholders had not objected to the motion, but they might still object to avoidance. Section 522(f) also has no time limitation for seeking avoidance relief, and the debtor would need to amend exemptions before seeking lien avoidance. Under the circumstances of this case, laches did not bar reopening. As to amendment of Schedule C, the Court identified three approaches to applying Rule 1009(a) to amendments when cases had been closed: (1) the strict absolute bar on certain amendments, which was found to be a minority approach; (2) the middle approach of

applying the standard of excusable neglect in Rule 9006(b)(1); and (3) the broadest approach of applying Rule 1009(a) "equally to open or reopened cases." This is the approach adopted by *In re Mendoza,* 595 B.R. 849 (B.A.P. 10th Cir. 2019), concluding that Rule 9006(b)(1) did not apply to Rule 1009, with no difference for amendment purposes between an open and reopened case. The motion to reopen was granted, and upon the debtor's filing of an exemption amendment and motion to avoid judicial liens, objections to the amendment and avoidance could be asserted based on the merits. In re Paduch, 636 B.R. 340 (Bankr. D. Conn. 2022), Judge Nevins.

**Reopening to allow filing of reaffirmation agreement was denied.** The pro se debtor moved to reopen her case to allow filing of a reaffirmation agreement, and the Court denied the motion, holding that § 524(c)(1) requires that an enforceable reaffirmation agreement be "made" before entry of discharge, and when an agreement is "made" is a question of when the parties had a meeting of the minds. Reopening the case would not allow entry of a reaffirmation agreement that was not made before entry of discharge. In re Ostrowski, 635 B.R. 181 (Bankr. M.D. Fla. 2022), Judge McEwen.

**No cause shown to reopen case to allow debtor to file financial management certificate twenty months after closing.** The Chapter 7 case had been closed without discharge due to debtor's failure to file certificate of completion of required financial management course, and the Court applied a four-factor test to determine whether cause for reopening had been shown: "(1) whether there is a reasonable explanation for the failure to comply; (2) whether the request was timely; (3) whether fault lies with counsel; and (4) whether creditors are prejudiced." The opinion cites prior opinions on this issue by this Court and others. Rule 1007(b)(7) requires a showing of cause, and the factors weighed against a finding of cause. In re Williams, 636 B.R. 484 (Bankr. E.D. Mich. 2022); In re Lewis, 635 B.R. 157 (Bankr. E.D. Mich. 2022); In re Motley, 635 B.R. 150 (Bankr. E.D. Mich. 2022); In re Brown, 634 B.R. 748 (Bankr. E.D. Mich. 2022), Judge Tucker.

**Discharge Injunction**

**Discharge of personal liability subjected mortgage servicer to potential discharge injunction violation but *Taggart* standard at play.** On summary judgment motions, the Court found that the Chapter 7 debtor's personal liability on mortgage had been

discharged and that the mortgage servicer's violation of the injunction would be measured under the *Taggart* standard. In this case, the mortgage statements sent to the debtor post-discharge did not contain disclaimer language or acknowledgment of the discharge, and those statements had a coercive effect that would violate the injunction. However, other notices did not violate the injunction, and there was insufficient evidence that the servicer knew about the debtor's discharge. Without such evidence, the Court "cannot determine whether it was objectively reasonable for [the servicer] to send the mortgage statements in a form that violated the discharge injunction." In re Lett, 635 B.R. 713 (Bankr. N.D. Ga. 2022), Judge Ellis-Monro.

**Conversion Chapter 7 to 13**

**Debtor's motion to convert to 13 denied.** Affirming the Bankruptcy Court's denial of the debtor's motion to convert from Chapter 7 to 13, the Bankruptcy Appellate Panel reviewed the standard for such conversions, applying *Marrama v. Citizens Bank of Mass.,* 549 U.S. 365 (2007), and concluding that *Law v. Siegel,* 571 U.S. 415 (2014), did not overrule *Marrama.* "The right to convert under § 706(a) is qualified by § 706(d), which requires that a debtor seeking conversion must qualify to be a debtor in the converted case. . . .Put another way, *Marrama*'s holding that the right to convert is not absolute was not premised upon the bankruptcy court's equitable power but on explicit provisions of the Bankruptcy Code. Thus, it does not run afoul of *Law.*" In the current case, the Bankruptcy Court found bad faith in the debtor's attempted conversion, and that finding was not clearly erroneous under the totality of circumstances. Also, the debtor lacked sufficient regular income to fund a Chapter 13 plan. In re Richards, ___ B.R. ___, 2022 WL 884593 (B.A.P. 9th Cir. Mar. 24, 2022).

**Chapter 7 trustee's compensation in case converted from 7 to 13.** The debtor objected to the Chapter 7 trustee's application for payment of administrative fees and costs because no disbursements had been made to creditors before the case was converted to Chapter 13, and the Court noted that this issue has not been consistently resolved by bankruptcy courts. The opinion reviews authority on compensation of the Chapter 7 trustee. In the current case, because the trustee had not recovered assets or made disbursements, compensation under § 326(a) was inapplicable, but the trustee had expended substantial efforts investigating and objecting to the debtor's homestead

exemption. These efforts led to the debtor's conversion to 13. The Court considered whether the trustee's requested compensation of $4,000 was available under quantum meruit or other theory, recognizing that equitable powers are constrained and that strict readings of §§ 326(a) and 330 do not provide a remedy. The trustee's substantial work was performed pursuant to § 704 statutory duties. Although sympathetic to trustees' work that leads to debtors' conversion, Congress permitted conversion at any time under § 706(a); therefore, the resulting inability to pay trustees for such work prior to conversion is "not an extraordinary circumstance that would permit this Court to look beyond the commission rates contained in § 326(a)." In re Mitchell, ___ B.R. ___, 2022 WL 659509 (Bankr. D. Idaho Mar. 4, 2022), Judge Meier.

**Chapter 13 Issues**

**Eligibility**

**Debtor ineligible when prior case was dismissed after stay relief order.** The Chapter 13 case was filed within 180 days after the prior case had been voluntarily dismissed following filing of a motion for stay relief and entry of order granting that relief. The Court agreed with those other courts finding § 109(g)(2) to be mandatory when the statute applied, with no requirement of a causal link between the filing of a stay relief motion and subsequent voluntary dismissal of the case. In re Holloway, 635 B.R. 149 (Bankr. E.D. Mich. 2022); In re Baker, 635 B.R. 147 (Bankr. E.D. Mich. 2022); In re Boston, 635 B.R. 483 (Bankr. E.D. Mich. Feb. 112, 2022), Judge Tucker. See also In re Hill, ___ B.R. ___, 2022 WL 804068 (Bankr. E.D. Mich. Mar. 9, 2022) (Incarcerated debtor's spouse took credit counseling for debtor but that was insufficient, and no motion was filed to excuse the debtor from requirement under § 109(h). The debtor was ineligible.).

**Debtor ineligible when debts exceeding debt limit were noncontingent and liquidated.** Examining § 109(e)'s eligibility requirement that debts be noncontingent and liquidated, the money judgments at issue met that requirement, and the debtor's continuing disputes of the judgments did not make them contingent or unliquidated. In re Ibbott, ___ B.R.___, 2022 WL 697287 (Bankr. D. Maryland Mar. 8, 2022), Judge Chavez-Ruark.

**Property of Chapter 13 Estate**

**Debtor retained interest in vehicle subject to title loan under Alabama law.** In a dispute over whether the Chapter 13 debtor and the bankruptcy estate had interests in a vehicle that was subject to pre-bankruptcy title loan, the Court analyzed Alabama common law and UCC, determining that the vehicle was not a pledged good under the State's Pawnshop Act's forfeiture provision and the lender had not obtained absolute title to the vehicle under that Act. The debtor was able to treat TitleMax in a plan as holder of a secured claim. In re Hambright, 635 B.R. 614 (Bankr. N.D. Ala. 2022), Judge Henderson. Compare In re Snyder, 635 B.R. 901 (Bankr. S.D. Ga. Jan. 13, 2022), Judge Coleman. Under Georgia's pawn law, pawn transactions, including for automobiles, are for 30-day periods, subject to extension for another 30 days, and failure to redeem the pawned property within an extended grace period results in the pawned vehicle not becoming property of the Chapter 13 estate. The unredeemed title pawn contract could not be modified in a plan as a secured claim. The opinion analyzes Eleventh Circuit authority and the effect of § 541(b)(8).

**Confirmation Issues**

**Interest rate on property taxes after tax sale.** Applying Illinois law on tax sales, the taxpayer may redeem the property by paying the tax-sale purchaser. The plan treated the purchaser as a secured creditor, but the amount of interest on the "sold taxes" was determined under Illinois law at 18%. In re Drake, ___ B.R. ___, 2022 WL 548016 (Bankr. N.D. Ill. Feb. 23, 2022).

**Completion of Plan**

**Plan determined to be fully performed and debtor's failure to turn over tax refunds forgiven.** In the confirmed plan, the debtor committed to pay 10% to unsecured creditors, to pay mortgage arrearages, and to turn over tax refunds each year during the 36-month plan, but the debtor failed to fully comply with the tax turnover requirement. Nevertheless, the total plan payments were sufficient to pay the mortgage arrearage, allowed attorney fees, and 10% of the only filed unsecured claim (City of Chicago parking tickets), but the trustee moved to dismiss the case for failure to fully comply with the tax turnover provision. The opinion discusses how tax refund expectations may be skewed, including by

inaccurate or excessive withholdings and by the refunds' inclusion of tax credits. The debtor had been providing tax returns to the trustee, disputing that failure to turn over all tax refunds was plan default, and the trustee had not enforced the turnover requirement consistently throughout the plan. Discussing the elements of laches, the Court found fault with both the debtor, debtor's counsel and trustee for the lack of compliance with the tax turnover plan provision, and the Court found that modification of the plan to require the debtor to pay all tax refunds would require the plan to run beyond 60 months because of the debtor's limited income. Under the Court's § 105(a) authority, the debtor's failure to fully perform the tax turnover provision was forgiven and plan payments were complete, In re Carter, ___ B.R. ___, 2022 WL 953495 (Bankr. N.D. Ill. Mar. 30, 2022), Judge Barnes.

**Conversion of Case**

**Proceeds from pre-conversion home sale, including appreciated value, belongs to debtors.** Concluding that section 348(f)(1)(A) provided that proceeds of the post-confirmation and pre-conversion sale by Chapter 13 debtors of their home belonged not to the estate but to the debtors, the Tenth Circuit affirmed its Bankruptcy Appellate Panel. The opinion acknowledges that there is a split of judicial authority, but the Circuit found the statutory language to be plain. The case had been converted to Chapter 7 after the Chapter 13 debtors had sold their home, which had increased in value after the 13 filing. The Chapter 7 trustee sought turnover of the appreciated equity above the previously allowed homestead exemption. Property had revested in the debtors at confirmation, and the Circuit held that section 348(f)(1)(A) provided that, absent bad faith, "after conversion, the Chapter 7 estate generally consists of the same interests in property that would have been included in the estate had the debtor originally filed under Chapter 7, so long as the debtor has possession or control of those interests at conversion." The Circuit concluded that section 541(a) recognizes that legal and equitable interests are legally distinct from proceeds from those interests, "Based on the plain language of § 348(f)(1)(A), the sale proceeds—a property interest distinct from the physical house from which they were derived—do not enter the converted Chapter 7 estate." As a result of the post-confirmation sale, the house was not in possession of or under control of the debtors at

conversion, and the proceeds of that sale did not exist at the time of filing the Chapter 13. The vesting effect of confirmation supported the Court's conclusion, with the trustee's turnover request ignoring the effect of revestment. The opinion noted in footnote that the Court was not deciding who would get appreciated value when the home was still owned by the debtors at the time of conversion to Chapter 7. In re Barrera, 22 F.4th 1217 (10th Cir. 2022).

**Debtor's Attorney**

**Procedure for no-look fee to debtor's attorney.** Finding that a "de facto no look fee agreement" had been implemented between the Chapter 13 trustee and debtors' counsel, the Court had "sole responsibility" to determine reasonable attorney fees; therefore, the Court adopted rules and procedures for a "presumptively reasonable fee," with requested fees beyond that amount requiring a fee request and hearing. Finding the "utility of presumptively reasonable fees persuasive," the presumptive fee would be $5,500, which was the basic fee currently being charged in the district in Chapter 13 cases. Mortgage loss mitigation had become the focus of local Chapter 13 cases, and the Court determined that it would no longer "entertain motions for loss mitigation in Chapter 7 or 13 cases," finding that "loss mitigation had morphed into an institutionalized process not supported by the Bankruptcy Code. It now seemingly exists not for the purpose originally intended but for the benefit of professionals, trustees, and institutions, often to the detriment of the creditors." Although encouraging debtors and secured creditors to reach consensual agreements, that process is voluntary, not one to be forced on creditors through a loss-mitigation process. The need for such a process had abated due to changes in interest rates, legislation addressing mortgage defaults and other factors. The Court found that it "has no legal authority under the Bankruptcy Code to enforce the loss mitigation program," including under § 105(a)." While parties could continue to submit motions to approve consensual mortgage modifications and consensual mediation, "this Court will no longer entertain loss mitigation motions in Chapter 13 [or 7] cases." The fee requested in the case before the Court involved loss mitigation work by the debtors' attorney. In re Tcherneva, 2022 WL 598324 (Bankr. E.D. N.Y. Feb. 28, 2022), Judge Grossman.

**Nunc pro tunc employment of personal injury attorney.** When the personal injury attorney for one of the joint debtors failed to seek timely employment and then settled the cause of action and disbursed funds without court approval, the Court considered whether nunc pro tunc employment was appropriate. Although finding that such employment may be permissible, with the *Acevedo* decision not a complete bar, there was no showing of excusable neglect to justify such employment in this case. The Court then addressed whether the personal injury attorney must disgorge fees received in the unauthorized settlement, with post-confirmation settlement proceeds being property of the Chapter 13 estate. Courts have split on whether § 327(e) applies to employment of an attorney by the debtor, and this Court found that it applied only to trustees' employment of attorneys, but personal injury attorneys have obligations under § 329(a) to seek approval of compensation because special counsel's representation in a post-petition matter is sufficiently connected to the bankruptcy case. Because this attorney disbursed settlement funds, including attorney fees, without disclosure and approval, the fees must be disgorged. Other issues about turnover of the funds disbursed to the debtor were not resolved in this opinion. In re Smith, ___ B.R. ___, 2022 WL 540016 (Bankr. S.D. Ga. Feb. 23, 2022), Judge Coleman. See also In re Mallinckrodt PLC, 2022 WL 906462 (D. Del. Mar, 28, 2022) (Rejected interpretation that *Acevedo* deprives courts of authority to approve professional retention retroactively.), District Judge Stark.

**Debtor standing**

**Chapter 13 debtors had standing to pursue action on behalf of estate against attorneys involved in foreclosure sale and eviction.** Without clear, controlling authority in the Sixth Circuit on whether only the Chapter 13 trustee has standing to bring avoidance and other causes of action on behalf of the Chapter 13 estate, or whether the debtor has concurrent standing with the trustee, at least six other circuits "appear to have come down on the side of concurrent standing for a Chapter 13 debtor to pursue causes of action on behalf of the estate," citing those Circuit opinions. The Court did not need to address the issue in this case, because the confirmation order provided for the debtor's standing to pursue the claims at issue. And *In re Isaacs,* 895 F.3d 904 (6th Cir. 2018), "makes it clear that standing can be approved by the court, even after the fact, to allow a

debtor to pursue a claim for the benefit of the estate." However, most allegations in the complaint failed to support claims under applicable Tennessee law, with only the alleged state trespass claim surviving motion to dismiss. In re Connor, ___ B.R. ___, 2022 WL 108356 (Bankr. M.D. Tenn. Jan. 4, 2022), Judge Mashburn.

**Chapter 13 Trustee**

**Trustee retains percentage fee paid before dismissal of case.** The District Court was persuaded by the Bankruptcy Appellate Panel's decision *In re Harmon,* 2021 WL 3087744 (B.A.P. 9th Cir. 2021) (which was a 2 to 1 unpublished decision), that 28 U.S.C. § 586(e)(2) controlled whether the Chapter 13 trustee could retain her percentage fee when the case was subsequently voluntarily dismissed. The opinion reviews the split of authority on whether § 1326(a)(2) or § 586(e)(2) controlled. The District Court found § 586(e)(2)'s language to be "plain and unambiguous. Its scheme lays out the details of the percentage fee: it goes to the Trustee for her work as the standing trustee and it comes from the payments made according to the chapter 13 plan. No further qualifiers, limitations, or exceptions appear in the language. Nowhere does § 586(e)(2) direct the Trustee to hold the fee until confirmation or denial of confirmation. It only directs the Trustee to collect the fee—not to hold it and then return it if the plan is not confirmed. Only when you look beyond the statute can you find any ambiguity to read into the statute. But by the plain language of § 586(e)(2), the Trustee keeps the percentage fee upon dismissal of the chapter 13 bankruptcy petition." Moreover, the Court found harmony between § 586(e)(2) and § 1326(a)(2), because the latter statute "differentiates between payments and the percentage fee, and the same subsection also explains that the Trustee may take the fee *before* the payment to creditors. . . .Both statutes lay out the timing for collecting the percentage fee and neither limits it to after confirmation." McCallister v. Evans, ___ B.R. ___, 2022 WL 392933 (D. Idaho, Feb. 8, 2022), District Judge Nye.

**Debtors' Attorneys**

**Unlawful practice of law.** In an examination of the business model of Upright Law and whether it engaged in the unlawful practice of law in the Middle District of Alabama, the

Court made extensive findings, including that Upright permitted non-attorney staff in Chicago to engage in the unauthorized practice of law in Alabama. The Court also found that attorneys in Alabama were not partners or regular associates in Upright when they worked on bankruptcy cases that were prepared by Upright and filed in Alabama. Findings were made that Upright and the Alabama attorneys did not provide competent representation or otherwise comply with Alabama Rules of Professional Conduct. Sanctions included disgorgement of all fees paid in 87 consumer cases because of improper fee sharing and fee disclosures, and counsel for the Bankruptcy Administrator and Chapter 13 and 7 trustees were awarded attorney fees. Upright and its successor were enjoined from further practice of law in the Court unless specific conditions were met and a motion to lift the injunction was granted. The Alabama attorneys who had worked with Upright were required to complete 15 hours of continuing legal education in consumer bankruptcy law. In re Deighan Law LLC, ___ B.R. ___, 2022 WL 630892 (Bankr. M.D. Ala. Mar. 4, 2022), Judge Sawyer.

**Claims**

**State law did not provide basis for attorney fees to prevailing debtor.** Nevada statute provided for attorney fees to prevailing party when opposing party's claim was without reasonable grounds or was brought to harass prevailing party, but the Bankruptcy Appellate Panel held that the statute could not be used to assess attorney fees to debtor when creditor filed a proof of claim for a time-barred debt. Under *Midland Funding, LLC v. Johnson,* 137 S.Ct. 1407 (2017), the definition of "claim" is a "right to payment" and that is broad enough to include a claim that is unenforceable because of running of the limitations period, which constitutes an affirmative defense that may be asserted by the debtor to the claim. The state claim was not "groundless" for purposes of applying the Nevada fee-shifting statute. LVNV Funding, LLC v. Andrade-Garcia, 635 B.R. 509 (B.A.P. 9th Cir. 2022).

**Shared responsibility payment under Affordable Care Act is tax entitled to priority.** The Sixth Circuit Bankruptcy Appellate Panel in split decision considered the Affordable Care Act's provision that individuals failing to maintain qualified health insurance or qualifying for exemption from the requirement are subject to a "shared responsibility

payment" for those months they lack health insurance coverage. The majority panel held that the liability is subject to priority treatment under § 507(a)(8)(A) in Chapter 13 plans, because the shared responsibility payment is a tax measured by income. The opinion discusses prior Supreme Court authority on the Affordable Care Act and applied the Sixth Circuit's "functional examination" of whether "an exaction is a 'tax' or 'penalty' for purposes of priority, and the majority held that § 507(a)(8)(A) "does not require that the tax be calculated *solely* or *primarily* by measuring income." In re Juntoff and McPherson, ___ B.R. ___, 2022 WL 830901 (B.A.P. 6th Cir. Mar. 21, 2022).

**Burdens on objection to claim.** Under § 502(a) a proof of claim is deemed allowed, with the objecting party carrying initial burden of persuasion to overcome the *prima facie* presumptive allowance, and if that is done, the burden shifts back to the claimant to produce evidence to overcome the objection and prove that the claim is allowable. To the extent an objection attacks one aspect for the claim, the claimant is only required to address that aspect. In this case, the objecting debtor failed to specify which subsection of § 502(b) was at issue, and the debtor failed to rebut the *prima facie* allowance of the claim. In re Speigel, ___ B.R. ___, 2022 WL 736253 (Bankr. N.D. Ill. Mar. 11, 2022), Judge Barnes.

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# Recent Developments in Bankruptcy Law, January 2022

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# Recent Developments in Bankruptcy Law, January 2022

## 1. AUTOMATIC STAY

### 1.1 Covered Activities

1.1.a ***Taggart v. Lorenzen* standard applies to stay violation in a corporate case.** The debtor sold assets prepetition. After the petition date, the buyer demanded payment of certain working capital adjustments provided under the purchase agreement. The automatic stay prohibits any act to collect or recover a prepetition claim. Section 362(k) allows an individual debtor to recover damages for willful violation of the stay. Under Sixth Circuit law, it does not protect non-individual debtors. Therefore, the remedy for a stay violation in a non-individual debtor case is a civil contempt citation under section 105(a). *Taggart v. Lorenzen*, 139 S. Ct. 1795 (2019), applied the general standards for a civil contempt citation to a violation of the discharge injunction, permitting a contempt finding only if the actor had no objectively reasonable basis on which to assert the discharge injunction did not apply. But in dicta, the decision distinguished automatic stay violations in individual debtor cases, suggesting a strict liability standard might be appropriate. Because section 362(k) does not apply in non-individual debtor cases, the distinction does not apply; the general civil contempt standards apply. In this case, compliance with the purchase agreement regarding purchase price adjustments would not violate the stay, but the belated demand for payment did. However, the seller had an objectively reasonable basis to conclude that the action did not violate the stay. Therefore, the court denies the request for sanctions. *Harker v. Eastport Holdings, LLC (In re GYPC, Inc.)*, ___ B.R. ___ (Bankr. S.D. Ohio Nov. 22, 2021).

1.1.b **Refusal to quash a prepetition garnishment writ does not violate the stay as long as the creditor stays all proceedings.** Before bankruptcy, the creditor obtained a writ of garnishment and garnished the debtor's bank account. The bank froze the account, but before it turned over any funds to the creditor, the debtor filed a bankruptcy petition. The creditor requested the state court stay the proceedings and advised the court that it had no objection to the bank's release of the funds, but it would not quash its writ or direct the bank to release the funds. The court stayed the proceedings, granted the debtor's request to quash the writ, and denied the debtor's request for a return of the funds. However, the bank unfroze the account a few days later. The automatic stay prohibits (1) a creditor from commencing or continuing an action to collect a prepetition debt, (2) enforcement against the debtor of a prepetition judgment, (3) any act to obtain possession of property of the estate or from the estate or to exercise control over such property, and (6) any act to collect or recover a prepetition claim. *City of Chicago v. Fulton*, 141 S. Ct. 585 (2021), held that section 362 requires a creditor holding property of the debtor or the estate to maintain the status quo but does not require turnover of the property, which is governed instead by section 542. Refusing to quash the garnishment was not the continuation of a prepetition action, nor is it an attempt to enforce a prepetition judgment, as long as the creditor stayed all proceedings in the action. Refusal to quash the writ was also not an act to obtain property or an act to collect the debt. Here, the creditor did nothing to change its position, and the debtor's account was unfrozen. Therefore, the creditor did not violate the stay. *Stuart v. City of Scottsdale (In re Stuart)*, 632 B.R. 531 (9th Cir. B.A.P. 2021).

### 1.2 Effect of Stay

### 1.3 Remedies

## 2. AVOIDING POWERS

### 2.1 Fraudulent Transfers

2.1.a **Tax foreclosure sale for the amount of taxes owing is subject to attack as a fraudulent transfer.** The debtor defaulted on property taxes. In accordance with state law, the local taxing authority foreclosed on the property by bidding in the amount of the taxes, which was about 10%

of the fair market value of the property. The debtor filed a chapter 13 case and brought a constructive fraudulent transfer action under section 548(a)(1)(B) to avoid the foreclosure sale. Section 548(a)(1)(B) permits a trustee (or a chapter 13 debtor) to avoid a transfer of property of the debtor made for less than reasonably equivalent value within two years before the petition date while the debtor was insolvent. In *BFP v. Res. Trust Corp.*, 511 U.S. 531 (1994), the Supreme Court held that a regularly conducted, non-collusive mortgage foreclosure sale resulted in reasonably equivalent value and so was not subject to avoidance as a fraudulent transfer. However, the Court did not address tax foreclosures. In this case, the ability of the taxing authority to purchase the property without an auction for a price that had no relation to the property's value gave rise to potential fraudulent transfer liability. *Lowry v. Southfield Neighborhood Revitalization Initiative (In re Lowry)*, ___ F.4th ___, 2021 U.S. App. LEXIS 13042 (6th Cir. Dec. 27, 2021).

### 2.2 Preferences

### 2.3 Postpetition Transfers

### 2.4 Setoff

### 2.5 Statutory Liens

2.5.a **Section 108(c) does not toll the period for giving notice under section 546(b).** A creditor recorded a notice of mechanics lien prepetition. State law required that the creditor file an action to enforce the lien within 90 days after recordation. The debtor filed its petition during the 90-day period. The creditor gave notice under section 546(b) more than 90 days after the recordation date. Section 546(b) provides that in lieu of seizing property or commencing an action required under nonbankruptcy law to continue or maintain perfection of a lien, the creditor may continue or maintain the lien "by giving notice within the time fixed by such law for such seizure or such commencement," and giving such notice does not violate the automatic stay. Section 108(c) tolls the limitations period for a creditor to commence an action until the later of the end of such period or 30 days after notice of termination of the automatic stay. Because section 546(b) gives an alternative—giving notice—that does not violate the stay, section 108(c) does not toll the period for giving notice. Therefore, the creditor's notice was late, and his lien terminated. *Philmont Mgmt., Inc. v. 450 Western Ave., LLC (In re 450 Western Ave., LLC)*, 633 B.R. 894 (9th Cir. B.A.P. 2021).

### 2.6 Strong-arm Power

### 2.7 Recovery

## 3. BANKRUPTCY RULES

## 4. CASE COMMENCEMENT AND ELIGIBILITY

### 4.1 Eligibility

4.1.a **Shareholder approval requirement for a bankruptcy petition is not contrary to public policy.** The LLC debtor borrowed from an investor, who also acquired, for a separate substantial price, a preferred equity interest. The debtor's LLC agreement was amended to provide that the debtor could not file a bankruptcy petition without the affirmative vote of a majority of the preferred units. Applicable nonbankruptcy law determines who has authority to file a bankruptcy petition. A court should enforce any provision in the debtor's organic documents that specifies who has the authority. Such a provision might be contrary to public policy if it provided only a "golden share" to a creditor to prevent a filing. Here, however, the creditor is also a substantial equity holder, who, as a non-managing member of an LLC, does not have fiduciary duties to the LLC or its other members and thus may protect its rights by withholding consent to the bankruptcy filing. *In re 3P Hightstown, LLC*, 631 B.R. 205 (Bankr. D.N.J. 2021).

4.1.b **Nonoperating debtor is not eligible for subchapter V.** The debtor was a physician who owned a medical practice that had closed some years before the petition date. She filed a chapter 11 case and elected to proceed under subchapter V. To do so, she had to be "engaged in business or commercial activity." "Engaged in," in the present tense, has a temporal element and requires the debtor be engaged in business or commercial activity as of the petition date, not at some earlier time. Such a reading comports with the statute's purpose to assist small businesses to reorganize as going concerns. Therefore, the debtor does not qualify for subchapter V. *Nat'l Loan Invs., L.P. v. Rickerson (In re Rickerson)*, ___ B.R. ___, 2021 Bankr. LEXIS 3403 (Bankr. W.D. Pa. Dec. 14, 2021).

### 4.2 Involuntary Petitions

### 4.3 Dismissal

## 5. CHAPTER 11

### 5.1 Officers and Administration

### 5.2 Exclusivity

### 5.3 Classification

### 5.4 Disclosure Statement and Voting

### 5.5 Confirmation, Absolute Priority

## 6. CLAIMS AND PRIORITIES

### 6.1 Claims

6.1.a **The court must evaluate factually whether a make-whole is the economic equivalent of interest; if it is, it is subject to disallowance as postpetition interest, which must be paid at the federal judgment rate in a solvent case.** The debtor was solvent and proposed a plan that provided substantial recovery for equity. For its unsecured noteholders, it proposed the class be unimpaired by payment in cash in full on the effective date in the principal amount plus interest accrued but unpaid as of the petition date, without payment of a make-whole or postpetition interest. The notes' redemption clause, not its acceleration clause, determines whether the holders are entitled to a make-whole. If the indenture requires it, then it may be allowed only if it is not the economic equivalent of interest, based on the make-whole's terms and their relationship to interest on the notes, which is a factual question. Section 502(b)(2) disallows postpetition interest, even in a solvent debtor case; a plan's treatment of the claim as disallowed under section 502(b) does not constitute an impairment. Section 1124(3)'s repeal did not require the payment of postpetition interest at the contract rate to unimpaired classes. But the solvent debtor exception survived to a limited extent through 1129(a)(7) and 726(a)(5) for an impaired class of unsecured claims. Those sections require payment of postpetition interest at the federal judgment rate. There is no reason to treat impaired and unimpaired classes differently, so the federal judgment rate applies to unimpaired classes in a solvent debtor case. *Wells Fargo Bank, N.A. v. The Hertz Corp. (In re The Hertz Corp.)*, ___ B.R. ___, 2021 Bankr. LEXIS 3491 (Bankr. D. Del. Dec. 22, 2021).

### 6.2 Priorities

## 7. CRIMES

## 8. DISCHARGE

### 8.1 General

### 8.2 Third-Party Releases

8.2.a **Only the district court has constitutional authority to approve nonconsensual third-party releases under a plan.** The debtor and its shareholders, directors, and officers contributed substantially to the nation's opioid epidemic. It proposed a plan under which the individuals, who did not file bankruptcy petitions, would have contributed $4.4 billion and received broad nonconsensual releases from any liability related to the marketing, sale, and distribution of opioids, including direct claims against them by creditors of the debtor and including claims for fraud and claims of governmental units for nonpecuniary loss penalties. Under section 157 of title 28, the district court may refer proceedings arising under title 11 or arising in or related to a bankruptcy case to the bankruptcy court. But Article III prohibits a bankruptcy court from issuing a final order in litigation that is not a constitutionally core proceeding (arising under or arising in) without the parties' consent. A nondebtor's claim against another nondebtor is not a core proceeding. An order providing for a release of such a claim finally determines the claim. Without consent, a bankruptcy court does not have constitutional authority to determine such a claim, even if such determination occurs without adjudication of the claim. Therefore, a third-party release under a plan may be approved only by the district court, even if the approval occurs within a core proceeding such as plan confirmation. *In re Purdue Pharma, L.P.*, ___ B.R. ___ (S.D.N.Y. Dec. 12, 2021).

8.2.b **A bankruptcy court has subject matter jurisdiction to approve third-party releases if the released claims are related to the bankruptcy case.** The debtor and its shareholders, directors, and officers contributed substantially to the nation's opioid epidemic. It proposed a plan under which the individuals, who did not file bankruptcy petitions, would have contributed $4.4 billion and received nonconsensual broad releases from any liability related to the marketing, sale, and distribution of opioids, including direct claims against them by creditors of the debtor and including claims for fraud and claims of governmental units for nonpecuniary loss penalties. Section 1334(b) of title 28 gives the district court jurisdiction over proceedings related to a bankruptcy case. Related-to jurisdiction reaches any proceeding that could have any conceivable effect on the estate. A release of third-party claims that, unless released, could result in reimbursement or contribution claims against the estate, that could cause the estate to incur material fees or expenses in defending the claims, or that could result in depletion of estate assets are sufficiently related to the bankruptcy case to be within the court's related-to jurisdiction. However, the third party's contribution of funds to the reorganization, standing alone, does not create related-to jurisdiction. Here, at a minimum, litigation of the claims could have generated indemnification claims and would have required the estate to incur substantial expenses in addressing the claims. Therefore, proceedings on the claims are related to the case, whether or not the individuals contributed funding for the plan. *In re Purdue Pharma, L.P.*, ___ B.R. ___ (S.D.N.Y. Dec. 12, 2021).

8.2.c **The Code does not authorize third-party releases under a plan.** The debtor and its shareholders, directors, and officers contributed substantially to the nation's opioid epidemic. It proposed a plan under which the individuals, who did not file bankruptcy petitions, would have contributed $4.4 billion and received nonconsensual broad releases from any liability related to the marketing, sale, and distribution of opioids, including direct claims against them by creditors of the debtor and including claims for fraud and claims of governmental units for nonpecuniary loss penalties. Section 1123(a)(5) permits a plan to contain provisions providing for the plan's implementation relating to the use or disposition of property of the estate. Because it deals only with property of the estate, it does not authorize a third-party release simply because the releases might generate plan funding from the releasees. Section 1123(a)(6) permits a plan to include any provision not inconsistent with the other terms of the Code, and section 105(a) permits the court to issue any order necessary to carry out the provisions of the Code. These provisions could

authorize a third-party release only if the release is not inconsistent with or necessary to carry out other provisions of the Code. No other provision of the Code authorizes a third-party release. Nor does the Code's silence on third-party releases imply any authority, and there is no residual authority on which the court may rely. As a comprehensive system for adjusting debtor-creditor relations, the Code would have addressed the issue if it were permitted. Moreover, section 523(a) excepts from discharge certain claims against an individual debtor, including claims for fraud and for certain governmental penalties. A third-party release that includes claims that would be nondischargeable is inconsistent with the Code. Section 524(e) provides that a discharge does not release a nondebtor's liability on a claim against the debtor. Because the claims here are direct claims against the third parties, not claims on which the debtor is liable, section 524(e) does not apply. For all these reasons, the court rules the plan's third-party release provisions are impermissible. *In re Purdue Pharma, L.P.*, ___ B.R. ___ (S.D.N.Y. Dec. 12, 2021).

8.2.d **A bankruptcy court does not have authority to grant third-party releases without the claimants' consent to the bankruptcy court's adjudication of the claims.** The debtor sold its assets and proposed a liquidation plan that provided broad third-party releases, particularly securities class action claims against directors and officers. The disclosure statement and ballots made clear that non-voting equity holders, who received nothing under the plan, and voting creditors could opt out of the releases. In providing notice of the releases and the opt-out right, the court focused only the securities class action litigation, not on all the other possible claims that the broad releases might cover and did not provide notice to those other potential claimants. The bankruptcy court does not have constitutional authority to hear and determine non-core claims without the parties' consent. Although a bankruptcy court has *in rem* jurisdiction over property of the estate, third-party claims are not property of the estate, and the bankruptcy court may not determine them. For these reasons, it does not have constitutional authority to determine the claims by releasing them without the parties' consent to its authority. An opportunity for third-party claimants to opt-out in plan voting does not constitute sufficient consent to the court's authority or to the releases to permit the bankruptcy court to determine the claims, because consent may not generally be based on inaction. Therefore, the bankruptcy court should have issued a report and recommendation to the district court to consider the third-party releases. *Patterson v. Mahwah Bergen Retail Group, Inc.* ___ B.R. ___, 2020 U.S. Dist. LEXIS 7431 (E.D. Va. Jan. 13, 2022).

8.2.e **Court disapproved third-party releases under liquidating plan.** The debtor sold its assets and proposed a liquidation plan that provided broad third-party releases, particularly securities class action claims against directors and officers. The disclosure statement and ballots made clear that non-voting equity holders, who received nothing under the plan, and voting creditors could opt out of the releases. In providing notice of the releases and the opt-out right, the court focused only the securities class action litigation, not on all the other possible claims that the broad releases might cover, and did not provide notice to those other potential claimants. In the Fourth Circuit, approval of third-party releases requires an identity of interests between the releasee and the debtor, contribution of substantial assets, importance to the reorganization, overwhelming plan acceptance, payment of substantially all of the classes affected by the release, an opportunity for non-settling claimants to recover in full and specific factual findings supporting the foregoing. Satisfaction of these factors means the releases are integral to the plan. The bankruptcy court did not make adequate findings on these factors. Moreover, a liquidating plan under which the releasees do not make any contribution does not satisfy the test. Therefore, the court disapproves the releases and, under the plan's severability provision, severs them from the plan. *Patterson v. Mahwah Bergen Retail Group, Inc.* ___ B.R. ___, 2020 U.S. Dist. LEXIS 7431 (E.D. Va. Jan. 13, 2022).

8.2.f **Actual notice of a third-party release satisfies due process, despite lack of formal notice**. The creditor was injured by a valet driver after dropping off his car at a hotel. He sued the valet company, the hotel owner, and several affiliates of the hotel, including the hotel operator, in state court. The hotel owner filed a chapter 11 case. Its plan provided for a third-party release and related injunction in favor of the affiliates, all of which it had indemnified under the various

agreements relating to the hotel's operation. The creditor received a copy of the plan and disclosure statement, which described the releases, but did not receive the notice required under Bankruptcy Rule 2002(c)(3), which requires specific notice of any injunction provided for in the plan. The creditor did not object to the releases. Due process requires that a creditor receive notice. Although the Rules require a specific form of notice, the Rules are only procedural, and actual notice satisfies due process. Therefore, the release and injunction bind the creditor. *Jackson v. Le Centre on Fourth, LLC (In re Le Centre on Fourth, LLC)*, ___ F.4th ___, 2021 U.S. App. LEXIS 33845 (11th Cir. Nov. 15, 2021).

8.2.g **Standard to approve litigation settlement bar order differs from standard to approve chapter 11 plan third-party release.** The chapter 11 creditors committee settled claims against the debtor's former officers and directors. The court approved the settlement, which included a bar order that released them from any claims directly or indirectly related to the bankruptcy. A bar order in ordinary litigation, whether or not in the bankruptcy court, differs from a third-party release under a chapter 11 plan. A court may approve a bar order if it is integral to the settlement agreement, that is, if the settling defendants would not have settled without it. By contrast, a court may approve a third-party release under a plan only if it is necessary for the reorganized entity to succeed. Here, because the agreement settled ordinary litigation claims and the bar order was necessary to the settlement, the court properly approved it. *Markland v. David (In re Centro Group, LLC)*, ___ Fed. App'x ___, 2021 U.S. App. LEXIS 32962 (11th Cir. Nov. 5, 2021).

### 8.3 Environmental and Mass Tort Liabilities

## 9. EXECUTORY CONTRACTS

9.1.a **Rejection relieves the estate from an arbitration agreement.** The debtor's limited partnership agreement provided for arbitration of disputes. The debtor in possession rejected the agreement. Later, it sued some of the limited partners, who demanded arbitration of the claims. Rejection of an executory contract relieves the estate from any specific performance obligation under the contract. An arbitration agreement within a contract is really a separate contract, not merely an enforcement mechanism in the case of a breach. Therefore, rejection relieves the estate from the obligation to arbitrate. *Highland Cap. Mgmt., L.P. v. Dondero (In re Highland Cap. Mgmt., L.P.)*, ___ B.R. ___, 2021 Bankr. LEXIS 3314 (Bankr. N.D. Tex. Dec. 3, 2021).

## 10. INDIVIDUAL DEBTORS

### 10.1 Chapter 13

### 10.2 Dischargeability

### 10.3 Exemptions

### 10.4 Reaffirmations and Redemption

## 11. JURISDICTION AND POWERS OF THE COURT

### 11.1 Jurisdiction

### 11.2 Sanctions

### 11.3 Appeals

11.3.a **U.S. trustee has standing to appeal plan confirmation.** The debtor sold its assets and proposed a liquidation plan that provided broad third-party releases, particularly securities class action claims against directors and officers. The disclosure statement and ballots made clear that non-voting equity holders, who received nothing under the plan, and voting creditors could opt out

of the releases. The U.S. trustee and the securities litigation lead plaintiff, who had opted out of the releases, objected to the releases. Because of the U.S. trustee's supervisory role and the express grant in section 307, he has standing to appeal plan confirmation. But the securities action lead plaintiff does not, because the releases do not affect him as an opt-out creditor. *Patterson v. Mahwah Bergen Retail Group, Inc.* ___ B.R. ___, 2020 U.S. Dist. LEXIS 7431 (E.D. Va. Jan. 13, 2022).

11.3.b **Section 363(m) prohibits relief on appeal even from an allegedly illegal sale authorization.** The individual debtors moved to approve a credit bid sale to its secured lender, which had rolled up its prepetition loan with a financing under section 364. After the court approved the sale, the debtors developed arguments why the sale should not have been approved. They moved to amend the sale order and stay the sale. The bankruptcy court denied the motion, and the debtors appealed. Section 363(m) prohibits the reversal or modification on appeal of an order authorizing a sale to a good faith buyer unless the authorization has been stayed pending appeal. Section 363(m) applies to any sale authorized by the court, not only sales authorized by the statute. Therefore, any argument that the roll up invalidated the creditor's postpetition lien, undermining the authority for a credit bid, did not affect section 363(m)'s application. Therefore, the appeal is moot. A concurrence questions whether the decision is consistent with a prior circuit precedent that permitted an appeal from an order authorizing a postpetition cross-collateralization on the ground that the Code does not authorize cross-collateralization. *Reynolds v. Servisfirst Bank (In re Stanford)*, ___ F.4th ___, 2021 U.S. App. LEXIS 32503 (11th Cir. Nov. 1, 2021).

### 11.4 Sovereign Immunity

## 12. PROPERTY OF THE ESTATE

### 12.1 Property of the Estate

### 12.2 Turnover

### 12.3 Sales

## 13. TRUSTEES, COMMITTEES, AND PROFESSIONALS

### 13.1 Trustees

13.1.a **Representation of creditor against debtor's shareholder in unrelated case disqualifies subchapter V trustee as not disinterested.** The subchapter V debtor's equity holder was a holding company that was jointly owned by a husband and wife. The husband was a director of another company that was a debtor in an unrelated bankruptcy case. The subchapter V trustee represented a creditor in the other bankruptcy case in litigation against the husband for matters related to the other case. The trustee moved to dismiss the case as a bad faith filing and opposed plan confirmation. Section 1183 requires a subchapter V trustee to be disinterested, that is, not to have "an interest materially adverse to the interest of … equity security holders." The creditor in the other case has an interest materially adverse to the interest of the husband. For these purposes, an attorney assumes the interest of the client. Although the husband owns the equity interest in the debtor indirectly, through a holding company, the concern is the holder's interest, not the form of ownership. Disinterestedness is especially important in a subchapter V case, because subchapter V requires the trustee to actively facilitate a plan and, in effect, to act more as a mediator, who is not adverse to the debtor or its equity holders. Thus, the disinterestedness requirement must be enforced strictly. The trustee here is not disinterested, and his appointment and compensation are denied. *In re 218 Jackson LLC*, 631 B.R. 937 (Bankr. M.D. Fla. 2021).

**13.2 Attorneys**

13.2.a **Court may authorize postpetition retainer for counsel.** After bankruptcy, the debtor in possession sought to substitute new counsel. The application provided for counsel to receive a retainer from the estate, to be held in counsel's trust account until the court allowed fees that could be collected from the retainer. Section 327 authorizes the debtor in possession to employ counsel, and section 328(a) authorizes the employment "on any reasonable basis, including a retainer." Therefore, the Code authorizes the application, which the court grants. *In re Golden Fleece Beverages, Inc.*, ___ B.R. ___, 2021 Bankr. LEXIS 3319 (Bankr. N.D. Ill. Nov. 24, 2021).

13.2.b **Court cautions attorney on plagiarism.** Debtor's counsel in a subchapter V case included with the schedules and statement of affairs a 10-page disclaimer, which counsel copied from various mega-case filings. The disclaimer denied any obligation to update the documents or to notify creditors of any changes, contrary to the requirements of the Bankruptcy Rules. The court takes counsel to task for such a broad disclaimer. The court goes further, challenging the ethics of an attorney who copies work written by another attorney in another case. Ultimately, the court acknowledges that attorneys (and judges too) often copy from prior documents, but admonishes attorneys to "copy smart," that is, to make sure the facts match up and the law is correct and hasn't changed since the original text was written. *In re Summit Fin., Inc.*, ___ B.R. ___, 2021 Bankr. LEXIS 3077 (Bankr. C.D. Cal. Nov. 5, 2021).

13.2.c **Court approves employment retroactively to date before the employment application was filed.** The trustee employed an accountant effective January 28, 9 days after the petition date, but did not file the application to approve the employment until February 17. *Roman Catholic Archdiocese v. Acevedo Feliciano*, 140 S. Ct. 696 (2020), prohibits a federal court from issuing a *nunc pro tunc* order except to correct the record to reflect what actually happened. Section 327 requires court approval of the employment of a professional, but it does not have a temporal limitation, as other sections, which require approval "after notice and a hearing," do. Applying *Acevedo* to an employment application would add a timing requirement that Congress did not impose. Moreover, Rule 9013 imposes a delay on approval because it requires a written application and a hearing. If *Acevedo* did not permit approval after a professional started work, the trustee would be severely hampered in carrying out duties. Moreover, this case differs from those where the employment application was delayed for months or years, often until the time of the final fee application. Since section 327 permits employment approval after actual employment, the court approves the employment effective as of January 28. *In re Hunanyan*, 631 B.R. 904 (Bankr. C.D. Cal. 2021).

**13.3 Committees**

**13.4 Other Professionals**

13.4.a **Disappointed professional has standing to assert RICO claim against competitor for noncompliance with disclosure obligations.** In at least 13 cases in which the financial adviser was employed at the expense of the estate, it did not disclose all its connections, as required by Rule 2014. A competitor sued, claiming a RICO violation and a pay-to-play scheme. The competitor claimed it was injured by not being able to pitch for positions in a number of the cases and that the defendant adviser received employment in cases in which full disclosure would have disqualified it as not disinterested, taking opportunities away from the competitor. RICO provides a private right of action to anyone injured by a violation but requires an adequate showing that the violation caused the injury. In determining the complaint adequately alleged cause, the court of appeals stresses the importance of insuring the integrity of the bankruptcy system. Finding that the complaint adequately alleged that the financial adviser's conduct corrupted the employment process, the court determines that unsuccessful participants in the process are directly harmed, as are litigants who are entitled to a level playing field. The fraud alleged requires the courts' unique supervisory responsibilities. Therefore, the claim may proceed. *Alix v. McKinsey & Co., Inc.*, ___ F.4th ___, 2022 U.S. App. LEXIS 1596 (2d Cir. Jan 19, 2022).

### 13.5 United States Trustee

## 14. TAXES

## 15. CHAPTER 15—CROSS-BORDER INSOLVENCIES

JENNER&BLOCK

# Recent Developments in Bankruptcy Law, April 2022

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## 1. AUTOMATIC STAY

### 1.1 Covered Activities

### 1.2 Effect of Stay

### 1.3 Remedies

## 2. AVOIDING POWERS

### 2.1 Fraudulent Transfers

2.1.a **Imposition and payment of a tax penalty is not a fraudulent transfer.** While insolvent, the debtor incurred and paid tax penalties before bankruptcy. A transfer of property of the debtor while the debtor was insolvent for less than reasonably equivalent value is avoidable as a constructively fraudulent transfer. By referring to an exchange for value and defining when a transfer is made as when it takes effect between the parties, the UFTA does not contemplate involuntary obligations such as tax penalties. Therefore, the UFTA does not apply to a tax penalty. *Cook v. U.S. (In re Yahweh Center, Inc.)*, 27 F.4th 960(4th Cir. 2022).

### 2.2 Preferences

2.2.a **First cousins are "relatives."** The trustee sued a first cousin of the debtor's principal to avoid as a preference a transfer made more than 90 days before the petition date. Section 547(b) permits the trustee to avoid a transfer to a "relative" made within one year before the petition date. The Bankruptcy Code defines "relative" as one within the third degree of affinity or consanguinity as determined by the common law. Courts have generally used state, not federal, law, but are divided on whether to use state common or civil law. Because of the ambiguity in the definition, the court may look to legislative history. The definition derives from the Bankruptcy Act of 1898 with no meaningful revision. The legislative history of that act shows that Congress intended reference to the common law of England, and case law supports that interpretation. Using English common law rather than state law also promotes uniformity. Under English common law, relation is defined by distance from a common ancestor. For first cousins, the common ancestor is the grandparent. The cousins are each two degrees removed from a common grandparent and so come within the third degree. *Ehrenberg v. Halajyan (In re Victory Entm't, Inc.)*, 634 B.R. 90 (Bankr. C.D. Cal. 2021).

### 2.3 Postpetition Transfers

### 2.4 Setoff

### 2.5 Statutory Liens

### 2.6 Strong-arm Power

2.6.a **Section 544(b) permits reliance only on filed or listed claims.** In its first-day motions, the debtor in possession obtained authority to pay prepetition withholding and employment taxes to the IRS. The debtor did not list the claims on its schedule of liabilities, and the IRS did not file a proof of claim. Under the Internal Revenue Code, the IRS fraudulent transfer avoiding power has a ten-year reachback. Section 544(b) permits a trustee to avoid any transfer "by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502." Section 502 authorizes the filing of a proof of claim, and unless a party in interest objects, the claim is deemed allowed. Section 1111(a) deems allowed in a chapter 11 case any claim that is listed on the debtor's schedules as undisputed, liquidated, and not contingent. If a claim is not listed and the creditor does not file a proof of claim, the claim cannot be allowed. Therefore, the trustee may not rely on such a claim under section 544(b). Because the IRS did not file a proof of claim, and the debtor did not list the IRS's claim on its schedules, the trustee

may not rely on the IRS as the triggering creditor under section 544(b). *Miller v. Fallas (In re J & M Sales Inc.)*, 2022 Bankr. LEXIS 434 (Bankr. D. Del. Feb. 22, 2022.

**2.7 Recovery**

## 3. BANKRUPTCY RULES

3.1.a **Court denies *ex parte* motion to extend statute of limitations.** The debtor refused to cooperate with the trustee's investigation of avoidable transfers. As a result, the trustee was delayed in learning the identity of transferees and other potential defendants. With the two-year statute of limitations approaching, the trustee filed an *ex parte* motion to extend the statute on equitable tolling grounds. Bankruptcy Rule 9006 governs extensions of time but does not permit extension of a congressionally mandated time period, such as the statutes of limitations in section 546 or 549. Equitable tolling may excuse a late-filed complaint. A defendant may contest the late filing and challenge whether equitable tolling applies. But an unknown defendant is unable to do so in response to an *ex parte* motion to extend the statute on equitable grounds. And an *ex parte* order would not bind a future defendant who had no notice of the motion because due process requires that the defendant have notice and an opportunity to be heard. Therefore, the court denies the motion as ineffective and seeking only an advisory ruling. *In re Cramer*, ___ B.R. ___ (Bankr. C.D. Cal. Feb. 8, 2022).

3.1.b **Failure to follow local rule requiring motion to withdraw reference waives jury trial right.** The bankruptcy court's local rules provide that a party waives the right to a jury trial unless the party files a motion to withdraw the reference at least 14 days before the initial status conference in the adversary proceeding. Although the defendant demanded a jury trial in the answer, she did not timely file a motion to withdraw the reference. The local rule implements, rather than overrides, Bankruptcy Rule 7038, because without consent, the bankruptcy court may not try a case before a jury. Only the district court may do so, which requires a motion to withdraw the reference. Therefore, by failure to follow the required procedure, the defendant waived the right to a jury trial. *Welt v. Bumshteyn (in re Bumshteyn)*, 2022 Bankr. LEXIS 90 (Bankr. S.D. Fla. Feb. 1, 2022).

3.1.c **Failure to move to apply Rule 23 to a putative class claim does not constitute excusable neglect to file late proofs of claims.** The claimants began a class action against the debtor before bankruptcy, which stayed the action. The court fixed a claims bar date, confirmed a plan, and granted the class representatives stay relief to pursue the class action. The class representatives and some putative class members filed proofs of claim. After stay relief, the class action court found the class action improper and dismissed the case. The remaining claimants then sought leave to file late individual claims in the bankruptcy court, nearly three years after the bar date. A court may permit late filing upon a showing of excusable neglect, considering four factors: prejudice to the estate, length of delay, reason for the delay (including whether it was within the claimant's reasonable control), and good faith. No factor is more important than any of the others. Prejudice requires substantive prejudice, which was not present here, not merely litigation costs and delay, especially because the debtor was aware of the pending claims. However, the nearly three-year long delay was too long, and the delay could significantly affect the resolution of the litigation and the bankruptcy. The reason for the delay—awaiting the outcome of the class action litigation—did not constitute excusable neglect. Several individual claimants filed proofs of claim before the bar date, so the delay was within the claimants' reasonable control. Finally, the claimants' and their counsel's failure to move under Rule 9014 for application of Rule 7023 to the purported class proof of claim evinced a lack of diligence and a misunderstanding of the Bankruptcy Rules and showed lack of good faith. As a result, the court denies the motion to file late claims. *W. Wilmington Oil Field Claimants v. Nabors Corp. Servs., Inc. (In re CJ Holding Co.)*, 27 F. 4th 1105 (5th Cir. 2022).

## 4. CASE COMMENCEMENT AND ELIGIBILITY

### 4.1 Eligibility

4.1.a **Court denies motion to dismiss divisional merger debtor's filing to address mass tort claims.** A consumer products company was subject to an increasing number of tort claims, some of which resulted from asbestos exposure. The litigation and liability costs exceeded the company's operating income. Using the Texas divisional merger statute to resolve all the tort claims without subjecting the entire enterprise to the bankruptcy process, the company divided into one company that continued the consumer products business, assuming all the assets and the ordinary course liabilities associated with that business, and another that received certain royalty streams and assumed all the tort liabilities. The continuing company agreed, without any reimbursement rights, to fund a trust to resolve the other company's litigation and bankruptcy expenses and tort liabilities to the extent its royalty streams and other assets were insufficient. The funding agreement was limited in amount to the value of the continuing company. The ultimate parent company guaranteed the funding agreement. Immediately after completing the divisional merger, the other company filed a chapter 11 case with the goal of addressing the tort claims through an asbestos claims trust, funded by the royalty streams, the funding agreement, and insurance proceeds. A chapter 11 case that is not filed in good faith is subject to dismissal. Good faith is determined based on the totality of the circumstances, focusing on whether the debtor's objectives are within the legitimate scope of the bankruptcy laws, including whether the petition serves a valid reorganization purpose or is filed merely to obtain a tactical litigation advantage. A desire to take advantage of a particular Bankruptcy Code provision, standing alone, is not determinative. A debtor need not be insolvent to qualify for a chapter 11 case, although to be eligible, it should show a need for a financial restructuring. The mounting costs of the tort claims litigation would likely drive the debtor (and, without the divisional merger, the continuing company) into insolvency, which creates a need for financial relief. Here, the debtor's intent is to use the Code as a whole to address its financial needs. The class action system is not available to address mass tort claims, and using the bankruptcy system, rather than the tort system, is a substantially better approach to addressing both present and future tort claims for both the debtor and the claimants. Because the tort claimants are in no worse position under the divisional merger and bankruptcy filing than they would be otherwise, the filing was not made to secure a tactical litigation advantage. Moreover, the debtor has the funding necessary to satisfy tort obligations to the extent of its pre-merger valuation, with a contractual right to look to the ultimate parent without having to establish independent liability. Finally, the potential business disruption, professional fees, and loss in market value that would likely result from a filing by the pre-merger company justifies the division and concentration of the bankruptcy on the resulting debtor company. *In re LTL Mgmt., LLC*, 2022 LEXIS Bankr. 510 (Bankr. D.N.J. Feb. 25, 2022).

### 4.2 Involuntary Petitions

4.2.a **Convertible notes give rise to contingent claims.** The debtor issued convertible promissory notes, which were convertible at their maturity at the holder's option into equity in the debtor. The holders of the notes filed an involuntary petition against the debtor before the notes' due date. To be an eligible petitioning creditor, the creditor must hold a claim that is not contingent. A claim is contingent if it remains uncertain at the petition date whether the debtor will be liable to pay it. The debtor would not be required to pay the notes if the holders converted. Therefore, the claims were contingent, and the creditors were not eligible petitioners. *In re Qdos, Inc.*, 634 B.R. 552 (Bankr. C.D. Cal. 2021).

4.2.b **Court may award damages only against "petitioners," not against agents who signed the petition.** Three creditors filed an involuntary petition, which the court dismissed. The debtor sought attorneys' fees and damages from the petitioners and from the individuals who signed the petition on behalf of the petitioners. Section 303(i) permits the court to grant judgment in favor of the debtor and against the petitioners for costs, fees, and in some cases, damages. "Petitioner" does not include the individual employees or agents of the entities that hold the claims.

Therefore, the court dismisses the claims against the individuals. *Visium Techs., Inc. v. Tarpon Bay P'ners, LLC (In re Visium Techs., Inc.)*, 635 B.R. 428 (Bankr. S.D. Fla. 2022).

### 4.3 Dismissal

## 5. CHAPTER 11

### 5.1 Officers and Administration

5.1.a **Court approves payment during the case of RSA Parties' professional fees.** Before bankruptcy, the debtor negotiated restructuring support agreements with three ad hoc committees of creditors. The agreements provided for payment of the groups' professional fees. After filing chapter 11, the debtor in possession sought approval of the assumption of the agreements to pay professionals and approval of postpetition agreements to pay professionals of additional ad hoc committees that agreed to the RSA. If the court did not authorize the payments, the committees would be released from any obligation to support a plan on the terms previously agreed, and early indications in the case were that negotiations would have collapsed and would need to start from scratch. Section 363(b) authorizes the debtor in possession to use property of the estate outside the ordinary course of business. Section 365(a) authorizes the debtor in possession, subject to court approval, to assume executory contracts. Both sections permit approval if the debtor in possession's action reflects a valid business justification. The prepetition reimbursement agreements require both sides to cooperate toward confirmation of a plan and require the debtor in possession to pay fees. Therefore, the agreements are executory and subject to assumption under section 365. The potential collapse of negotiations and the attendant increase in expenses supported the judgment to assume the agreements and pay the professionals. Section 503(b)(4) permits payment as an administrative expense, after the fact, of professional fees of creditors who have made a substantial contribution to the case. It provides for retroactive review and payment and does not restrict the court's authority under sections 363 and 365 to approve payments during the case. *City of Rockford v. Mallinckrodt PLC (In re Mallinckrodt PLC)*, 2022 U.S. Dist. LEXIS 54785 (D. Del. Mar. 28, 2022).

### 5.2 Exclusivity

### 5.3 Classification

### 5.4 Disclosure Statement and Voting

### 5.5 Confirmation, Absolute Priority

5.5.a **Unfair discrimination may be measured against a baseline entitlement recovery amount.** The debtors comprised over 60 related entities. Most creditors' claims were against only a few entities, but a class of unsecured notes claims were guaranteed by nearly all entities. The plan provided for a distribution to the notes class of about 90%, which was less than the claims' full entitlement based on the debtors' value, and distribution of substantially lower percentages to seven other unsecured claims classes. The baseline entitlements of many of the seven other classes was zero, but the plan provided for recoveries to those classes derived from the value the notes class was foregoing. Those classes did not accept the plan. Section 1129(b) permits confirmation over the nonacceptance of one or more classes if the plan is fair and equitable to and does not discriminate unfairly against the nonaccepting classes. Unfair discrimination can be measured by relative recoveries between similar priority classes or by comparison of the plan recovery to a hypothetical baseline recovery under the absolute priority rule. Because the nonaccepting classes were receiving a recovery in excess of their baseline amounts as a result of the notes class's acceptance of less than its full absolute priority entitlement, the plan does not discriminate unfairly and may be confirmed. *In re Mallinckrodt PLC*, ___ B.R. ___, Case No. 20-12522 (Bankr. D. Del. Feb. 3, 2022).

## 6. CLAIMS AND PRIORITIES

### 6.1 Claims

6.1.a **Court provides treatise on postpetition interest in solvent debtor case, allowing postpetition interest.** The individual debtor suffered a substantial prepetition judgment. He filed chapter 11 to prevent execution on the judgment. Under applicable nonbankruptcy law, interest on the judgment ran at 12%. Because of favorable postpetition events, the debtor was solvent both in a hypothetical liquidation and on a balance sheet basis and had sufficient assets to pay all creditors in full plus postpetition interest. The debtor proposed a plan that provided for payment in full, without postpetition interest. The class comprising the claims of the judgment creditors did not accept the plan. Section 1129(b) permits plan confirmation over the nonacceptance by a class of unsecured claims if the plan is fair and equitable with respect to the class. The "fair and equitable" requirement incorporates pre-Code law, which required payment of postpetition interest on unsecured claims if the debtor was solvent, and permits the court to consider the equities to determine to appropriate interest rate, despite section 502(b)(2), which disallows postpetition interest as part of an allowed claim. Generally, the contract rate should apply. But the consideration supporting the contract rate—negotiated at arms' length—do not apply to a state-law judgment rate. Still, considering all the factors in this case, including the debtor's ability to pay, the court requires application of the judgment rate for the plan to be fair and equitable. Section 1129(a)(7) requires that a plan provide as much value on claims and interests as would be paid in a liquidation case. Section 726(a)(5) provides for surplus funds to be paid to creditors for interest "at the legal rate." Uniformity within federal law and equality of treatment of creditors require that "the legal rate" be interpreted as the federal judgment rate. *In re Mullins*, 633 B.R 1 (Bankr. D. Mass. 2021).

### 6.2 Priorities

6.2.a **Court may subordinate lien as well as claim under section 510(b).** The creditor and individual debtor were partners in several ventures. After a falling out and litigation, they settled under an agreement that provided for the creditor to transfer all his interests in the ventures and other consideration in exchange for four payments, secured by a lien on the interests in the ventures. The debtor made only two of the payments. The creditor obtained a judgment for breach of the settlement agreement. Section 510(b) provides that a claim "for damages from the purchase or sale of [a security of the debtor or an affiliate of the debtor] … shall be subordinated to all claims or interests that are senior to or equal the claim or interest represented by such security." Because the settlement provided for the sale of the securities in the ventures, it was subject to subordination under section 510(b), even though the judgment arose from a claim for violation of the settlement agreement that resulted in the sale. Because the settlement agreement did not apportion the payments between payments for interests in the ventures and the other consideration, the entire claim was subordinated. Even though section 510(b) addresses only claims, it permits the court to subordinate liens as well. The term "claim" encompasses the right to payment, whether personal or *in rem*. Failure to subordinate the lien would defeat the purpose of section 510(b). Therefore, the creditor's claim may receive a distribution only after all general unsecured claims are paid in full. *Kurtin v. Ehrenberg (In re Elieff)*, 2022 Bankr. LEXIS 711 (9th Cir. B.A.P. Mar. 21, 2022).

6.2.b **Underfunded defined benefit pension plan liability is not an administrative expense.** The debtor maintained a defined benefit pension plan for its employees. At the petition date, there was a substantial underfunding liability. During the chapter 11 case, the debtor in possession continued to employ the employees and incurred administrative and current service liabilities for the plan. Section 503(b) grants administrative expense priority to the actual and necessary costs of preserving the estate. Employee compensation is such an expense. But only the administrative and current expenses of the plan are payable on account of the employees' postpetition services. The underfunding liability existed at the petition date and arose because of prepetition services.

Accordingly, the underfunding liability is not an administrative expense. *In re Verity Health Sys. of Cal.*, 633 B.R. 607 (Bankr. C.D. Cal. 2021).

## 7. CRIMES

## 8. DISCHARGE

### 8.1 General

**8.2** ***Taggart v. Lorenzen*** **applies to violations of chapter 11 plan confirmation orders.** The debtors confirmed a chapter 11 plan that provided for reinstatement of payments on a home mortgage, although the amount of payments required was unclear. The new mortgage servicer determined that the debtors had not made payments during the chapter 11 case and began foreclosure proceedings. The debtors sought a contempt citation for violating the plan's terms. *Taggart v. Lorenzen*, 139 S. Ct. 1795 (2019), held that a civil contempt citation for violating a chapter 7 discharge order required the same findings as any contempt citation for violating an injunction. A "bankruptcy court's authority to enforce its own orders … derives from the same statutes and the same general principles the Supreme Court relied on in *Taggart*." Therefore, the *Taggart* standard applies equally to any contempt proceeding for violating a chapter 11 plan's terms. *Beckhart v. Newrez, LLC*, ___ F.4th ___, 2022 U.S. App. LEXIS 10287 (4th Cir. Apr. 15, 2022).

### 8.3 Third-Party Releases

8.3.a **Chapter 11 plan release of an "affiliate" does not include a creditor's direct claims against the affiliate.** The debtor leased a retail store. Its parent unconditionally guaranteed the lease. Because of the pandemic, the debtor never opened the store and filed chapter 11. The plan released claims of creditors against affiliates (among others) that arise out of or relate to the debtor. The release should be read to release only claims that are derivative of the debtor's claims, not an independent obligation, such as a guarantee, that the parent owed to the lessor. *605 Fifth Prop. Owner, LLC v. Abasic, S.A.*, 2022 U.S. Dist. LEXIS 41123 (S.D.N.Y. Mar. 8, 2022).

### 8.4 Environmental and Mass Tort Liabilities

## 9. EXECUTORY CONTRACTS

9.1.a **U.S. government may waive Anti-Assignment Act.** The debtor leased a hotel and related facilities from a "non-appropriated fund instrumentality" of the United States. The lease and contract prohibited assignment without the government's consent, which consent was not to be unreasonably withheld. The debtor in possession moved for approval of the assumption of the lease and related contracts. Section 365(c) prohibits assumption of a contract that is non-assignable under applicable non-bankruptcy law. The federal Anti-Assignment Act prohibits assignment of a contract with the U.S. government without the government's consent. Under applicable circuit law, the court applies the "hypothetical test" to determine whether the debtor in possession may assume a contract or lease that is otherwise non-assignable. Here, the hypothetical test would ordinarily prohibit contract assumption. But the government may waive the Anti-Assignment Act and may do so prospectively. By limiting its power in the lease to reject assignments, the government waived the assignment prohibition of the Anti-Assignment Act. *In re Minesen Co.*, 2021 Bankr. LEXIS 3178 (Bankr. D. Haw. Nov. 17, 2021).

## 10. INDIVIDUAL DEBTORS

### 10.1 Chapter 13

### 10.2 Dischargeability

10.2.a **FCC nonpecuniary penalty is nondischargeable in a chapter 11 case.** The telecommunications provider debtor defrauded customers. The FCC brought an action against the debtor, in which the debtor agreed to reimburse customers and pay a civil penalty to the FCC, which was not defrauded and did not suffer loss. Section 1141(d)(6) makes nondischargeable in a corporate case any debt that would be excepted from discharge under section 523(a)(2), which excepts from discharge in an individual case any debt for money, property, or services to the extent obtained by fraud or false pretenses. In *Cohen v. de la Cruz*, 523 U.S. 213 (1998), the Supreme Court held that nonpecuniary loss penalties (in that case, treble damages) arising from a debtor's fraud fell within section 523(a)(2) because "to the extent obtained by" modifies "money, property, or services," not "any debt." Because section 1141(d)(6) makes section 523(a)(2) applicable in a corporate chapter 11 case, the FCC penalty is nondischargeable. *U.S. v. Fusion Connect, Inc. (In re Fusion Connect, Inc.)*, 634 B.R. 22 (S.D.N.Y. 2021).

### 10.3 Exemptions

### 10.4 Reaffirmations and Redemption

## 11. JURISDICTION AND POWERS OF THE COURT

### 11.1 Jurisdiction

### 11.2 Sanctions

11.2.a **Court distinguishes sources of bankruptcy court's sanction authority.** Debtor's counsel filed a chapter 7 case as a litigation tactic, omitted substantial assets and transfers from the schedules and statement of affairs, failed to ensure that the debtor complied with the trustee's information requests, used state court litigation, including an action against the chapter 7 trustee, to attempt to dismiss the case, withdrew as attorney of record yet still moved to dismiss the case. A bankruptcy court may sanction counsel under Bankruptcy Rule 9011, under section 105(a), and under its inherent authority. Sanctions under Rule 9011 may be imposed only for filing a paper with the court in violation of the requirements of that Rule. Sanctions under section 105(a) may be imposed for civil contempt to remedy a violation of a specific order, including an "automatic" order such as the automatic stay or discharge injunction. Sanctions under the court's inherent authority may be imposed to deter and provide compensation for improper litigation tactics, including bad faith litigation tactics. This last power is broader than the other two, is not mutually exclusive with the others, and extends to the full range of litigation abuses. It requires a finding of recklessness plus frivolousness, harassment, or an improper purpose or of bad faith (or conduct tantamount to bad faith). Here, although the bankruptcy court imposed sanctions under section 105(a), counsel's conduct amounted to improper litigation tactics and purpose and bad faith and should have been imposed under the court's inherent power. But because the bankruptcy court made sufficient finding to support sanctions under its inherent authority, the appellate court affirms the award. *Stanley v. Mason (In re BCB Contracting Servs., LLC)*, ___ B.R. ___ (9th Cir. B.A.P. Apr. 21, 2022) (unpublished).

### 11.3 Appeals

11.3.a **Notice of appeal on main case docket does not bring up adversary proceeding order for review.** The confirmed plan established a litigation trust with a limited life, vested causes of action in the trust, and continued the automatic stay to protect the trust. Former shareholders brought an action in the bankruptcy court that belonged to the trust. The trustee moved to dismiss the adversary proceeding and sought sanctions. The bankruptcy court issued an order in the

adversary proceeding dismissing it and an order in the main bankruptcy case granting sanctions. The shareholders filed a notice of appeal in the main case but not in the adversary proceeding, attaching a copy of only the sanctions order. The main case and the adversary proceeding are distinct for purposes of appeal. Moreover, Bankruptcy Rule 8003(a)(3)(B) requires an appellant to attach a copy of the order appealed from to the notice of appeal. Therefore, the notice of appeal in this case did not bring up the dismissal order for review, and the court of appeals lacked jurisdiction to hear it. *Kreit v. Quinn (In re Cleveland Imaging and Surg. Hosp., L.L.C.)*, 26 F.4th 285 (5th Cir. 2022).

11.3.b **Court denies defendant standing to appeal approval of trustee's litigation funding order.** The liquidating trustee under a chapter 11 plan entered into a litigation funding agreement to pursue claims against the debtor's bank. The agreement required the trustee to consult in good faith with the funder over any settlement discussions. The bank objected, contending that the funder would unduly influence the litigation and prevent settlement. As of the time of the bank's appeal, no settlement discussions had occurred. To appeal, a party must have Article III standing and be a "person aggrieved." Article III standing requires a concrete, particularized, and imminent injury in fact. Here, the bank's injury is not imminent but is speculative, based on an attenuated chain of possibilities, because no settlement discussions have taken place, and the result of any future discussions is uncertain. An appellant is a person aggrieved only if it has a direct and substantial interest in the question being appealed. Being subject to litigation and risking liability in an adversary proceeding is not such an interest. Moreover, the interest must be one the Code protects or regulates. A defendant's interest in avoiding liability is antithetical to the Code's goals. Finally, a desire to preserve the integrity of the bankruptcy process is not sufficient to give an appellant "person aggrieved" status. Therefore, the bank lacks standing to appeal. *Valley Nat'l Bank v. Warren (In re Westport Holdings Tampa, Ltd. P'shp)*, ___ 4th ___, 2022 U.S. App. LEXIS 8480 (11th Cir. Mar. 31,

### 11.4 Sovereign Immunity

11.4.a **Section 106 abrogates U.S. sovereign immunity for actions under section 544(b).** The trustee sued the United States under section 544(b), relying on state fraudulent transfer law, to avoid tax penalty obligations and to recover the tax penalty payments. The United States would have a sovereign immunity defense to an action by a creditor under a state fraudulent transfer law. Section 106(a) abrogates sovereign immunity for actions under section 544. Therefore, the trustee is not barred by sovereign immunity from suing the United States. *Cook v. U.S. (In re Yahweh Center, Inc.)*, 27 F.4th 960 (4th Cir. 2022).

## 12. PROPERTY OF THE ESTATE

### 12.1 Property of the Estate

12.1.a **Liquidation trustee has standing to defend appeal even after termination of the trust.** The confirmed plan established a litigation trust with a limited life, vested causes of action in the trust, and continued the automatic stay to protect the trust. After the trust terminated, former shareholders brought an action in the bankruptcy court that belonged to the trust. The trustee sought sanctions, which the bankruptcy court granted and the shareholders paid. The shareholders appealed. An appellate court does not have jurisdiction over an appeal unless both parties have standing. An appellee must show an ongoing interest in the dispute. Although the trust had terminated, the trustee had the payment from the shareholders and still had an obligation to return trust property to the beneficiaries. Therefore, even though the trustee lacked wind-up power, he had an interest in defending the appeal, which gives him standing. *Kreit v. Quinn (In re Cleveland Imaging and Surg. Hosp., L.L.C.)*, 26 F.4th 285 (5th Cir. 2022).

12.1.b **Liquidation trustee may continue litigation after trust terminates if trust agreement so provides.** The confirmed plan established a liquidation trust to prosecute claims against third

parties. The trustee brought the claims; the court denied motions to dismiss, and the litigation was in discovery. After the filing of the complaint and the motions to dismiss but before the court's denial of the motions, the trust terminated by the terms of the trust agreement. However, the trust agreement also provided that after termination, "for the purpose of liquidating and winding up the affairs of the Liquidation Trust, the Liquidation Trustee "shall continue to act as such until its duties have been fully performed." Because the trust agreement requires the trustee to continue to act after the trust terminates, and because the trustee has not "fully performed" his duties while litigation remains pending, the trustee retains standing to prosecute litigation that he commenced before termination. Therefore, the court denies the defendants' motion to dismiss the litigation. *Energy Conversion Devices Liquidation Trust v. Ovonyx, Inc. (In re Energy Conversion Devices, Inc.)*, 634 B.R. 537 (Bankr. E.D. Mich. 2021).

12.1.c **Lender is liable for concealment, excessive fees, breach of loan agreement, and fraud.** After a new lender's due diligence over several months, the debtor entered into replacement financing facility with the new lender, comprising an accounts receivable factoring and an inventory line of credit. Within months, the lender declared a default over a minor, curable breach and began reducing availability under the lines. Though availability remained, the lender represented otherwise to the debtor and refused to advance, despite continuing to collect all the debtor's receivables. The lender also took over payment of the debtor's payables, dictating which vendors would be paid. The lender also charged excessive fees that were not authorized by the credit agreement and refused to disclose the charges to the debtor. The lender then promised to restore availability if the debtor's principal pledged his homestead but reneged after receiving the pledge. The lender then terminated the agreements but continued to collect all receivables, even after internal documents showed that the debtor's obligations had been satisfied in full. All the while, the lender's internal emails showed malice and an intent to destroy the debtor's business. The debtor filed a chapter 11, but the business failed. The principal and the chapter 7 trustee sued the lender under multiple theories. The lender breached the credit agreements by withholding the debtor's accounts receivable collections and demanding that the debtor continue to send new receivables to the lender even after termination of the agreement. The breaches caused the loss of the debtor's legacy business; the lender was liable to the debtor for its value. It also caused the loss of an anticipated future business line, and the lender was liable for that value too. When a lender takes excessive control over a business, it becomes a fiduciary and owes a duty of transparency and loyalty. Here, the lender breached those duties. The lender also defrauded the debtor by misrepresenting the lack of availability under the credit lines and concealing information about fees and charges, which were not authorized. The court holds the lender liable for breach of contract and breach of the duty of good faith and fair dealing, fraudulent misrepresentation, the tort of contractual and business interference, and willful automatic stay violations (to the extent the withholding of collections occurred after the petition date). *Bailey Tool & Mfg. Co. v. Republic Bus. Credit, LLC (In re Bailey Tool & Mfg. Co.)*, 2021 Bankr. LEXIS 3502 (Bankr. N.D. Tex. Dec. 23, 2021).

**12.2 Turnover**

**12.3 Sales**

12.3.a **Buyer with actual knowledge of adverse interest is not a good faith purchaser under section 363(m).** A partnership granted a right of first refusal over a real estate parcel; the grantee recorded the right in the land records office. The partnership later dissolved, and the individual partners obtained the real estate. The individual partners filed bankruptcy. They did not list the grantee as a creditor or party in interest. The trustee sold the parcel free and clear of adverse interests to a buyer who had searched the land records and learned of the right. Neither the trustee nor the buyer notified the grantee of the sale. Later, the buyer sought to sell the parcel. The grantee objected and sued in state court to assert the right. Section 363(m) provides that an appellate court's reversal or modification of an order approving a sale may not affect the validity of a sale to a good faith purchaser of property of the estate. Section 363(m) applies broadly to protect any good faith purchaser's interest and so would protect the buyer here if in good faith.

However, the buyer's constructive knowledge (through the recorded interest) and actual knowledge (through its examination of the land records) of the adverse interest and its failure to notify the grantee or the court of the right prevented the buyer from being a good faith purchaser. *Archer-Daniels-Midland Co. v. Country Visions Coop.*, ___ F.4th ___, 2022 U.S. Ap.. LEXIS 9008 (7th Cir. Apr. 4, 2022).

## 13. TRUSTEES, COMMITTEES, AND PROFESSIONALS

### 13.1 Trustees

13.1.a **Barton doctrine applies to a subpoena issued to an estate fiduciary.** The chapter 7 trustee received two subpoenas from a federal criminal case pending in another district, seeking production of information in the trustee's possession. The *Barton* doctrine requires leave of the bankruptcy court before one may bring any legal proceeding against a trustee in another forum. Without leave, the other forum is without jurisdiction to hear the matter. A subpoena is an order of the issuing court commanding the recipient to appear in another court and may require a trustee who receives a subpoena to expend estate assets to comply, defend, or face contempt proceedings for noncompliance. In addition, a subpoena may seek to control information that is property of the bankruptcy estate in potential violation of the automatic stay. Another court may not interfere with such property or, in effect, order the trustee to expend estate property to address the subpoena. Therefore, the *Barton* doctrine applies to a subpoena as much as to an action against an estate fiduciary. *In re Eagan Avenatti, LLP*, 2022 Bankr. LEXIS 552 (Bankr. C.D. Cal. Mar. 3, 2022).

### 13.2 Attorneys

13.2.a **Court may not award attorney compensation for performing trustee duties.** The trustee employed counsel to assist in administering the estate. The trustee ultimately paid all claims and returned a surplus to the debtor. The attorney's services included some tasks that might have been part of the trustee's duties, such as reviewing the debtor's records, liquidating property of the estate, and investigation the debtor's financial affairs. Section 330(a) permits the court to authorize fees for actual, necessary services rendered by an attorney for the trustee. Section 704 specifies the trustee's duties. It is not "necessary" (or proper) for an attorney to perform any of the trustee's duties, since the trustee must perform them. Section 326 fixes the trustee's compensation as a commission. The trustee may not evade section 326's limits by delegating some of the duties to an attorney, who would be compensated separately. Finally, section 327 permits the trustee to serve as attorney or accountant for the estate, and section 328 limits the compensation for doing so to compensation for services generally performed by the trustee without the assistance of a professional. Taken together, these provisions require the court to scrutinize an attorney's services to ensure the attorney is not compensated for trustee services. The existence of a surplus estate does not lessen the court's duty. *Sylvester v. Chaffee McCall, L.L.P. (In re Sylvester)*, 23 F.4th 543 (5th Cir. 2022).

13.2.b **Court may approve attorney employment retroactively to petition date.** The debtor in possession filed an "ordinary course professionals" motion two days after the petition date, seeking to employ attorneys in the ordinary course, with approval *nunc pro tunc* to the petition date. The court granted the motion. Three months later, the debtor in possession filed a motion to employ one of the ordinary-course attorneys under section 327(e), *nunc pro tunc* to the petition date. In *Roman Catholic Archdiocese of San Juan v. Acevedo Feliciano*, 140 S. Ct. 696 (2020), the Supreme Court prohibited the use of *nunc pro tunc* orders except to reflect on the docket what had actually occurred. However, that case involved the lower court's jurisdiction, which could not be created retroactively. Properly read, the decision does not prohibit a court of equity "to deem an action to have been taken as of a time when it should have been taken, but was not due to circumstances not attributable to the laches of the parties." This principle permits a bankruptcy court, under appropriate circumstances, which are present here, to approve

employment of professionals retroactive to the petition date. *City of Rockford v. Mallinckrodt PLC*, 2022 U.S. Dist. LEXIS 54786 (D. Del. Mar. 28, 2022).

### 13.3 Committees

### 13.4 Other Professionals

### 13.5 United States Trustee

## 14. TAXES

## 15. CHAPTER 15—CROSS-BORDER INSOLVENCIES

15.1.a **Section 109 eligibility requirements do not apply in chapter 15.** The foreign debtor did not own any property in the United States but owned a corporation that owned U.S. property. The foreign representatives sought recognition of the debtor's foreign proceeding. Section 109 permits only an entity with a domicile, a residence, property, or a place of business within the United States to be a debtor under the code. Section 103 provides that chapter 1 (which includes section 109) applies in a case under chapter 15. Section 1502(1) defines "debtor for purposes of chapter 15 as "an entity that is subject of a foreign proceeding." Section 1517 provides the court shall grant recognition if the foreign proceeding is a foreign main proceeding or a foreign nonmain proceeding, the foreign representative is a person or body, and the petition meets section 1515's requirements. Because chapter 15 uses a special definition of "debtor," section 109's eligibility requirements, which apply to a debtor as defined more generally in section 101, do not apply, and the mandatory language of section 1517 requires the court to grant recognition if section 1517's conditions are met. The court grants recognition. *In re Al Zawawi*, 634 B.R. 11 (Bankr. M.D. Fla. 2021).

15.1.b **Debtor's or foreign representative's bad faith is not a ground to deny recognition.** The foreign debtor and the foreign representative acted together in bad faith in filing a petition seeking recognition of a Monegasque insolvency proceeding. Section 1501 states the purposes of chapter 15, including to "promote fair and efficient administration of cross-border insolvencies" and "protect the interests of all creditors." Section 1517 requires recognition of a foreign proceeding if the petition meets section 1515's requirements. Section 1506 permits a court to deny recognition is it would be manifestly contrary to U.S. public policy. Section 1501 is not intended to confer any substantive rights, is intended only to assist in interpretation, and therefore is not a ground to deny recognition. Section 1506 applies only to the foreign law, not to the conduct of the debtor or the foreign representative. Here, the Monegasque insolvency regime, though differing in substantial ways from U.S. law, is not manifestly contrary to U.S. public policy. Therefore, the court must grant recognition to the Monegasque proceeding. The court may deal with bad faith through other means, including abstention under section 305, granting stay relief, or modifying or terminating recognition under section 1517(d) if grounds for granting it were fully or partially lacking or ceased to exist. *Samba v. Int'l Petro. Prods. and Additives Co., Inc. (In re Black Gold S.à.R.L.)*, 635 B.R. 517 (9th Cir. B.A.P. 2022).

# Faculty

**Hon. Benjamin A. Kahn** is a U.S. Bankruptcy Judge for the Middle District of North Carolina in Greensboro, sworn in on Feb. 3, 2014. He also is the chair of the Advisory Committee on Bankruptcy Judge Education for the Federal Judicial Center, for which he serves as one of the instructors for Phase I and Phase II Orientation for Newly Appointed Bankruptcy Judges. Judge Kahn is a member of the U.S. Judicial Conference Advisory Committee on the Bankruptcy Rules, and is chair of its Forms Subcommittee. In addition, he is a conferee of the National Bankruptcy Conference, for which he previously served on the Executive Committee and currently serves as chair of the Committee on the Court System and Bankruptcy Administration and on the Nominating Committee. Judge Kahn is a contributing author and member of the board of editors for *Collier on Bankruptcy* and serves as the judicial chair of ABI's Southeast Bankruptcy Workshop. Prior to his appointment, he was a member of Nexsen Pruet PLLC and clerked for Bankruptcy Judge Jerry G. Tart of the Middle District of North Carolina. Judge Kahn is certified as a specialist in business and consumer bankruptcy law by the American Board of Certification, for which he served as a member of its board of directors until his appointment to the bench. Prior to joining the bench, Judge Kahn was a certified mediator in North Carolina and was recognized as among the Top 10 North Carolina *Super Lawyers* across all practice areas for the two years immediately preceding his appointment, elected to the Legal Elite Hall of Fame by *Business North Carolina Magazine* in 2014 as the category winner in North Carolina for Bankruptcy, and was included among Band 1 bankruptcy practitioners in North Carolina in *Chambers and Partners USA*. He received his B.A. in political science and history in 1990, and his J.D. with honors in 1993, from the University of North Carolina at Chapel Hill.

**Hon. Sage M. Sigler** is a U.S. Bankruptcy Judge for the Northern District of Georgia in Atlanta, appointed in March 2018. She succeeded Hon. Mary Grace Diehl, for whom she clerked after graduating from law school. Prior to her appointment to the bench, Judge Sigler was a partner in Alston & Bird LLP's Bankruptcy Group. She is an active member of ABI, IWIRC and the Bankruptcy Section of the Atlanta Bar Association, and she enjoys being a volunteer presenter for the Credit Abuse Resistance Education (CARE) program. Judge Sigler was an honoree in ABI's inaugural class of "40 Under 40" in 2017. She received her B.A. in political science from the University of Florida in 2001 and her J.D. in 2006 from Emory University School of Law, where she was the executive symposium editor of the *Emory Bankruptcy Developments Journal*.

**Prof. Lindsey Simon** is an assistant professor of law at the University of Georgia School of Law in Athens, Ga., where she teaches courses in bankruptcy and secured transactions. Her research focuses on the bankruptcy system, drawing concepts from bankruptcy structure and procedure to address broader institutional design challenges. Prof. Simon's articles have been published in the *Administrative Law Review*, *Cardozo Law Review*, *Indiana Law Journal* and *North Carolina Law Review*. Her most recent scholarship addresses the intersection between mass torts and bankruptcy, including an article on nondebtor relief in chapter 11 forthcoming in the *Yale Law Journal*. Prof. Simon has assisted academics, judges, members of Congress and many other stakeholders on the subject of mass-tort bankruptcies, and her commentary in connection with the Purdue Pharma, Boy Scouts of America and USA Gymnastics bankruptcies has appeared in various media outlets, including *The Wall Street Journal*, *The New York Times*, *Forbes*, *The Economist*, NPR and Reuters.

Before coming to UGA in 2018, she was an associate at Kilpatrick Townsend & Stockton, where her practice involved a mix of commercial litigation and corporate restructuring matters. She represented corporations, committees and individuals in state and federal litigation, both in and out of the bankruptcy context. Prof. Simon also practiced at a litigation boutique in Chicago and clerkwed for Hon. Beverly B. Martin at the U.S. Court of Appeals for the Eleventh Circuit. Additionally, she taught as an adjunct professor at the Georgia State University College of Law. Prof. Simon is an active member of ABI, where she serves as a member of its Diversity Working Group. She previously served as vice chair and community service co-chair for the Georgia Network of the International Women's Insolvency & Restructuring Confederation and as vice president of the board of directors of the Georgia Latino Law Foundation. Prof. Simon received her B.Mus. *magna cum laude* and her M.Ed. from Vanderbilt University, and her J.D. *magna cum laude* from the Northwestern University Pritzker School of Law.