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Consumer Update: Hot Topics in Consumer Law

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AMERICAN BANKRUPTCY INSTITUTE

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

In re:

QUICK CASH, INC.,

Case No. 15-11800-j11

Debtor.

**CONSUMER CLAIMANTS' COMMITTEE'S MOTION TO APPLY FED. R. BANKR. P
7023 TO THE CLAIMS ALLOWANCE AND DISALLOWANCE PROCESS AND TO
IMPLEMENT A SCHEDULE FOR CERTIFYING CLASS CLAIMS**

The official Consumer Claimants' Committee of the Quick Cash, Inc. bankruptcy estate (the "**Committee**"), by counsel, pursuant to 11 U.S.C. §§ 105(a), and other applicable law, if any, moves the Court to apply Fed. R. Bankr. P. 7023 to the claims allowance and disallowance process and to implement a schedule for certifying class claims, and in support thereof states:

BACKGROUND

1. On July 6, 2015 (the "**Petition Date**"), Quick Cash, Inc. (the "**Debtor**") commenced this bankruptcy case by filing a voluntary petition for relief under chapter 11 of the Bankruptcy Code. Pursuant to Bankruptcy Code §§107(a) and 1108, Debtor has retained possession of its assets, as Debtor in Possession.

2. On September 23, 2015 this Court entered an Order Extending Claims Bar Date (Doc. No. 45), which extended the bar date for filing proofs of claim in this bankruptcy case through until December 23, 2015.

3. On October 2, 2015 the Court entered a *Scheduling Order Resulting from Preliminary Hearing on Emergency Motion to Enforce Settlement Agreement and Request for Hearing*, (Doc. No. 52) which, *inter alia*, set a deadline of October 9, 2015, to file any motions requesting special noticing procedures, or any special class procedures.

4. The Committee and the Debtor are engaged in discovery and have agreed to an extension of the deadlines to submit motions requesting special noticing and claims procedures, other than an extension of the deadline to request application of Fed. R. Bankr. P. 7023 to the claims allowance and disallowance process.

5. As a result, this Motion is not intended to be a comprehensive statement of the Committee's requested claims and noticing procedures, but only reflects one component thereof: the request by the Committee for the Court to apply Fed. R. Bankr. P. 7023 to the claims allowance and disallowance process.

6. The Committee intends to request additional claims and noticing procedures by separate motion in accordance with the briefing schedule agreed by the Committee and the Debtor.

CLASS CLAIMS PROCEDURES

Based on the fact that there are at least six thousand identified Consumer Claimants thus far, and are likely a very large number of as-yet-unidentified Consumer Claimants, the Committee moves the Court to establish class claims procedures. There is potential in this case to have thousands of proofs of claim, many of which are likely, based on the disadvantaged and unsophisticated nature of the Consumer Claimants, to be filled out incorrectly or incompletely. Additionally, as is frequently done in mass tort cases, the Committee believes that a customized proof of claim form specific to the Consumer Claimants would be of significant benefit in assisting Consumer Claimants in filing clear, coherent proofs of claim which can be analyzed and administered effectively and efficiently.

The Committee requests that this Court apply Fed. R. Bankr. P. 7023 to the claims allowance and disallowance process to permit the filing of class claims. In 1994, the United States District Court for the District of Colorado, addressed the issue of whether class proofs of

claim were permitted in bankruptcy, on appeal. *Jones v. Amdura Corp. (In re Amdura Corp.)*, 170 B.R. 445 (D. Colo. 1994). In *Amdura*, The bankruptcy court had determined that class claims could not be permitted in bankruptcy on the basis of the Tenth Circuit’s decision in *Sheftelman v. Standard Metals Corp.*, 817 F.2d 625, (10th Cir. 1987) (hereinafter, “**Standard Metals I**”). *Id.* at 446-7. However, the Tenth Circuit’s statement upon rehearing in *Standard Metals II* that “[i]n view of the disposition of this appeal it is not necessary to consider the class action claims issue” indicates that any discussion of class claims in *Standard Metals I* is dictum. *Id.* (quoting *Sheftelman v. Standard Metals Corp.*, 839 F.2d 1383, 1387 (10th Cir. 1987) *cert. dismissed* 477 U.S. 811, 109 S.Ct. 201 (1988) (hereinafter, “**Standard Metals II**”). *See also Certified Class in Charter Securities Litigation v. Charter Co. (In re The Charter Co.)*, 876 F.2d 866, 869 n. 4, (11th Cir. 1989) *cert. dismissed* 496 U.S. 944, 110 S.Ct. 3232 (1990) (stating that the discussion of class proofs of claim in *Standard Metals I* may be dictum). The *Amdura* court found that since the Tenth Circuit’s discussion of class proofs of claim in *Standard Metals I* was not necessary to the decision of the case, it was dictum, and therefore “not binding as authority within the stare decisis rule...even on courts inferior to that from which it emanated.” *Amdura*, 170 B.R. at 448 (citing *McDaniel v. Sanchez*, 452 U.S. 130, 141 (1981); *United States v. 5,935 Acres of Land, Tax Map Key (3)2-8-017-43, Honomu*, 752 F. Supp. 359, 632 (D. Hawaii 1990)).

After rejecting the Tenth Circuit’s commentary on class claims as not controlling, the *Amdura* Court went on to find that bankruptcy courts have discretion to invoke Fed. R. Bankr. P. 7023 and thereby invoke the class action rule at any stage of a contested matter, including the claims allowance and disallowance process, via Fed. R. Bankr. P. 9014(c). *Amdura*, 170 B.R. at 448-449. This is in accordance with the majority view of courts nationwide. *See In re Adam Aircraft Industries Inc.*, 2009 WL 2100929 at * 5-7 (D. Colo. 2009) (collecting and summarizing

cases). See, e.g. *In re American Reserve Corp.*, 840 F.2d 487, 492-494 (7th Cir. 1988) (Easterbrook, J.). As the Fourth Circuit has said, the view that class claims cannot be filed in bankruptcy “is unduly cramped and unsuited for application by a court in equity, seeking, by application of the Bankruptcy Rules, to accomplish the purposes of the Bankruptcy Act. The Bankruptcy Rules are tools, which include Rule 7023 and derivatively Civil Rule 23, by which the bankruptcy court as a court of equity is to accomplish the Act’s purposes.” *Gentry v. Siegel*, 668 F.3d 83, 89 (4th Cir. 2012) (citations omitted).

In addition to the District of Colorado, and the Fourth and Seventh Circuits, the Second Circuit, Sixth Circuit, Ninth Circuit, Eleventh Circuit, and the First Circuit Bankruptcy Appellate Panel, as well as numerous lower courts have all found that class claims are permitted in bankruptcy cases. See *In re Dynegy, Inc.*, 770 F.3d 1064, 1069-70 (2nd Cir. 2014); *Reid v. White Motor Corp.*, 886 F.2d 1462, 1469 (6th Cir. 1989); *In re Birting Fisheries Inc.*, 92 F.3d 939 (9th Cir. 1996); *In re The Charter Co.*, 876, F.2d 866 (11th Cir. 1989); *In re Trebol Motors Distribution Corp.*, 220 B.R. 500, 502 (BAP 1st Cir. 1998); *In re Kaiser Group Intern. Inc.*, 278 B.R. 58, 62 (Bankr. D. Del. 2002) (collecting cases). The Eleventh Circuit, in determining whether to permit class claims, found that legislative history “evinces a congressional intent to open bankruptcy proceedings to the widest range of possible ‘players.’” *Charter*, 876, F.2d at 870 (11th Cir. 1989). That is precisely the goal furthered by permitting class claims. “Because claims may be contingent or of uncertain value, potential claimants may not realize that they can recover, unless the efforts of a representative make them aware...[I]kewise, the effort and cost of investigating and initiating a claim may be greater than many claimants’ individual stake in the outcome, discouraging the prosecution of these claims absent a class action filing procedure.”

| *Id.* at 871 (citing *American Reserve*, 840 F.2d at 489).

The Committee believes that the majority view, permitting application of Fed. R. Bankr. P. 7023 to filing proofs of claim is correct. Fed. R. Bankr. P. 9014 permits Fed. R. Bankr. P. 7023 to be applied to “any stage” in a contested matter. Fed. R. Bankr. P. 9014(b). As Judge Easterbrook stated, “[f]iling a proof of claim is a ‘stage.’” *American Reserve*, 840 F.2d at 488. The dictum regarding class claims in the *Standard Metals I* decision focuses on whether the filer of such a claim would be an “authorized agent” under Fed. R. Bankr. P. 3001(b) and 11 U.S.C. § 501. *See Standard Metals I*, 817 F.2d at 631. However, as Judge Easterbrook explained “Section 501 does not interfere with filing by agents. The representative in a class action is an agent for the missing.” *American Reserve*, 840 F.2d at 493. The Committee believes that Judge Easterbrook is correct. If a class is certified and Fed. R. Bankr. P. 7023 is applied to the claims administration process, a class representative has sufficient authority to sign a proof of claim on behalf of all members of such class. *American Reserve*, 840 F.2d at 493. Should there be any doubt regarding the authority of a class representative to do so, this Court could provide such authority to class representatives under its 11 U.S.C. § 105(a) powers.

In this case, since the Debtor filed bankruptcy before the United States District Court for the District of New Mexico could rule on class certification in *Tullie et al. v. Quick Cash Inc.*, Case No. 1-14-CV-00491 (the “**Tullie Case**”), no class has yet been certified under Fed. R. Civ. P. 23. In the Tullie Case, the to-be-certified class includes persons who, within four years of the filing of the complaint, were charged a \$25 “application fee” which was not disclosed as a finance charge, and/or who did not receive disclosure of the date and frequency of payments. *See Plaintiff’s Brief in Support of Motion for Class Certification*, Tullie Case, Doc. No. 67, p. 2. In addition to the to-be-certified-class in the *Tullie* case, the Committee believes that there are additional potential classes of Consumer Claimants, including:

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- a. Claims based on unlawful repossessions by the Debtor, under both New Mexico and tribal law;
- b. Claims based on loan splitting and multiple refinancing issues; and
- c. Claims based on unlawful withholding of important original documents, including social security cards and vehicle titles.

Thus, the Committee proposes that the Court enter an order (1) applying Fed. R. Bankr. P. 7023 to the claims filing process, (2) setting a deadline by which class certification must be requested, (3) setting a date for the final hearing on class certification for any classes requesting certification (the “**Certification Hearing**”), including witness and exhibit list deadlines, (4) setting a date by which any classes certified as a result of the Certification Hearing must file a class proof of claim, and (5) ordering that the representative of any class which becomes certified shall have authority under Fed. R. Bankr. P. 3001(b) to file a class proof of claim as an agent for such class.

The Committee believes that given the socio-economically disadvantaged nature of the Consumer Claimants, the majority of whom are Navajos, the proposed procedures are necessary to protect the rights of the Consumer Claimants. The Committee believes that in the event the Consumer Claimants are treated as sophisticated parties, and required to file individual proofs of claim, that a great number of the Consumer Claimants will fail to realize they have a claim against the Debtor for violating their legal rights, or fail to understand how the bankruptcy system works, and not file proofs of claim at all. This is particularly likely given the very large number of potential Consumer Claimants. On the other hand, the Committee believes that the proposed procedures go a long way towards ensuring that the rights of the majority of Consumer Claimants are protected.

WHEREFORE the Trustee requests that the Court enter an Order (1) applying Fed. R. Bankr. P. 7023 to the claims filing process, (2) setting a deadline by which class certification

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must be requested, (3) setting a date for the final hearing on class certification for any classes requesting certification (the “**Certification Hearing**”), including witness and exhibit list deadlines, (4) setting a date by which any classes certified as a result of the Certification Hearing must file a class proof of claim, and (5) ordering that the representative of any class which becomes certified shall have authority under Fed. R. Bankr. P. 3001(b) to file a class proof of claim as an agent for such class.

Respectfully submitted,

ASKEW & MAZEL, LLC

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*Proposed Attorneys for the Consumer
Claimants' Committee*

This certifies that on October 9, 2015 a copy of the foregoing pleading was served by the Bankruptcy Court’s electronic filing system on all parties who have entered an appearance in this case.

s/ filed electronically
Daniel A. White

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UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

In re:

QUICK CASH INC., a New Mexico Corporation,
Debtor

CAROLINE TULLIE, on her own behalf
as next friend of NELSON TULLIE,
and on behalf of all others similarly situated,

Plaintiff,

v.

Case No. 15-11800-j11

QUICK CASH, INC.,
d/b/a CASH COW LOAN CO.,

Defendant.

**PLAINTIFF CAROLINE TULLIE'S MOTION TO ALLOW CLASS PROOFS OF CLAIM,
TO APPLY FED. R. BANKR. P. 7023 TO THE CLAIMS ALLOWANCE
AND DISALLOWANCE PROCEDURE
AND TO IMPLEMENT A SCHEDULE FOR CERTIFYING CLASS CLAIMS**

Plaintiff Caroline Tullie, through counsel, respectfully requests that the Court allow class proofs of claim; apply Fed. R. Bankr. P. 7023 to the claims allowance and disallowance procedure; implement the schedule proposed in the Consumer Claimants' Committee's Motion to Apply Fed. R. Bankr. P. 7023 to the Claims Allowance and Disallowance Process; and Implement a Schedule for Certifying Class Claims.

The Tenth Circuit has taken no definitive position on the issue of class proof of claims. The overwhelming position among federal courts, including most circuits, is that class proofs of

claim may be submitted in Bankruptcy Court. Moreover, in this case, compelling reasons exist to allow Ms. Tullie to file such a claim.

In its Scheduling Order Resulting from Preliminary Hearing on Emergency Motion to Enforce Settlement Agreement and Request for Hearing [Doc. 52], the Court expressed “uncertainty about whether it has the authority to allow class proofs of claim, citing *In re Standard Metals Corp.*, 817 F.2d 625 (10th Cir.), on reh’g sub nom. *Sheftelman v. Standard Metals Corp.*, 839 F.2d 1383 (10th Cir. 1987). Although the Court is correct that *In re Standard Metals Corp.* questioned there could be a class proof of claim, the 10th Circuit’s rehearing in *Sheftelman* explicitly clarified that position and stated that “**it is not necessary to consider the class action claims issue**” to decide the case. 839 F.2d at 1387. As such, the Tenth Circuit panel reconsidered and set aside the issue of class proofs of claim in *In re Standard Metals Corp.* It removed that issue from that court’s analysis of the case; the earlier opinion does not even constitute *dictum*. Recognizing this point, lower Courts in the 10th Circuit have permitted class proofs of claim. *In re Amdura Corp.*, 170 B.R. 445 (D. Colo. 1994); *In re Adam Aircraft Indus., Inc.*, No. 08-11751MER, 2009 WL 2100929 (Bankr. D. Colo. Mar. 20, 2009).

The modern view, held by the overwhelming majority of courts, permits the filing of class proofs of claim. *In re Dynegy, Inc.*, 770 F.3d 1064 (2nd Cir. 2014); *Gentry v. Siegel*, 668 F.3d 83 (4th Cir. 2012); *In re Birting Fisheries, Inc.*, 92 F.3d 939 (9th Cir. 1996); *Reid v. White Motor Corp.*, 886 F.2d 1462 (6th Cir. 1989); *In re Charter Co.*, 876 F.2d 866 (11th Cir. 1989); *Matter of Am. Reserve Corp.*, 840 F.2d 487 (7th Cir. 1988); *In re Trebol Motors Distrib. Corp.*, 220 B.R. 500 (B.A.P. 1st Cir. 1998) (“The First Circuit has not addressed the issue of class claims in bankruptcy, but all of the circuit courts which have spoken have held that they are permitted.”);

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In re MF Global Inc., 512 B.R. 757 (Bankr. S.D.N.Y. 2014) (“most courts agree that class proofs of claim are allowed in bankruptcy proceedings”); *In re Craft*, 321 B.R. 189 (Bankr. N.D. Tex. 2005) (“courts declining to permit class proofs of claim are recognized as being in the minority”); *In re First Interregional Equity Corp.*, 227 B.R. 358 (Bankr. D.N.J. 1998) (“the vast majority of courts who have recently considered the issue have concluded that class proofs of claim are now regularly permitted in a bankruptcy proceeding”).

The reasoning behind these decisions is sound and sets to rest the concerns raised by the 10th Circuit in *In re Standard Metals Corp.* In that case, the 10th Circuit averred that under the Act and the Rules, “each individual claimant must file a proof of claim or expressly authorize an agent to act on his or her behalf.” 817 F.2d at 631. The Court did not believe that a class representative could be considered an “authorized agent.” *Id.* Subsequent decisions put this concern to rest. *In re Charter Co.*, 876 F.2d at 873 (“the filing claimant’s status as a putative representative is at least minimally sufficient to authorize his agency for class filing purposes”); *Gentry v. Siegel*, 668 F.3d at 90 (“Pending approval, therefore, the Named Claimants were putative agents of the similarly situated unnamed claimants.”); *Matter of Am. Reserve Corp.*, 840 F.2d at 493 (“The representative in a class action is an agent for the missing.”).

For these reasons, the Court *can* allow class proofs of claim. Equally importantly, it *should* allow class proofs of claim. “[T]he bankruptcy statute has the goal of facilitating creditor compensation.” *In re Charter Co.*, 876 F.2d at 873. “Persons holding small claims, who absent class procedures might not prosecute them, are no less creditors under the Code than someone with a large, easily filed claim.” *Id.* Cash Cow’s predatory lending practices targeted unsophisticated borrowers, many of them unsophisticated members of the Navajo Nation living

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in poverty in a remote corner of the southwest. Cash Cow knows that these people are highly unlikely to advocate for themselves in this Court. The Bankruptcy Court should not permit Cash Cow to cast off these victimized borrowers when the class action could be used simply and efficiently to compensate them.

For these reasons, Ms. Tullie joins with the Consumer Claimants' Committee in requesting that the Court allow class proofs of claim in this matter, apply Fed. R. Bankr. P. 7023 to the claims allowance and disallowance procedure, implement the schedule proposed in the Consumer Claimants' Committee's Motion to Apply Fed. R. Bankr. P. 7023 to the Claims Allowance and Disallowance Process, and Implement a Schedule for Certifying Class Claims.

Respectfully Submitted,

/s/ Richard N. Feferman
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UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

In re:

QUICK CASH, A New Mexico Corporation,
Debtors.

Case No. 15-11800-j11

**SECURED CREDITOR SUPERIOR FABRICATION, INC.'S LIMITED OBJECTION
TO CONSUMER CLAIMANTS' COMMITTEE'S MOTION TO APPLY
FED.R.BANKR.P 7023 TO THE CLAIMS ALLOWANCE AND DISALLOWANCE
PROCESS AND TO IMPLEMENT A SCHEDULE FOR CERTIFYING CLASS CLAIMS**

Secured Creditor Superior Fabrication, Inc., ("SFI") by and through its attorneys Modrall, Sperling, Roehl, Harris & Sisk, P.A. (Paul M. Fish), hereby submits its limited objection to Consumer Claimants' Committee's Motion To Apply Fed.R.Bankr.P 7023 To The Claims Allowance And Disallowance Process And To Implement A Schedule For Certifying Class Claims ("CCC's Motion") [Doc 55] filed in Case No. 15-11800-j11 and as grounds therefore would show the Court that CCC's Motion

1. SFI is a secured creditor with valid perfected security interests in essentially all assets of the Debtor.
2. The major asset of the Debtor is the portfolio of loans outstanding to consumers.
3. Many if not most of the proposed members of the purported class which is the subject of the CCC's Motion owe money to the Debtor, which debts are pledged to SFI.
4. As a general proposition, the filing of a proof of claim is a consent to the jurisdiction of the bankruptcy court over the purported creditor. *In re Apex Corp*, 190 F.3d 624, fn. 7 (4th Cir. 1999). Any order granting authority to file a class proof of claim should specifically so state, and notice to the purported class members should alert all those owing money to the Debtor that the bankruptcy process may affect their legal rights and claims as well

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as defenses to actions to recover a debt owed by them, unless they opt out of the class by a date certain.

5. SFI does not consent to the use of its cash collateral for any notices to purported class members. Those purporting to file a proof of claim on behalf of a class should bear the cost of their proof of claim as any other creditor would.

6. The movants should be required to bear the cost of notice to the class it seeks to represent, not the Debtor. SFI does not consent to the use of its cash collateral to give such notice.

WHEREFORE, Secured Creditor Superior Fabrication, Inc., prays that CCC's Motion be denied.

MODRALL SPERLING ROEHL HARRIS & SISK, P.A.

By: /s/ Paul M. Fish
Paul M. Fish
Bank of America Centre
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(505) 848-1800
Attorneys for Superior Fabrication, Inc.

In accordance with NM LBR 9036-1 and Fed. R. Civ. P. 5(b)(2)(D), this certifies that service of the foregoing document was made this 12th day of October, 2015, via the notice transmission facilities of the case management and electronic filing system of the Bankruptcy Court.

By: /s/ Paul M. Fish
Paul M. Fish

W2568556.DOC

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO**

In re:

**QUICK CASH, A New Mexico Corporation,
Debtors.**

Case No. 15-11800-j11

**SECURED CREDITOR SUPERIOR FABRICATION, INC.'S LIMITED OBJECTION
TO PLAINTIFF CAROLINE TULLIE'S MOTION TO ALLOW CLASS PROOFS OF
CLAIM, TO APPLY FED.R.BANKR.P.7023 TO THE CLAIMS ALLOWANCE AND
DISALLOWANCE PROCEDURE AND TO IMPLEMENT A SCHEDULE FOR
CERTIFYING CLASS**

Secured Creditor Superior Fabrication, Inc., ("SFI") by and through its attorneys Modrall, Sperling, Roehl, Harris & Sisk, P.A. (Paul M. Fish), hereby submits its limited objection to Plaintiff Caroline Tullie's Motion To Allow Class Proofs of Claim, To Apply Fed.R.Bankr.P 7023 To The Claims Allowance And Disallowance Process And To Implement A Schedule For Certifying Class Claims ("Tullie's Motion") [Doc 57] filed in Case No. 15-11800-j11 and as grounds therefore would show the Court that Tullie's Motion

1. Tullie's Motion seeks essentially the same relief as sought by the Consumer Claimants' Committee's Motion to Apply Fed.R.Bankr.P. 7023 to the Claims Allowance and Disallowance Process and to Implement a Schedule for Certifying Class Claims [Doc 55] (the "Committee's Motion").

2. On October 12, 2015, SFI filed its limited objection (the "Limited Objection") to the Committee's Motion which was filed as [Doc 59].

3. Tullie's Motion has the same defects as the Committee's Motion.

4. SFI here realleges all responses and objections contained in its Limited Objection as if set forth herein.

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WHEREFORE, Secured Creditor Superior Fabrication, Inc., prays that Tullie's Motion be denied.

MODRALL SPERLING ROEHL HARRIS & SISK, P.A.

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In accordance with NM LBR 9036-1 and Fed. R. Civ. P. 5(b)(2)(D), this certifies that service of the foregoing document was made this 12th day of October, 2015, via the notice transmission facilities of the case management and electronic filing system of the Bankruptcy Court.

By: /s/ Paul M. Fish
Paul M. Fish

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**UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO**

In Re:

QUICK CASH, INC.
a New Mexico corporation,

Debtor.

No. 15-11800- j11

**DEBTOR'S RESPONSE TO CONSUMER CLAIMANTS' COMMITTEE'S MOTION
TO APPLY FED. R. BANK. P. 7023 TO THE CLAIMS ALLOWANCE AND
DISALLOWANCE PROCESS AND TO IMPLEMENT A SCHEDULE
FOR CERTIFYING CLASS CLAIMS**

The debtor, through Moore, Berkson, Bassan & behles, P.C., its counsel, makes the following response to the *Consumer Claimants' Committee's Motion to Apply Fed. R. Bank. P. 7023 to the Claims Allowance and Disallowance Process and to Implement a Schedule for Certifying Class Claims* (Doc. #55, hereinafter the "Motion").

1. Debtor acknowledges the agreement reached with the Consumer Claimants Committee (the "Committee") as set forth in paragraphs 1 through 6 of the Motion. The Motion and this Response address only the issue of whether the Court should allow the filing of class proofs of claim, which would necessitate the application of FRBP 7023 to the claims allowance and disallowance process, which is a contested matter. The parties have agreed to defer the issue of special noticing procedures and forms of notice for possible additional consumer claims until after some discovery has been conducted.

2. To date only a single type of Consumer claim has been identified. That claim is the subject of adversary case number 15-01063J, which is a class action proceeding removed from the Federal District Court for the District of New Mexico. At the time of removal no class had been certified, and the Bankruptcy Court has not yet entered an order certifying the proposed

class in that proceeding. The named Plaintiff in that adversary proceeding is a member of the Committee.

3. All known members of the proposed class have already been given notice of a claims bar deadline, and the fact that their claims were disputed, and the fact that a claim would have to be filed in order to share in any distributions under a Plan. (Doc. #17 & 22). Several (but a very minor number, compared to the total prospective membership of the class) claims have already been filed by members of the class.

4. This court has ruled (Doc. #46) that the previously established claim filing deadline will be extended until December 23, 2015, so that additional claims may be filed by members of the proposed class. The Court has further ordered that new and more informative notice procedures be devised, either by agreement between the Debtor and the Committee, or by Court Order, to insure that the Notice of the extended claim deadline, and the necessity for filing claims, will be readily understood by prospective class members, and afford them a reasonable opportunity to file a claim.

5. The controlling authority in the 10th Circuit, which Debtor believes is binding upon this Court, is *Sheftelman v. Standard Metals Corp.*, 817 F.2d 625 (10th Cir. 1987). It is true, as the Committee argues, that a Federal District Court in Colorado has ruled that the holding in *Sheftelman* (that class proofs of claim are not allowed in bankruptcy) is only dicta, based on the fact that the Tenth Circuit Court of Appeals, upon rehearing *Sheftelman*, upheld the decision on other grounds, and stated that “in view of the disposition of this appeal it is not necessary to consider the class action claims issue.” (*Sheftelman v. Standard Metals Corp.*, 839 F.2d 1383, 1387 (10th Cir. 1987 cert. dismissed 477 U.S. 811, 109 Sup. Ct. 201 (1988)). However, no New Mexico District Court has ever ruled upon the issue, and it remains unclear whether the

determination by a Colorado District Court about what is, and is not, *dicta*, releases a New Mexico Court from the clear holding of *Sheftelman*.

6. It is also true that several other Circuits have determined that Class claims may be allowed in bankruptcy, based upon a statutory analysis of FRBP 9014 and 7023. Most of the decisions allowing class proofs of claim focus upon the equitable nature of the bankruptcy court. A cogent statement of this line of reasoning can be found in *Gentry v. Siegel*, 668 F.3d 83 (6th Cir., 1989) at 88-89:

“Because the Bankruptcy Rules accept the notion that class action rules may, in appropriate circumstances, be employed in a bankruptcy case, we conclude that they therefore necessarily embrace the notion that the proposal to represent a class is tentative pending approval. And with that notion comes the equally necessary propositions that if the proposal is approved, the approval relates back to when it was made, and if it is rejected, the putative class members must be given time after the court’s rejection to file individual proofs of claim. Stated otherwise, by recognizing class actions, the Bankruptcy Rules also recognize that putative class representatives can keep the class action process alive until the court decides the issue. Thus, we conclude that Rule 3001 should be construed to allow class proofs of claim, at least on a tentative basis, until the court rejects the class-action process.”

7. However, two common threads run through the various cases that have allowed the filing of class proofs of claim in bankruptcy cases. One common theme is that in almost every case, members of the putative class had NOT been given notice of the pendency of the bankruptcy or the need for filing a proof of claim. The second factual predicate found in most of the cases allowing the filing of class proofs of claim is that the classes have typically been certified prior to the bankruptcy filing. Neither of those circumstances exist in this case. No class has yet been certified, and all putative class members have already received notice of the necessity and opportunity for filing a claim, and will receive a further notice and opportunity to file.

8. What we have, then, is a tension between the circuit decisions allowing class

proofs of claims, at least in cases where there has been a class certified and no notice provided to members of the class, and the 10th Circuit decision in *Sheftelman* prohibiting such claims. How do we resolve this tension?

9. One possible procedure might be as suggested in *Teta v. Chow*, 712 F.3d 886 (5th Cir., 2013). Allowing a class claim in bankruptcy is actually a two-step process, as the title of the Committee’s Motion suggests: First the court has to determine whether to apply the class action rules in a contested matter. The adversary rules provide that FRCP 23 is applicable in adversary proceedings, but it is not automatically applicable in contested matters. The court must decide, under FRBP 9014, whether or not to make rule applicable in the contested matter. As stated in *Teta v. Chow*: (892-893)

Pursuant to Rule 7023—which falls within Part VII of the Federal Bankruptcy Rules—Rule 23 of the Federal Rules of Civil Procedure “applies in adversary proceedings.”² Fed. R. Bankr.P. 7023. Thus, “[i]n an appropriate situation, class adversary proceedings may be commenced in a bankruptcy case provided that the requirements of the various subdivisions of Rule 23 are satisfied.” 10 Collier on Bankruptcy ¶ 7023.01; see also In re Wilborn, 609 F.3d at 754 (“[C]lass action proceedings are expressly allowed in the Federal Bankruptcy Rules, which provide that the requirements for class actions under Federal Rule of Civil Procedure 23 apply in adversary proceedings.”).

Rule 23 does not necessarily apply, however, to a class proof of claim. First, our circuit has not addressed whether a class proof of claim even is permissible. Second, Rule 9014, which governs contested matters, provides that only certain procedural rules automatically apply when an objection is lodged to a proof of claim. See Fed. R. Bankr.P. 9014. Rule 7023 is not designated as one of these automatically applicable rules, but Rule 9014 does state that “[t]he court may at any stage in a particular matter direct that one or more of the other rules in Part VII shall apply.” Fed. R. Bankr.P. 9014 (emphasis added).

Given this discretion, Rule 23’s operation in contested matters involves a two-step process. 10 Collier on Bankruptcy ¶ 7023.01. “First, the court must exercise its discretion [under Rule 9014] as to whether to apply Rule 23 to the contested proceeding.” Id. Second, if the court decides to apply Rule 23, it then must determine whether the Rule’s requirements for class certification have been satisfied. Id. In considering whether to apply Rule 23 in the first instance: the court will consider a variety of factors relating to the bankruptcy case. These include: (1) whether the class was certified pre-petition, (2) whether the members of the putative class received notice of the bar date, and (3) whether class certification will adversely affect the

administration of the case, especially if the proposed litigation would cause undue delay. Id. The court also may consider the benefits and costs of class litigation to the estate. In re Computer Learning Ctrs., Inc., 344 B.R. 79, 86 (Bankr.E.D.Va.2006).

10. In the present case no class has been certified pre-petition. All members of the putative class have already received notice, and will receive further notice pursuant to the Court's Order extending the claim deadline. Class certification will almost certainly delay the administration of the estate, since the alleged wrongdoing is a technical statutory violation and no real economic damages are pled, but only statutory damages. There will surely be a claim objection filed by the debtor if a class claim is filed, and no reasonable Plan of Reorganization could be proposed with seven thousand indeterminate claimants. Furthermore, the Court has already extended the deadline for filing individual claims and required the parties to confer and devise more informative notice procedures. What would be the purpose of requiring all the additional time and expense attendant upon such additional notice procedures if individual claims would be supplanted by a Class proof of claim?

11. The Court should also consider the impact that allowing a class claim would have upon the members of the purported class. By allowing a class claim they would be foreclosed from filing an individual claim or from asserting individual damages different than those asserted in a class claim. Would those members who have already filed claims have their claims ignored in favor of the class claim? Having already been notified of their right to file a claim, taking away that right (or the right NOT to file a claim) by allowing a class claim, might raise serious due process complications.

12. Two other important policy considerations militate in favor of not allowing class claims in this proceeding. The first has to do with one of the general rationales for allowing class action lawsuits in the first place is to avoid the possibility of inconsistent outcomes occurring if

similar lawsuits were filed by similarly situated claimants in multiple courts and jurisdictions. Uniformity of outcome given similar fact situations is a laudable goal. But the debtor here is in bankruptcy Court, and one of the rationales for the Bankruptcy Stay is the same as in class action suits – to avoid dissimilar outcomes by requiring all claims to be asserted in the same proceeding. Because Chapter 11 already provides protection against the risk of dissimilar results, the incentive for authorizing class claims is diminished. All claims asserted by purported class members, who may have similar factual situations, will be heard by this court, and this court can guard against inconsistent results because it will hear all similarly situated claims.

The second policy argument against class claims has to do with jurisdiction. Probably the great majority of purported class members are Native Americans residing on the Navajo reservation. As such, they are beneficiaries of many protective mechanisms established in Navajo Tribal Courts to prevent members of the Navajo Nation from being taken advantage of. In bankruptcy, filing a proof of claim submits the claimant to the jurisdiction of the Bankruptcy Court. Oftentimes claimants, particularly secured claimants willing to rely on their security for re[payment, do not file claims in bankruptcy, so as not to subject themselves to jurisdiction in the Bankruptcy Court, often in another state. If a class proof of claim were filed, all members of the class would have submitted themselves to the jurisdiction of the New Mexico Bankruptcy Court, and might waive safeguards otherwise available to them. This is particularly true since most members of the purported class are debtors to the Debtor in Bankruptcy. Pre-bankruptcy, the debtor would usually be required to pursue collection activities against class members in the Navajo Tribal courts. If a Class proof of claim is filed and the members become subjected to this Court's jurisdiction, the special protections available if the claimants could only be sued in Tribal Court might be unavailable. This Court should not lightly rule that all members of the

purported class will necessarily be benefited by subjecting themselves to this Court's jurisdiction. Given notice of the right to file a claim. Class members should be allowed to decide for themselves whether their interests are better served by filing a claim in bankruptcy and becoming subject to Bankruptcy Court jurisdiction.

13. This court does not need to address the thorny issues that arise if it allowed a class claim to be filed. The simple answer to the tension between the *Sheftelman* holding and the opposite Circuit court decisions is to ignore the issue. Before a class claim could be allowed this court must determine that rule 23 should be applied in the context of a contested claims allowance matter. Applying the various factors set forth in *Teta v. Chow*, it becomes apparent that rule 23 should not be made applicable to the claims process in this Chapter 11 proceeding. The court has great discretion in deciding whether or not to apply Rule 23. The decisions the Court has already made concerning additional notice and noticing procedures argue against applying class action rules in the claims process. It is unduly burdensome upon the debtor and the estate to require the debtor to go to extreme measures to notify all potential class members, *and* to allow the filing of a class proof of claim, which presumptively eliminates the need for the extended bar date and additional notices which the Court has determined should be given.

14. In essence, there are two potential paths the claims process can take in this bankruptcy. Down one path, the Court would disobey the strictures of the *Sheftelman* decision, ignore the various factors used to determine whether Rule 23 should be made applicable under rule 9014, make redundant the procedures already set in place for notices and claim deadlines, and allow a class claim to be filed. Down the other path the Court would simply continue the individual claims filing process that was commenced back in July when the claim deadline was notice to over 7200 claimants, and will be re-noticed again. Having already chosen one of two

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alternatives, the Court should not reverse course, delay this bankruptcy proceeding, incur yet more expense and frustrate the expenditures that have already been made.

The debtor respectfully request the Court deny the Motion to make FRCP 23 applicable to the claims allowance process in this case, thereby disallowing the filing of class claims.

In its Motion the Committee also requested the Court to establish procedures and deadlines for certifying other potential classes of claimants. Since no such classes have yet been identified (if indeed they exist) and since it is therefore impossible to consider whether the numerosity and superiority requirements for allowing class actions exist, Debtor cannot adequately respond to this request. However, the rationale for disallowing class proofs of claims remain valid, regardless of how many potential “classes” may exist. For that reason the debtor opposes the allowance of any “class” proofs of claim, whether filed on behalf of the single identified (but uncertified) proposed class, or on behalf of other, as yet unidentified and unasserted “classes” of consumer claimants.

Respectfully submitted:

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I certify that a true copy of the foregoing pleading was served upon all counsel of record via the Court’s CNM/ECF system on the date this pleading was filed with the Court.

/S/ Daniel J. Behles

2018 WINTER LEADERSHIP CONFERENCE

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO**

In re:

QUICK CASH INC., a New Mexico corporation
Debtor.

Case No. **15-11800-j11**
Chapter 11

CAROLINE TULLIE,
on her own behalf
as next friend of NELSON TULLIE,
and on behalf of all others similarly situated,

Plaintiff,

Adversary No. **15-01063J**

v.

QUICK CASH INC.,
d/b/a **CASH COW LOAN CO.**,

Defendant.

**DEBTOR'S RESPONSE TO PLAINTIFF CAROLINE TULLIE'S MOTION
TO ALLOW CLASS PROOFS OF CLAIM,
TO APPLY FED. R. BANK. PROC. 7023 TO THE CLAIMS ALLOWANCE AND
DISALLOWANCE PROCEDURE AND
TO IMPLEMENT A PROCEDURE FOR CERTIFYING CLASS CLAIMS**

The debtor, through Moore, Berkson, Bassan & Behles, P.C., its counsel, makes the following response to *Plaintiff Caroline Tullie's Motion to Allow Class Proofs of Claim, to Apply Fed. R. Bank. P. 7023 to the Claims Allowance and Disallowance Process and to Implement a Procedure for Certifying Class Claims* (Doc. #57, hereinafter the "Motion").

1. Debtor believes Tullie has no standing to assert such a request in this bankruptcy case. Tullie is an individual claimant in an adversary proceeding, who seeks but has not yet been granted status as the representative for a proposed class. Tullie has not entered an appearance in the main Bankruptcy case, nor has her counsel. Tullie has filed this Motion with the adversary

case caption, but has filed it in the main bankruptcy case.

2. Without waiving its Objection to Tullie's standing, Debtor states that it has filed a response (Doc. #61) to a similar Motion filed herein by the Consumer Claimant's Committee, and it incorporates herein and adopts by reference all the arguments, points and authorities raised in that response.

3. Without waiving its Objection to Tullie's standing, Debtor responds to Tullie's Motion as follows.

4. Tullie asserts that the holding in

5. *Sheftelman v. Standard Metals Corp.*, 817 F.2d 625 (10th Cir.), that class claims are not generally allowed in bankruptcy, is not binding on this court. Whether the holding in *Sheftelman* is binding, or merely *dicta*, in the absence of any 10th Circuit decision specifically overruling *Sheftelman*, the better course of judicial discretion is to give precedential authority to *Sheftelman*.

6. Even if this Court concludes that it is not bound by *Sheftelman*, the issue becomes, as admitted by Tullie, not whether the court *can* allow class proofs of claim, but whether it *should* allow class proofs of claim in this particular case. The policy reasons for not doing so, and the discretionary reasons for not applying FRCP 23 to the claims allowance process in this case, are set forth in Debtor's Response to the Committee's parallel motion, and will not be repeated here.

7. However, the arguments made by Tullie are based in large part upon an unproven contested assertion made by Tullie, as if it were a matter of proof. Tullie asserts that "Cash Cow's predatory lending practices targeted unsophisticated borrowers" and that "The Bankruptcy Court "should not permit Cash Cow to cast off these victimized borrowers". These

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are bald-faced assertions without any basis in fact. The original complaint filed by Tullie (Docket #1 in the removed case, 14-cv-00491-SMV-scy, attached as an exhibit to the removal) asserted a request for statutory damages under the federal TILA for failure to include a fee in the calculation of the annual percentage rate, and for failure to state the day of the month on which each monthly payment became due. There is no assertion that the application fee was hidden or undisclosed. A second claim seeks actual damages, trebled, for alleged violations of the New Mexico UPA. No additional factual assertions are plead, other than that the disclosures are “deceptive” and “misleading”. Even if each and every one of Tullie’s assertions were proven true, they would not amount to predatory practices. The amounts Tullie was required to pay are fully and completely disclosed – the primary issue is whether the \$25 fee, fully disclosed, should have been calculated as part of the APR, or not. Tullie was not victimized, and was not the target of predatory lending. Indeed, the agreements in dispute are refinance agreements of loans previously made, and nothing in the complaint alleges that the original loans were “predatory”, deceptive or misleading in any way. To argue that not allowing class claims would somehow permit the debtor to “cast off” victimized borrowers is a mischaracterization of the facts alleged in the complaint.

WHEREFORE. For the reasons expressed herein, and in debtor’s response to the Committee’s Motion, Docket #61, Debtor requests that the Motion be denied.

Respectfully Submitted

Moore, Berkson Bassan & Behles, P.C.

By: filed electronically

Daniel J. Behles

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I certify that a true copy of the foregoing pleading served upon all counsel of record via the Court's CM/ECF noticing system on the day this pleading was filed with the Court. I further certify that a true copy was served via first class mail, on October 14, 2015, upon:

Richard N. Feferman
300 Central Ave. SW, Suite 2000 West
Albuquerque, NM 87102

/S/ Daniel J. Behles

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO**

In re:

**QUICK CASH, A New Mexico Corporation,
Debtors.**

Case No. 15-11800-j11

**SECURED CREDITOR SUPERIOR FABRICATION, INC.'S SUPPLEMENTAL
OBJECTION TO CONSUMER CLAIMANTS' COMMITTEE'S MOTION TO APPLY
FED.R.BANKR.P 7023 TO THE CLAIMS ALLOWANCE AND DISALLOWANCE
PROCESS AND TO IMPLEMENT A SCHEDULE FOR
CERTIFYING CLASS CLAIMS**

Secured Creditor Superior Fabrication, Inc., ("SFI") by and through its attorneys Modrall, Sperling, Roehl, Harris & Sisk, P.A. (Paul M. Fish), hereby submits its additional and supplemental limited objection to Consumer Claimants' Committee's Motion To Apply Fed.R.Bankr.P 7023 To The Claims Allowance And Disallowance Process And To Implement A Schedule For Certifying Class Claims ("CCC's Motion") [Doc 55] filed in Case No. 15-11800-j11 and as grounds therefore would show the Court that CCC's Motion

1. SFI is a secured creditor with valid perfected security interests in essentially all assets of the Debtor.
2. The major asset of the Debtor is the portfolio of loans outstanding to consumers.
3. Many if not most of the proposed members of the purported class which is the subject of the CCC's Motion owe money to the Debtor, which debts are pledged to SFI.
4. SFI hereby incorporates its Limited Objection filed as Docket No. 59. This Supplemental Limited Objection is in addition to the Objection previously filed.
5. The fling of the class proof of claim creates significant binding legal obligations on those for whom the proof of claim is filed, including subjecting the claimant to the jurisdiction of this Court.

6. The Court should not authorize the Consumer Claimants' Committee (the "CCC") or any other creditor to file a class proof of claim. The Bankruptcy Code, 11 U.S.C. § 501(b), provides that if a creditor does not file a proof of claim, an entity that is liable to such creditor with the debtor or that has secured such creditor may file proof of such claim. The Bankruptcy Code, 11 U.S.C. § 501(c), provides that if a creditor does not file a proof of claim, the debtor or the trustee may file proof of such claim. The Bankruptcy Code does not provide for filing proofs of claim by a committee appointed pursuant to 11 U.S.C. § 1102. The Bankruptcy Code does not provide for creditors similarly situated to another creditor to file a class proof of claim (although SFI recognizes the issues raised by various courts in addressing the issue of a class proof of claim).

7. If the Court decides to allow a class proof claim to be filed, such filing should not be allowed to be made by the CCC because committees are not permitted to bind their constituents. 7-1103 *Collier on Bankruptcy 16 Ed.* ¶ 1103.05(i) Committees May Not Bind Their Constituents; *In re Donlevy's, Inc.*, 111 B.R. 1, 2 (Bkrcty Mass 1990) ("the committee does not have statutory authority to bind creditors to the acceptance of a plan proposal...") The CCC does not have the statutory authority to create significant binding obligations on its constituents.

8. The bankruptcy estate pays the legal fees of the CCC. The major asset of the bankruptcy estate consists of the obligations of the putative class members. Of those obligations, according to the Monthly Operating Report filed by the Debtor for August of 2015, only 39% of the amount owed is in the 0-30 aging category. Upon information and belief, a majority of the amount owed in the 0-30 aging category is not "current" in the sense that all payments required by the loan documents to that date have been paid. Rather, most are loans for which some

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In accordance with NM LBR 9036-1 and Fed. R. Civ. P. 5(b)(2)(D), this certifies that service of the foregoing document was made this 22nd day of October, 2015, via the notice transmission facilities of the case management and electronic filing system of the Bankruptcy Court.

By: /s/ Paul M. Fish
Paul M. Fish

W2574284.DOC

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

In re: QUICK CASH, INC.,
a New Mexico corporation,

No. 11-15-11800 JA

Debtor.

**MEMORANDUM OPINION AND ORDER ON MOTIONS TO APPLY FED. R. BANKR.
P. 7023 TO THE CLAIMS ALLOWANCE AND DISALLOWANCE PROCESS**

THIS MATTER is before the Court on the following motions: 1) Plaintiff Caroline Tullie's Motion to Allow Class Proofs of Claim, to Apply Fed. R. Bankr.P. 7023 to the Claims Allowance and Disallowance Procedure and to Implement a Schedule for Certifying Class Claims ("Tullie Motion" – *See* Docket No. 57); and 2) Consumer Claimants' Committee's Motion to Apply Fed. R. Bankr.P. 7023 to the Claims Allowance and Disallowance Process and to Implement a Schedule for Certifying Class Claims ("CCC Motion" – Docket No. 55) (together, the "Motions"). The Debtor, Quick Cash, Inc. ("Quick Cash"), and its secured lender, Superior Fabrication, Inc. ("SFI"), objected to the Motions. *See* Docket Nos. 59, 60, 61, 62, and 65. The Court heard oral argument on the Motions on October 27, 2015, and took the Motions under advisement.¹

Having considered the parties' arguments in light of the relevant case law, applicable Bankruptcy Code sections, and Bankruptcy Rules, and being otherwise sufficiently informed, the Court concludes that although class proofs of claim are permissible, additional evidence must be presented before the Court can determine, in its discretion, whether to apply Bankruptcy Rule

¹ The Court allowed the Unsecured Creditors' Committee to argue at the final hearing despite not having filed a response or objection to the Motions. Upon the request of counsel for the Consumer Claimants' Committee, the Court permitted the Consumer Claimants' Committee to file a supplemental brief in response to the Unsecured Creditor Committee's arguments made in open court. The Consumer Claimants' Committee declined to file a supplemental brief.

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7023 to allow Ms. Tullie to file a class proof of claim in this bankruptcy case on behalf of similarly situated consumer creditors.

BACKGROUND AND PROCEDURAL HISTORY

Quick Cash filed a voluntary petition under Chapter 11 of the Bankruptcy Code on July 6, 2015. On July 29, 2015 the United States Trustee appointed an official Committee of Unsecured Creditors (the “UCC”). *See* Docket No. 24. The United States Trustee appointed a Consumer Creditors Committee (“CCC”) on August 11, 2015. *See* Docket No. 38. Ms. Tullie is a member of the CCC.

On May 14, 2014, a little over a year before Quick Cash filed its bankruptcy case, Caroline Tullie, on her own behalf as next friend of Nelson Tullie, and on behalf of all others similarly situated, filed a Class Action Complaint for Damages against Quick Cash in the United States District Court for the District of New Mexico as Case No. 1:14-cv-00491-SMV-SCY (the “Class Action Suit”). In the Class Action Suit, Ms. Tullie asserted claims against Quick Cash for alleged violations of the federal Truth in Lending Act (“TILA”) and the New Mexico Unfair Trade Practices Act (“UPA”). Such claims are based on Ms. Tullie’s assertion that Quick Cash charged a \$25.00 “application fee” to persons who borrowed money from Quick Cash, but failed to include or disclose that fee as part of the finance charge reported in its loan documents and/or failed to disclose to borrowers sufficient information about loan payment schedules. Ms. Tullie alleged in the Class Action Suit that there are more than 4,700 similarly situated persons in the putative class.

Ms. Tullie removed the Class Action Suit to this Court on August 5, 2015, thereby initiating Adversary Proceeding No. 15-1063 J. Prior to removal, the class certification was ripe for a decision. The parties had briefed the issue of class certification and submitted evidence, but

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no decision on class certification had been made. At a status conference in the Adversary Proceeding held on August 10, 2015 counsel for Ms. Tullie and counsel for Quick Cash represented to the Court that the parties had reached a tentative settlement of the Class Action Suit contingent upon certification of the class. When Quick Cash failed to approve a stipulated class certification order and indicated through counsel that it did not intend to go through with the tentative settlement, Ms. Tullie filed a motion in the Adversary Proceeding seeking to enforce the settlement. *See* Emergency Motion to Enforce Settlement Agreement and Request for Hearing (“Motion to Enforce Settlement”), Adversary Proceeding No. 15-1063 J – Docket No. 6. The Court denied the Motion to Enforce Settlement without prejudice based on procedural defects. *See* Order Denying Emergency Motion to Enforce Settlement Agreement, Adversary Proceeding No. 15-1063 J – Docket No. 15.

In the bankruptcy case, on July 9, 2015, three days after filing its voluntary Chapter 11 petition, Quick Cash filed an *ex parte* motion to set the last day for filing proofs of claim. *See* Debtor’s *Ex Parte* Motion to Establish Bar Date for Filing Proofs of Claims [sic.] (“Claims Bar Date Motion”) – Docket No. 14. The Claims Bar Date Motion did not disclose the Class Action Suit or seek guidance from the Court whether any special procedures should be implemented for giving notice of the claims bar date to the putative class members. The Court entered an Order Fixing Time for Filing Proofs of Claim and Interests, in a form typically entered in Chapter 11 cases in this district where fixing a claims bar date is a routine matter. The order fixed a general claims bar date of sixty days after the date of service of notice of general claims bar date. *See* Docket No. 17. On July 27, 2015, Quick Cash sent a notice with a stated general claims bar date of September 23, 2015 for filing proofs of claim. *See* Notice of Deadline for Filing Proofs of Claim and Interests Notice of Disputed, Contingent, or Unliquidated Claim (“Claims Bar Date

Notice”) – Docket No. 22. Quick Cash sent the Claims Bar Date Notice to all creditors and parties in interest listed on the mailing matrix for Quick Cash’s bankruptcy case (over 7,200 recipients), which included members of the putative class.

As of September 22, 2015, only thirty-six proofs of claim were filed in Quick Cash’s bankruptcy case. *See* Claims Register. Of those, not more than seven appear to have been filed by putative class members. *See*, Claim Nos. 17-1, 23-1, 24-1, 33,-1, 34-1, 35-1 and 36-1. A few proofs of claim assert claims based on Quick Cash’s alleged wrongful repossession of the claimant’s vehicle. *See, e.g.*, Claim No. 31-1.

On September 22, 2015, the CCC filed a motion requesting the Court to extend the claims bar date to consumer claimants, consisting of the more than six thousand persons with potential claims against Quick Cash for alleged violation of TILA that Quick Cash identified in its Schedule F (who received the Claims Bar Date Notice), plus potential thousands of other unknown consumer claimants who did not receive notice of the September 23, 2015 general claims bar date. *See* Consumer Claimants’ Committee’s Motion (I) to Stay, or in the Alternative, Extend, the Claims Bar Date as to Consumer Claimants and (II) for an Order Establishing Claim Procedures for Consumer Claims (“Motion to Extend Claims Bar Date”) – Docket No. 44. Following a hearing on the Motion to Extend Claims Bar Date, the Court entered an Order Extending Claims Bar Date which extended the deadline for filing proofs of claim to December 23, 2015. *See* Docket No. 45. The Court found that the Claims Bar Date Notice provided insufficient notice to potential consumer claimants. *Id.* A hearing on the establishment of special procedures or special forms of notice of the deadline for filing proofs of claim is scheduled for November 12, 2015.

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Quick Cash operates its business in Gallup, New Mexico, including retail sales of furniture and merchandise, an auto tire and repair facility, and a consumer loan business. *See* Docket No. 3. One of Quick Cash's principal assets is its portfolio of consumer loan accounts receivable. *Id.* Quick Cash's income derives in part from payments under those consumer loans. SFI asserts a security interest in essentially all of Quick Cash's assets. *See* Claim No. 26-1. At the hearing on the Motions, SFI asserted that Quick Cash's bankruptcy estate is administratively insolvent. There is no evidence currently before the Court with respect to Quick Cash's prospects for reorganization, including whether any funds will likely be available to pay any allowed nonpriority unsecured claims, and, if so, how much.

DISCUSSION

A. Whether filing a class proof of claim is prohibited in the Tenth Circuit

After a careful review of Tenth Circuit case law on whether class actions are permissible in bankruptcy cases, the Court has determined that it is an open question in this jurisdiction. The Tenth Circuit decisions on the issue are not dispositive of the issue before the Court. The Tenth Circuit initially determined under the 1978 Bankruptcy Act that class proofs of claim are not permissible. *See Sheftelman v. Standard Metals Corp. (In re Standard Metals Corp.)*, 817 F.2d 625, 632 (10th Cir. 1987) ("*Standard Metals I*"), *vacated and rev'd on other grounds on rehearing*, 839 F.2d 1383 (10th Cir. 1987) ("We join those bankruptcy courts that have refused to allow class proofs of claim."). While acknowledging that neither the Bankruptcy Act nor the Bankruptcy Rules "expressly permit or expressly prohibit class proofs of claim," the Tenth Circuit reasoned in part that Bankruptcy Rule 3001(b)² requires the filing of a claim by the creditor or the creditor's authorized agent, and that, absent express authorization by all class

² All future references to "Rule" refer to the Federal Rules of Civil Procedure or the Federal Rules of Bankruptcy Procedure; those denominated in a single or double digit are Civil Rules, and those denominated in the thousands are Bankruptcy Rules.

members to an agent for filing of a proof of claim on their behalf, a class representative cannot file a class proof of claim. *Id.* at 631.³ Instead, each individual creditor must file a claim.⁴

However, after rehearing *Standard Metals I*, the Tenth Circuit decided to base its appellate ruling on other grounds, and determined that it was unnecessary for it to consider the class proof of claim issue. *Sheftelman v. Standard Metals Corp. (In re Standard Metals Corp.)*, 839 F.2d 1383, 1387 (10th Cir. 1987) (“*Standard Metals II*”) (“In view of the disposition of this appeal **it is not necessary to consider the class action claims issue.**”) (emphasis added). *Standard Metals I* is not, therefore, binding on this Court. See *Jones v. Amdura Corp. (In re Amdura Corp.)*, 170 B.R. 445, 448 (D. Colo. 1994) (holding that “the ruling of the Tenth Circuit on the issue [of class proofs of claim] is not controlling law [in the Tenth Circuit.]”); *In re The Charter Co.*, 876 F.2d 866, 869 n.4 (11th Cir. 1989) (suggesting that “the discussion of class proofs of claim in the [*Standard Metals I*] opinion may be dicta.”); *Scoggin v. Adam Aircraft Indus., Inc. (In re Adam Aircraft Indus., Inc.)*, 2009 WL 2100929, *3 (Bankr. D.Colo. Mar. 20, 2009) (observing that “the Tenth Circuit courts have not reached a definitive resolution or consensus as to the propriety of class proofs of claim.”).

At the final hearing on the Motions, the UCC directed the Court to *Unioil v. H.E. Elledge (In re Unioil, Inc.)*, 962 F.2d 988 (10th Cir. 1992), another Tenth Circuit case decided after *Standard Metals I* addressing the claims filing process. In *Unioil*, the Tenth Circuit held that even though Rule 17 permits a trustee of a trust to sue in his own name, the trustee could not file a claim on behalf of the trust in his own name without identifying his representational capacity,

³ *Standard Metals I* commented further: “Rule 3001(b) allows a creditor to decide to file a proof of claim and to instruct an agent to do so; it does not allow an ‘agent’ to decide to file a proof of claim and then inform a creditor after the fact.” *Standard Metals I*, 817 F.2d at 631.

⁴ *Id.* at 632 (“The requirement of individual filing . . . does not disappear when a large number of similar claims are involved Class action procedures can be employed in a bankruptcy proceeding only to consolidated claims that have already been properly filed.”) (citation omitted).

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notwithstanding Rule 17, because Rule 17 does not govern the procedures for filing proofs of claim. *Unioil*, 962 F.2d at 991-92. The Tenth Circuit explained that Rule 3001(a) and (b), not Rule 17, applies to claims filing requirements. *Id.* Under Rule 3001 and the official proof of claim form, the creditor or its authorized agent must execute the proof of claim, and both the person authorized to file the claim and the creditor-principal on whose behalf the claim is filed must be identified on the proof of claim. *Id.* at 992. *Unioil* cited *Standard Metals I* for the proposition that “while class action procedure is available in adversary proceedings under Bankr.R. 7023, lack of comparable provision in rules governing claims procedures precludes use of class proof of claim.” *Unioil*, 962 F.2d at 991 (citing *Standard Metals I*, 817 F.2d at 631-32 and n.10).⁵

Neither *Standard Metals I* nor *Unioil* compel this Court to conclude that class proofs of claim are prohibited. In *Unioil*, the bankruptcy court had not made Rule 7017 applicable to the claims allowance process pursuant to Rule 9014. As a result, the Tenth Circuit did not address whether a bankruptcy court can make provisions of Part VII of the Bankruptcy Rules, including the class action provisions found in Bankruptcy Rule 7023 (that incorporates Rule 23), applicable to the claims allowance procedure through Bankruptcy Rule 9014. Further, as explained below, procedures can be established so that allowing a class proof of claim will be consistent with the requirements of Rule 3001(a) and (b). No such procedures had been established or addressed in *Standard Metals I* or in *Unioil*.

This Court agrees with the Fourth, Sixth, Seventh, Ninth and Eleventh Circuits who have all held that the bankruptcy court may authorize the filing of class proofs of claim. *See Gentry v. Siegel*, 668 F.3d 83, 90 (4th Cir. 2012) (concluding “that Rule 3001 should be construed to allow

⁵ *Unioil* ultimately found that it was appropriate to allow the amendment to the proof of claim because amendment was consistent with the claims filing procedures contained in Rule 3001. *Unioil*, 962 F.2d at 992-993.

class proofs of claim, at least on a tentative basis, until the court rejects the class-action process”); *Reid v. White Motor Corp.*, 886 F.2d 1462, 1470 (6th Cir. 1989) (the Bankruptcy Code and Rules, read together, “clearly evinces the permissibility for filing a class proof of claim”); *In re American Reserve Corp.*, 840 F.2d 487, 493 (7th Cir. 1988) (it is within the judge’s discretion to allow the filing of class proofs of claim in bankruptcy cases); *Birting Fisheries, Inc. v. Lane* (*In re Birting Fisheries, Inc.*), 92 F.3d 939, 939 (9th Cir. 1996) (per curiam) (“the bankruptcy code should be construed to allow class claims”); *Charter Co.*, 876 F.2d at 873 (concluding that “class proofs of claim are allowable in bankruptcy”). *See also In re Dynegy, Inc.*, 770 F.3d 1064, 1069 (2nd Cir. 2014) (acknowledging that the bankruptcy court may apply the class action procedure to contested matters under Bankruptcy Rule 9014). No Circuit Court has held to the contrary.

In concluding that class proofs of claim are permissible, these courts reason, in part, that the bankruptcy court has the discretion to apply the class action procedures of Rule 23, by making Bankruptcy Rule 7023 applicable to contested matters under Bankruptcy Rule 9014. *See, e.g., American Reserve*, 840 F.2d at 488 (observing that “Rule 9014 thus allows bankruptcy judges to apply Rule 7023-and thereby Fed.R.Civ.P. 23, the class action rule- to ‘any stage’ in contested matters. . . . So the right to file a proof of claim on behalf of a class seems secure, at least if the bankruptcy judge elects to incorporate Rule 23 via Rule 7023 via Rule 9014”); *Reid v. White Motor*, 886 F.2d at 1469-70 (“Rule 9014 authorizes bankruptcy judges, within their discretion, to invoke Rule 7023, and thereby Fed.R.Civ.P. 23, the class action rule, to ‘any stage’ in contested matters, including, class proofs of claims.”). *See also, Charter Co.*, 876 F.2d at 873 (acknowledging that “under Bankruptcy Rule 9014, the bankruptcy judge may at his discretion

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apply Bankruptcy Rule 7023, and by extension Rule 23, in a contested matter.”) (citation omitted).

The unanimous view of the five circuits that have issued precedential decisions on the issue is supported by Rule 9014. Rule 9014 makes some but not all rules in Part VII rules automatically applicable to contested matters unless that court otherwise directs. Fed.R.Bankr.P. 9014(c). In addition, Rule 9014(c) provides: “The court may at any stage in a particular matter direct that one or more of the other rules in Part VII shall apply.” Rule 7023 is one of the other rules in Part VII.

Section 501 of the Bankruptcy Code, governing proofs of claim or interests, allows individual creditors to file proofs of claim. See 11 U.S.C. § 501(a) (“A creditor . . . may file a proof of claim”).⁶ See also *Charter Co.*, 876 F.2d at 868 (“Normally, with one enumerated exception, proofs of claim are filed individually, usually by a creditor.”) (citations omitted). Class proofs of claim do not run afoul of the requirements of § 501 because that that section does not preclude the filing of a claim by an agent. *American Reserve*, 840 F2d at 492 and 493 (stating that “[n]either the legislative history nor the structure of the 1978 Code suggests that the list in § 501 is exclusive” and finding further that “Section 501 does not interfere with filing by agents”). Class proofs of claim are also consistent with the procedural requirements of

⁶ Section 501 provides, in full:

- (a) A creditor or an indenture trustee may file a proof of claim. An equity security holder may file a proof of interest.
 - (b) If a creditor does not timely file a proof of such creditor’s claim, an entity that is liable to such creditor with the debtor, or that has secured such creditor, may file a proof of such claim.
 - (c) If a creditor does not timely file a proof of such creditor’s claim, the debtor or the trustee may file a proof of such claim.
 - (d) A claim of a kind specified in section 502(e)(2), 502(f), 502(g), 502(h), or 502(i) of this title may be filed under subsection (a), (b), or (c) of this section the same as if such claim were a claim against the debtor and had arisen before the date of the filing of the petition.
 - (e) A claim arising from the liability of a debtor for fuel use tax assessed consistent with the requirements of section 31705 of title 49 may be filed in by the base jurisdiction designated pursuant to the International Fuel Tax Agreement (as defined in section 31701 of title 49) and, if so filed, shall be allowed as a single claim.
- 11 U.S.C. § 501(a).

Bankruptcy Rule 3001, which expressly contemplates the filing of proofs of claim by “authorized agents.” Fed. R. Bankr.P. 3001(b) (“A proof of claim shall be executed by the creditor or the creditor’s authorized agent”). In a class action, where a class is certified under Rule 23, the representative of the class acts as an agent for the class in the assertion and prosecution of the class claims. *See American Reserve*, 840 F.2d at 493 (observing that a class action “is a device by which the representative is an agent for persons who have not appeared” and that “the representative is an agent only if the class is certified”) (citations omitted). Likewise, the representative of a class certified under Rule 23 may act as the authorized agent of the class for purposes of filing a class claim in a bankruptcy case if the bankruptcy court permits the filing of a class proof of claim. *American Reserve*, 840 F.2d at 493 (“The representative in a class action is an agent for the missing.”) (citation omitted). *See also Gentry v. Siegel*, 668 F3d at 91 (concluding “that creditors may file proofs of claims . . . as putative agents for members of a class who are similarly situated . . . on a conditional basis.”).⁷

The Court holds that class proofs of claim are permissible under the Bankruptcy Code and Bankruptcy Rules if the Court in the exercise of its reasonable discretion makes Rule 7023 applicable to the claims allowance procedure pursuant to Rule 9014 and establishes a procedure under which putative class members may authorize the class representative to file claims on their behalf.

B. Whether the Court should make Fed. R. Bankr.P. 7023 applicable to allow the filing of a class proof of claim

Having determined that the Bankruptcy Code and Rules permit the Court to authorize the filing of a class proof of claim in appropriate cases, the Court must determine whether, in the

⁷ *But see Kahler v. Firstplus Fin. Inc. (In re Firstplus Fin. Inc.)*, 248 B.R. 60, 69 (Bankr. N.D.Tex. 2000) (criticizing the *American Reserve* approach as contrary to the requirements of Rule 3001(b), stating that allowing class proofs of claim absent express authorization constitutes a “springing authorized agency” whereby the Court attempts to “ratify the unauthorized filing [of a class proof of claim] by the putative class representative”).

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exercise of its reasonable discretion, it should make Bankruptcy Rule 7023 applicable to the claims allowance process in this bankruptcy case so as to authorize the filing of a class proof of claim.

After reviewing the relevant case law, the Court has concluded that the following factors are relevant to the Court's determination of whether to make Rule 7023 applicable to the claims allowance process in a particular case:

- 1) Whether a class has been certified in a class action lawsuit whose members are those on whose behalf a class claim would be filed, and, if not, whether the putative class representative has satisfied or potentially can satisfy the requirements of Rule 23 for certification of the class.⁸ If a class cannot be certified under Rule 23, then making Rule 7023 applicable to the claims allowance process would be pointless as it could not result in a grant of authority to file a class claim.⁹
- 2) Whether the notice of the claims bar date to class members or putative class members provides them with a meaningful opportunity to assert their claims in the bankruptcy case absent the filing of a class claim,¹⁰ and whether the public policy reasons favoring class action suits should be applied to the claims process in the bankruptcy case.¹¹ This factor includes an examination of the nature of the class action, including whether it is an opt-in or opt-out class.
- 3) The timing of the request to file a class proof of claim.¹²

⁸ See *In re Sacred Heart Hospital of Norristown*, 177 B.R. 16, 22 (Bankr. E.D.Pa. 1995) (application of Rule 7023 to allow class proof of claim is best suited to pre-petition class certification by a nonbankruptcy court); *In re Craft*, 321 B.R. 189 (Bankr. N.D.Tex. 2005) (finding that class proofs of claim are permissible when the class was certified prepetition). See also *Reid v. White Motor*, 886 F.2d at 1471 (putative class representative seeking to file a class proof of claim must be authorized to represent the class).

⁹ Cf. *In re Computer Learning Centers, Inc.*, 344 B.R. 79, 86 (Bankr. E.D.Va. 2006) (expressing a two-step approach to the class proof of claim process: 1) determine whether Rule 7023 should be applied to the claims process; and 2) decide whether to certify the class under Rule 23, but that “[a] decision favorable to the class on one step is not sufficient” to allow the filing of a class proof of claim).

¹⁰ See *Adam Aircraft*, 2009 WL 2100929 at *8 (suggesting that application of Rule 7023 to the claims process as a contested matter may be appropriate “when notice of the case or bar date is inadequate or when unnamed class members are in large part ‘unknown creditors.’”) (quoting *Bailey v. Jamesway Corp. (In re Jamesway Corp.)*, 1997 WL 327105,*5 (Bankr.S.D.N.Y. June 12, 1997) (deciding whether to apply Rule 7023 to an adversary proceeding)).

¹¹ See *Charter*, 876 F.2d at 871 (applying Rule 23 to allow class proofs of claim is consistent with “the goal of permitting the prosecution of small claims which would not be economical to prosecute individually”); *In re Musicland Holding Corp.*, 362 B.R. 644, 651 (Bankr. S.D. N.Y. 2007) (proponent of class proof of claim “must . . . show that the benefits derived from the use of the class claim device are consistent with the goals of bankruptcy”) (citing *In re Woodward & Lothrop Holdings, Inc.* 205 B.R. 365, 369 (Bankr. S.D.N.Y. 1997)); *Adam Aircraft*, 2009 WL 2100929 at * 9 (declining to apply 7023 to allow a class proof of claim where all potential class members had already been given notice of the claims bar date and had “already been afforded one bite at the claims apple”).

¹² See *Reid v. White Motor*, 886 F.2d at 1471 (refusing to allow claimant to file class proof of claim where putative class representative “failed to timely petition the bankruptcy court to apply the provisions of Rule 9014 and 7023”);

- 4) Whether potential jurisdictional issues serve as an impediment to filing a class proof of claim, such as subjecting class members to the jurisdiction of the bankruptcy court as to claims by the debtor against them.
- 5) The potential impact of the filing of a class proof of claim on the Debtor's reorganization prospects and the potential prejudice to other creditors and potential benefit to members of the class or putative class.¹³

The Court will address each of these factors in turn. Because the Court has ruled that it will certify the class in the Class Action Suit, if the Court makes Bankruptcy Rule 7023 applicable to the claims allowance process, the Court will also authorize Ms. Tullie to file a class proof of claim for those members of the class who authorize her to do so.

1. *Class Certification*

The Court has ruled that it will certify the class in the Class Action Suit. If the Court authorizes a class proof of claim, the filing of a class claim therefore will not result in thousands of individually litigated contested matters. The certified class is an opt-out class. As described below, a procedure could be put in place to ensure that Ms. Tullie has authority to file a claim on behalf of class members. This factor weighs in favor of applying Rule 7023 to the claims allowance process.

2. *Notice and the Nature of the Class Action*

The second factor involves whether the notice of the claims bar date to class members or putative class members provides them with a meaningful opportunity to assert their claims in the bankruptcy case absent the filing of a class claim and how public policy considerations impact the class claim issue. Quick Cash argues that traditional policies underlying class action

Computer Learning, 344 B.R. at 89 (“A Rule 7023 motion should be filed as soon as practicable and should be denied if it comes so late as to prejudice a party.”).

¹³ See *Musicland*, 361 B.R. at 656 (declining to apply Rule 7023 to authorize the filing of a class proof of claim where allowance of a class proof of claim would greatly delay the administration of the bankruptcy case); *Craft*, 321 B.R. at 199 (factors relevant to the court's decision to apply Rule 7023 “include . . . prejudice to the debtor or its other creditors, prejudice to putative class members, efficient estate administration, the conduct in the bankruptcy case of the putative class representatives, and the status of proceedings in other courts.”).

litigation do not apply in bankruptcy cases. Those policies include concentrating a large number of claims in one forum to promote judicial economy and avoid inconsistent results. In bankruptcy cases, a large number of claims can be concentrated in the bankruptcy forum and decided by the same judge. While these arguments may be persuasive in some cases, particularly where there is an opt-in class or individual class claims are large, they are not compelling here. The second factor weighs in favor of allowing the filing of a class claim for two reasons.

First, despite notice to more than 4700 putative class members of the claims bar date,¹⁴ not more than seven filed claims based on the claims alleged in the Class Action Suit by the originally set claims bar date. That is understandable, given the fact that the class claims are relatively small consumer claims of a type that normally would be held by unsophisticated individuals who may not understand that they even have a claim. The low number of filed claims suggests the claim did not have a meaningful opportunity to protect their interests by filing a claim.

Second, requiring all individual class members to file individual proofs of claim would effectively change the nature of the class from an “opt-out” class to an “opt-in” class.¹⁵ Failure to file a claim in the bankruptcy case would bar the claim, effectively excluding the claimant from the class. Excluding members from the class unless they file an individual proof of claim would be inconsistent with the policies underlying opt-out classes. There are potentially a large

¹⁴ Ms. Tullie has alleged that there are over 4,700 potential class members in the Class Action Suit, which the Quick Cash does not dispute. See Adversary Proceeding No. 15-1063 J - Docket No. 1- 5.

¹⁵ This Court has certified a class in the Class Action Suit under Rule 23(a) and 23(b)(3). See Adversary Proceeding No. 15-1063 Docket No. 17. The class is an opt-out class, meaning that all putative class members will be members of the class unless they opt out of the class. See Rule 23(c)(2)(B) (under Rule 23(c)(2)(B), the notice to members of a class certified under Rule 23(b) must, among other things, inform the class member “that the court will exclude from the class any member who requests exclusion.”). See Rule 23(c)(2)(B)(v). Thus, a member of a class certified under Rule 23(b)(3) will automatically be included within the class unless the class member “opts out” of the class. *Id.* See also *In re Integra Realty Res., Inc.* 354 F.3d 1246, 1263 (10th Cir. 2004) (acknowledging that Rule 23(b)(3) “allows class members to opt out of the class”).

number of creditors who may be unaware that they have potential claims against Quick Cash as part of the Class Action Suit. Allowing a class proof of claim would promote the class action “goal of permitting the prosecution of small claims which would not be economical to prosecute individually.” *Charter Co.*, 876 F.2d at 871. Not allowing the filing of a class proof of claim could lead to class decertification if substantially all the claims of class members are time barred in the bankruptcy case.

The Court previously determined that the Claims Bar Date Notice provided inadequate notice to the putative class members of the general claims bar date.¹⁶ An additional claims bar date notice to putative class members can require members who do not wish to authorize Ms. Tullie to file a class proof of claim on their behalf to file a notice withholding their consent or to file an individual claim and thereby exclude themselves from a class claim. Creditors can be apprised that the failure to file the notice or an individual proof of claim would constitute a grant of authority for Ms. Tullie to file a claim on their behalf.

SFI objects to Quick Cash using cash collateral to send additional notice of an extended claims bar date to putative class members and others. But, by obtaining a general claims bar date using the *ex parte* procedure available in this district under circumstances in which fixing a claims bar date is a routine matter, without informing the Court of the existence the Class Action Suit and the potential class action claims, Quick Cash took the risk that the Court might find that special noticing procedures may be required. If Quick Cash wishes for the Court to establish a claims bar date, it must bear the cost of giving appropriate notice.¹⁷

¹⁶ See Scheduling Order Resulting from Preliminary Hearing on Emergency Motion to Enforce Settlement Agreement and Request for Hearing – Docket No. 52 (finding “that meaningful notice was not given to the putative class members . . . [and] that the Bar Date Notice was inadequate to provide reasonable notice to creditors.”) (citing *Rowe Int’l, Inc. v. Herd (In re Herd)*, 840 F.2d 757, 759 (10th Cir. 1988)).

¹⁷ Of course, any notice to putative class action members required pursuant to Rule 7023 in the Class Action Suit will be borne by the plaintiffs in that adversary proceeding.

3. *Timing of the Request*

The third factor, the timing of the request to file a class proof of claim, weighs in favor of allowing a class claim. Rule 9014 contains no time limitation for requesting the Court to apply Rule 7023 to a contested matter. *See* Fed.R.Bankr.P. 9014(c) (“the Court may at any stage in a particular matter direct that one or more of the other rules I Part VII shall apply.”); *Computer Learning*, 344 B.R. at 89 (“Rule 9014 establishes no deadline for filing a Rule 7023 motion.”). Although generally it takes an objection to a claim to initiate a contested matter,¹⁸ a putative class representative seeking to file a class proof of claim may request the Court to apply Rule 7023 before filing a proof of claim. *See Musicland*, 362 B.R. at 651 (acknowledging that courts have taken a more practical approach in allowing a class representative to “move at any time for a declaration that it may file a class proof of claim”) (citations omitted); *Computer Learning*, 344 B.R. at 88 (reasoning that “the issue in controversy is whether the proof of claim may be filed as a class proof of claim in the first instance. This is the contested matter. It is resolved by filing a Rule 7023 motion which itself commences the contested matter.”).¹⁹

The Court finds that the UCC and the CCC filed their Motions in sufficient time for the Court to address their request to permit the filing of a class claim, without undue interference with the bankruptcy proceeding or the claims allowance process. The UCC and the CCC acted promptly. The Court extended the original September 23, 2015 claims bar date to December 23, 2015, before it otherwise would have expired, and can extend it further if a further extension is

¹⁸ *See* 11 U.S.C. § 502(a) (“A claim or interest, proof of which is filed under section 501 of this title, is deemed allowed, unless a party in interest . . . objects.”); *In re Trans World Airlines, Inc.*, 280 B.R. 806, 807 (D. Del. 2002) (“if a proof of claim is objected to, the claim will be a contested matter between the debtor and claimant”); *Musicland*, 362 B.R. at 651 (“[T]he filing of a proof of claim does not trigger a contested matter. Instead the objection to the claim commences the contested matter.”) (citing *Woodward & Lothrop*, 205 B.R. at 369-70).

¹⁹ *See also Ephedra Products Liability Litigation*, 329 B.R. 1, 6 (S.D.N.Y. 2005) (requiring an objection to claim before making a request to apply Rule 23 “would mean that a debtor and others with interests adverse to a class claim could prevent the claimant from asking the court to apply Rule 23 simply by withholding their objections until the eve of confirmation and then move to expunge the class claim on the grounds that applying Rule 23 would unduly delay distribution.”).

appropriate. Following the hearing on the CCC's motion to extend claims bar date and on Ms. Tullie's Motion to Enforce Settlement Agreement,²⁰ the Court issued a Scheduling Order fixing a deadline of October 9, 2015 for any party in interest to file a motion requesting the Court to allow the filing of class proofs of claim.²¹ The UCC and the CCC filed their Motions by the October 9, 2015 deadline, about three months after commencement of the bankruptcy case. Quick Cash has not yet filed a proposed plan of reorganization.

In addition, although the absence of pre-petition class certification in some instances could weigh against allowing the filing of a class proof of claim, that is not so here. At the time this bankruptcy case was commenced, the issue of class certification in the Class Action Suit was ripe for a decision. The tentative settlement between the parties, and subsequent litigation over its enforceability before this Court, delayed class certification. Nevertheless, about four months after commencement of the bankruptcy case and prior to expiration of the claims bar date, this Court ruled that it will certify the class. These circumstances support the Court's determination that the timeliness factor weighs in favor of allowing the filing of a class proof of claim.

4. *Jurisdictional Constraints*

SFI and Quick Cash assert that filing a class proof of claim raises jurisdictional concerns. Quick Cash's portfolio of consumer loans appears to be its primary asset. SFI points out that many if not most of the putative class members likely are borrowers who owe money to Quick Cash. SFI and Quick Cash assert that the Court should not authorize a class proof of claim because doing so will subject the members of the class to the jurisdiction of this Court. SFI asserts further that by subjecting the class members to the jurisdiction of this Court, many could

²⁰ The Motion to Enforce Settlement Agreement and the CCC's motion to extend the claims bar date each included a request for the Court to apply Fed.R.Bankr.P. 7023 to the claims administration process.

²¹ See Scheduling Order Resulting from Preliminary Hearing on Emergency Motion to Enforce Settlement Agreement and Request for Hearing – Docket No. 52.

lose defenses to claims against them by Quick Cash or be deprived of a favorable forum in Tribal Court.

Filing a proof of claim subjects the creditor to the jurisdiction of the Bankruptcy Court to determine the claim. *See Langenkamp v. Culp*, 498 U.S. 42, 44, 111 S.Ct. 330, 112 L.Ed.2d 343 (1990) (“by filing a claim against a bankruptcy estate the creditor triggers the process of ‘allowance and disallowance of claims,’ thereby subjecting himself to the bankruptcy court’s equitable power.”) (quoting *Granfinanciera v. Nordberg*, 492 U.S. 33, 58, 109 S.Ct. 2782, 106 L.Ed.2d 26 (1989)). However, the filing of a proof of claim does not constitute consent by the creditor to the jurisdiction of the bankruptcy court to adjudicate state law counterclaims asserted by the debtor against the creditor, unless the counterclaim would necessarily be resolved in the claims allowance process. *See Stern v. Marshall*, ___ U.S. ___, 131 S.Ct. 2594, 180 L.Ed.2d 475 (2011) (holding that Article III of the Constitution prevents the bankruptcy court from issuing a final judgment on a debtor’s state law counterclaims against a creditor who files a claim against the estate, absent consent by the creditor, unless adjudication of the claim against the estate necessarily resolves the counterclaim). It does not appear that adjudication of Ms. Tullie’s class claims would, in general, necessarily resolve a claim by the estate against a claimant for breach of a loan agreement.

Any potential jurisdictional impact on class members by authorizing the filing of a class claim can be eliminated or diminished in two ways. First, all putative class claim members will be given an opportunity to opt out of the class on whose behalf the class representative files a class claim, and will receive a notice explaining the consequences of not opting out. Second, the Court could abstain, where appropriate, from hearing claims by the Quick Cash against members of the class who otherwise could have the claims heard in Tribal Court.

5. Impact on Reorganization Prospects and the Benefit or Prejudice to Creditors

The fifth factor for the Court to consider is the potential impact of the filing of a class proof of claim on the Quick Cash's prospect of successfully reorganizing and the potential benefit to members of the class or putative class and the potential prejudice to other creditors. The Court has insufficient information to assess whether the class claimants would actually receive a distribution on their claims if the claims were allowed, or, if so, in what amount. The Court also has insufficient information to assess the impact of allowing class claims on the recovery by other creditors on their claims or on the long term ability of Quick Cash to continue to operate.

In addition, the CCC has identified several other potential classes of consumer claimants, including consumers holding claims based alleged unlawful repossessions, "loan splitting and multiple refinancing issues," and unlawful withholding of important original documents, such as social security cards and vehicle titles. *See* Docket No. 55. None of these claims have been asserted in a class action lawsuit. Before the Court can assess the impact of authorizing Ms. Tullie to file a class proof of claim, the Court must know whether other class claims will be filed.

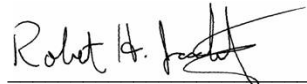
The Court requires evidence to assess the fifth factor. Accordingly, the Court will set an evidentiary hearing on the Tullie Motion. The type of evidence that may be relevant to the fifth factor includes, for example, evidence regarding Quick Cash's historical profitability, the reasons that Quick Cash commenced its Chapter 11 case, the amount of Quick Cash's liabilities and the value of its assets, Quick Cash's projected future profitably, and whether authorization of a class claim will affect Quick Cash's ability to use cash collateral.

WHEREFORE, IT IS HEREBY ORDERED:

1. The Motions are GRANTED, to the extent they seek a determination that class proofs of claim are permissible in bankruptcy.

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2. The first four factors the Court considers to determine whether to apply Rule 7023 to allow the filing of a class proof of claim in this case weigh in favor of allowing Ms. Tullie to file a class proof of claim. The fifth factor requires the Court to assess the impact of allowing a class proof of claim on the reorganization prospects and the benefit or detriment to other creditors. Further evidence on this factor is required before the Court can rule on the pending Motions.
3. A status conference on the Motions will be held on **November 12, 2015 at 9:00 a.m.** in the Sandia Courtroom, thirteenth floor, Dennis Chavez Federal Building and United States Courthouse, 500 Gold Ave. SW, Albuquerque, New Mexico to schedule a continued final, evidentiary hearing on the Motions and to address any other issues related to the pending Motions.



ROBERT H. JACOBVITZ
United States Bankruptcy Judge

Date entered on docket: November 10, 2015

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THE PAWN TRANSACTION EXCLUSION: (MOSTLY)
A MATTER OF STATE LAW AND TIMING

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A. Section 541(b)(8)

Section 541(b)(8)¹ was added by BAPCPA. It is very broadly written, but has been widely interpreted as intended to protect pawnbrokers by allowing them to retain their possessory security interests.² It excludes from property of the estate collateral pledged or sold for a loan if: (1) the transferee is in possession of the property; (2) the debtor has no obligation to buy back the property and (3) neither the debtor, nor the trustee has exercised a redemption right under state statute or contract law in a timely manner according to section 108(b).³

A pawn transaction necessarily requires a consideration of property interests. As we all know, “property interests are created and defined by state law.”⁴ The court in *In Re Northington*⁵ noted that the inquiry is two-tiered. First, the question is what constitutes property of the estate. The second inquiry is into the nature of debtor’s property interests, which turns on state law.⁶ States have long regulated pawn transactions.⁷ The *Northington* court concluded that the “Bankruptcy Code takes an estate’s constituent property interest as it finds them.” If the

¹ 11 U.S.C. §541(b)(8) states:

(b)Property of the estate does not include...

(8)subject to subchapter III of chapter 5, any interest of the debtor in property where the debtor pledged or sold tangible personal property (other than securities or written or printed evidences of indebtedness or title) as collateral for a loan or advance of money given by a person licensed under law to make such loans or advances, where—

(A) the tangible personal property is in the possession of the pledgee or transferee;

(B) the debtor has no obligation to repay the money, redeem the collateral, or buy back the property at a stipulated price; and

(C) neither the debtor nor the trustee have exercised any right to redeem provided under the contract or State law, in a timely manner as provided under State law and section 108(b)...

² See, e.g. *In Re Martin*, 418 B.R. 710, 713 (Bankr. S.D. Ohio 2009).

³ Collier on Bankruptcy ¶5-41.24 (16th Ed. 2015); see, also *In Re Mosher*, 2007 WL 1487399 (Bankr. D. Mont.)

⁴ *Buiner v. United States*, 440 U.S. 48, 55 (1992).

⁵ 876 F. 3d 1302 (11th Cir. 2017).

⁶ *Id.*, at 1311.

⁷ *Id.* at 1312.

nature of the asset is unchanging, then the nature of the asset does not change upon entry into the bankruptcy estate. But if the nature of the asset is dynamic and changeable, then “that characteristic will follow the asset into the estate.”⁸

For example, under the Georgia pawn statutes, which the *Northington* court examined, after the loan’s maturity date the debtor had a conditional right to possess the collateral and to redeem it, but after the redemption period, the debtor had no further rights in the property and they were extinguished.⁹ The property, thus, “evaporated” from the estate.

B. Right to Redeem

It is an understatement to note that pawnshop laws vary widely from jurisdiction to jurisdiction.¹⁰ But very generally speaking, the majority of jurisdictions provide that pawned property automatically vests in the pawnbroker at the end of the redemption period.¹¹ The redemption period may or may not be set by statute. Because a lot of the case law regarding pawn transactions was decided under Georgia law, it is a good example.

Georgia law permits a borrower to pledge a motor vehicle by providing a certificate of title.¹² All pawn transactions must be for at least 30 days, but may be extended for an additional 30 days by written agreement of the parties.¹³ If the parties do not agree to extend the transaction period and the borrower does not pay the amounts owing, the borrower has an additional grace period of 30 days to redeem the property, in the case of motor vehicles.¹⁴ At the end of the period the collateral automatically forfeits to the pawnbroker.¹⁵

⁸ *Id.*, at 1314.

⁹ *Id.*, at 1315.

¹⁰ *See, In Re Sorensen*, 586 B.R. 527, 336 n. 7 (9th Cir. BAP 2018).

¹¹ *See, e.g.* O.C.G.A. §44-12-130(5); *In Re Howard*, 507 B.R. 394, 397 (Bankr. N.D. Ga. 2014).

¹² O.C.G.A. §44-12-131(a)(1).

¹³ O.C.G.A. §44-14-403(b).

¹⁴ O.C.G.A. §44-14-403(b)(3).

¹⁵ *In Re Moore*, 448 B.R. 93, 100 (Bankr. N.D. Ga. 2011).

If the redemption and grace periods expired before the borrower filed for bankruptcy relief and the pawnbroker has repossessed the vehicle, the pawned collateral does not become property of the estate.¹⁶ But if the debtor files a petition while there is still a right to redeem, the right of redemption becomes property of the estate.¹⁷

Section 541(b)(8)(C) specifically refers to section 108(b) in determining what constitutes redemption in a “timely” manner. Under section 108(b), any period to “cure a default, or perform any other similar act” under non-bankruptcy law is extended for 60 days from the date of the order for relief.¹⁸ It is well accepted that section 108(b) controls the pawn transaction redemption period. Although section 362(a), the automatic stay, is not specifically excluded under section 541(b)(8) (and the relationship and will be discussed below), in general it does not apply to indefinitely extend the redemption period.¹⁹

C. Sorensen²⁰ and the Automatic Stay

In a case of first impression the Ninth Circuit BAP held that under California law, because the pawnshop failed to validly terminate the redemption period, pawned jewelry entered and then remained property of the estate. The automatic stay prevented the pawnshop from sending a notice postpetition to terminate the redemption period. In March, 2016 the debtor pledged five pieces of jewelry as collateral for five pawn loans. The debtor later obtained replacement loans with a termination date of November 18, 2016. She filed for bankruptcy relief under Chapter 13 before the termination date of the pawn loans.

Sorensen proposed a Chapter 13 plan, which listed the pawnshop as a secured creditor and sought to pay off the loans through the plan. Postpetition on November 18, 2016, the

¹⁶ *Howard*, 507 B.R., at 398 (and cases cited therein).

¹⁷ *In Re Paul*, 534 B.R. 430, 432 (Bankr. M.D. Ga. 2015).

¹⁸ 11 U.S.C. §108(b).

¹⁹ *Sorensen*, 586 B.R. at 336 n. 6; *Mosher*, 2007 WL 1487399*8; *In Re Schmitt*, 20 B. R. 57, 66-67 (Bankr. D. Mont. 2002), *Dunlap v. Cash Pawn of Nashville (In Re Dunlap)*, 158 B.R. 724, 728 (M.D. Tenn. 1993).

²⁰ *In Re Sorensen*, 586 B.R. 327 (9th Cir. BAP 2018).

pawnshop sent a notice of loan termination providing a ten day right to redemption as required by state law. The debtor filed an adversary complaint against the pawnshop and sought injunctive relief to stop the pawnshop from disposing of the jewelry, claiming it was property of the estate. Her proposed plan was confirmed, there being no objection from the pawnshop.

California law allowed a four month loan period, which expired on November 18, 2016.²¹ But if the pawn collateral was not redeemed before the end of the loan period the pawnshop had to issue a notice of the loan termination and provide a ten-day redemption period.²² The court found that the debtor's right to redeem the jewelry was property of the bankruptcy estate.²³

Next the court held that under California law §548(b) does not automatically exclude pawned property because there is a requirement that the pawnshop issue an additional ten day notice and redemption period. Finally, the court determined that the ten-day notice, sent post-petition was an act "to exercise control over property of the estate[.]" to 'enforce a lien [that]...secures a claim[.]' and 'to collect, assess or recover a claim against the debtor'" in violation of sections 362(a)(3),(5) and (6).²⁴ The pawnshop failed to seek relief from stay to issue the postpetition notice. The redemption notice was thus void ab initio. The ten-day period never began to run, the debtor's redemption right was never extinguished and the pawnshop never took title. Section 541(b)(8) failed to exclude the jewelry from the estate.

²¹ Cal. Fin. Code §2101(d).

²² *Sorensen*, 586 B.R. at 334.

²³ *Id.*, at 332.

²⁴ Section 362(a) provides in relevant part:

(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title...operates as a stay, applicable to all entities of—

...

(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;

...

(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;

(6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title[.]

§362(a)(3), (5), (6).

The court analyzed the *Northington* court's reasoning in some depth, agreeing with it all. The difference the court said was in the application of state law.²⁵ In an enlightening footnote the court discussed how widely divergent pawnshop laws were. In particular it noted that only thirteen jurisdictions require additional notice like California's statute: California, Kentucky, New York, Ohio, Oregon, Pennsylvania, South Carolina, Wisconsin, District of Columbia and Guam.²⁶

In *Sorensen* the court found that the pawnshop's failure to seek relief from the automatic stay voided the termination of the pawn loan redemption period. In *In Re Spinner*,²⁷ a bankruptcy court in Georgia found the entire pawn transaction void. The court found that the pawnshop violated both TILA²⁸ and Georgia law regarding the contractual requirements of the Georgia Pawnshop Act. Both laws required strict construction. The pawnshop charged excessive interest rates, which rendered the transaction void.²⁹

Consequently, the pawned vehicle became property the estate and was protected by the automatic stay. When the pawnshop sold the vehicle postpetition, it was a willful violation of the automatic stay. The court awarded damages under section 362(k) including \$2,356.70 for emotional distress.³⁰

D. Effect of a Confirmed Plan Under §1327(a) on the Pawn Transaction

Sorensen noted, but did not decide, whether the pawnshop was bound by the terms of a confirmed plan under §1327(a) and *Espinosa*,³¹ finding that it was affirming on a separate,

²⁵ *Sorensen*, 586 B.R. at 335.

²⁶ *Id.*, at 336 n. 7.

²⁷ 398 B.R. 84 (Bankr. N.b. Ga 2008).

²⁸ Truth In Lending Act; 15 USC §1601, *et. seq.*

²⁹ *Spinner*, 398 B.R. at 94.

³⁰ *Id.*, at 95-97.

³¹ 11 U.S.C. §1327(a); *Espinosa v. United Student Aid Funds, Inc.*, 553 F.3d 1193 (9th Cir. 2008) *aff'd*, 559 U.S. 260 (2010).

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sufficient ground.³² Red Flag Warning: the wise pawnbroker should not, as occurred in *Sorensen*, ignore the confirmation process. The cases are intensely fact specific, but even under Eleventh Circuit law the failure of a pawnshop to participate and object to confirmation can bar it from complaining later. In *In Re Young*,³³ a case, which predated the exclusion under §541(b)(8), the court considered a pledge of musical equipment and whether the automatic stay applied.

At the time the debtors filed for bankruptcy protection under Chapter 13 the debtors still had a right of redemption in the musical equipment. Consequently §108(b) extended the redemption period for 60 days. The debtors were able to confirm a plan within the extended redemption period.³⁴ The court, thus, was able to distinguish *In Re Dunlap*.³⁵

The court next rejected the pawnshop's claim that it was not in a debtor/creditor relationship with the debtor. Under Alabama law, the pawn transaction was described as a "loan" and the pawn ticket stated that debtor gave a security interest in the pawned goods and even included a repayment schedule.³⁶ Further, debtor proposed to pay the pawnshop 100% of the loan amount, listed it as a secured creditor and sent notice of the confirmation hearing. The pawnshop failed to object and declined to participate. The pawnshop slept on its rights and was barred by res judicata from belatedly asserting its claim. The court found that the musical equipment was property of the estate and protected by the automatic stay.³⁷

³² *Sorensen*, 586 B.R. at 336.

³³ 281 B.R. 74 (Bankr. S.D. Ala. 2001).

³⁴ *Id.*, at 77.

³⁵ 158 B.R. 724 (Bankr. M.D. Tenn. 1993)(Holding that when a redemption period expired pre-petition a contract could not be modified under §1322(b) because all title and interest in the goods have vested in the pawnbroker), *see also In Re Howard*, 507 B.R. 394 (Bankr. N.D. Ga. 2014)(Debtor's obligation matured before case filed).

³⁶ 281 B.R. at 78-79.

³⁷ *Id.*, at 79-80, but *see, In Re Moore*, 448 B.R. 93 (Bankr. N.D. Ga. 2011)(while the pawned vehicles were property of the estate the debtors are required to take affirmative steps to exercise right of redemption and the Chapter 13 plan may not be used to do so); *see also Charles Hall Motors, Inc. v. Lewis (In Re Lewis)*, 137 F. 3d 1280 (11th Cir. 1998)(Prepetition repossession of vehicle left debtor with only the right to redeem by paying debt in full).

Similarly, in *In Re Jackson*,³⁸ the debtor's confirmed a plan to which a pawnshop with a security interest in debtor's vehicle failed to object. The court noted defects in the pawn transaction, but focused on the pawnshop's failure to object to the plan.³⁹ The pawnshop did not deny that it received notice of the proposed plan. In fact, the pawnshop filed a proof of claim and the court found that the filing of the proof of claim constituted acceptance of the plan.⁴⁰

E. Title Loans

Whether title loans on motor vehicles are "pawn transactions" is, of course, a matter of state law. It is apparent, for example, that title loans are pawn transactions under Georgia law.⁴¹ There are, however, significant differences between traditional pawn transactions and title loans. In *In Re Schwab*⁴², Judge Markell authored a tome length opinion, which examined the characterization of title loans under Nevada law.

The debtor obtained title loans on two vehicles prepetition. The court first defined the traditional pawnbroker transaction. Pawnbrokers are bailees of property held as collateral for loans. If the loan is not paid the pawnbroker sells the goods, keeps the proceeds and the debtor is not liable for a deficiency. The transaction requires delivery of the collateral to the pawnbroker.⁴³ The pawnshop in *Schwab* did not hold the vehicles, only the certificates of title. The court rejected the pawnshop's claim of constructive possession, finding no basis for the concept under Nevada law.⁴⁴

The court went on to find that the pawn ticket was a security agreement, which it attached and was perfected through the Department of Motor Vehicles. Consequently, the pawnshop was

³⁸ 2007 WL 954751 (Bankr. E.D. Pa.).

³⁹ *Id.*, at *3-*b.

⁴⁰ *Id.*, at *7 - *10.

⁴¹ *See, generally, In Re Bell*, 279 B.R. 890 (Bankr. N.D. Ga. 2002)(Examining whether involuntary forfeiture of pawned vehicle might be a fraudulent transfer under §548(a)(1)(B) and thus property of the estate under §541(a)(3)).

⁴² 347 B.R. 726 (Bankr. D. Nev. 2006).

⁴³ *Id.*, at 739.

⁴⁴ *Id.*, at 740.

obligated to proceed under Part 6 of Article 9. The pawnshop's strict foreclosure on the vehicles violated Article 9.⁴⁵ The court assessed damages for those violations which were offset against the pawnshop's claims. The court confirmed a plan in which the pawnshop's claims were crumpled down to the original loan amounts and paid over 36 months at 10% interest.⁴⁶

As noted previously, Nevada law varies significantly from Georgia law. Under Georgia law, by statute, possession of a certificate of title constitutes constructive possession of the vehicle.⁴⁷ The Nevada legislature passed a law regulating title loan services, just before the decision in *Schwab*.⁴⁸ It specifically provided for the application of the Uniform Commercial Code to title loans.⁴⁹

F. Recap

Section 541(b)(8) excludes pawn collateral from property of the estate when the pawn loan has terminated and the redemption period has expired. If the debtor's right to redemption has not expired when the petition is filed, then it is extended for 60 days under Section 108(b). The automatic stay does not generally apply to indefinitely extend the redemption period but pawn transactions are defined and regulated under state law. Thirteen jurisdictions including California require an additional notice and redemption period. In *Sorensen*, the court determined that under California law issuing the additional notice violated the automatic stay. The attempt to terminate the redemption period was, thus, void ab initio and the pawn collateral remained property of the estate. Motor vehicle title loans may or may not be pawn transactions depending on the state law.

⁴⁵ *Id.*, at 747-52.

⁴⁶ *Id.*, at 759, NRS Chapter 104.

⁴⁷ O.C.G.A. 6.A 344-12-1230(5), O.C.G.A. 44-12-130(5).

⁴⁸ NRS Chapter 604A.

⁴⁹ NRS §604.5078(1) states: NRS 604A.5078 Applicability of Uniform Commercial Code; repossession of vehicle; civil action. 1. Except where in conflict with provisions of this section, the provisions of chapter 104 of NRS apply to any title loan between a licensee who operates a title loan service and a customer.

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586 B.R. 327
 United States Bankruptcy Appellate
 Panel of the Ninth Circuit.

IN RE: Sydney Eileen SORENSEN, Debtor.
 Schnitzel, Inc., dba R & J Jewelry & Loan, Appellant,
 v.
 Sydney Eileen Sorensen, Appellee.

BAP No. NC-17-1152-FBTa

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 Bk. No. 16-52281

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 Adv. No. 17-05018

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 Argued and submitted on May 25,
 2018 at San Francisco, California

|
 Filed—June 15, 2018

Synopsis

Background: Chapter 13 debtor sued for declaratory and injunctive relief to prevent pawnbroker from selling jewelry that she had pawned prepetition. Pawnbroker moved to dismiss. The United States Bankruptcy Court for the Northern District of California, Stephen J. Johnson, J., denied motion, and pawnbroker appealed.

Holdings: The Bankruptcy Appellate Panel, Faris, J., as matter of apparent first impression, held that:

[1] all of debtor's interests in jewelry that she had pawned prepetition, including any unexpired redemption rights, became part of her bankruptcy estate as of commencement of her Chapter 13 case, and

[2] notice of termination of loan which pawnbroker issued postpetition was void ab initio as violative of automatic stay.

Affirmed.

West Headnotes (12)

[1] **Bankruptcy**

☞ Conclusions of law;de novo review

Bankruptcy Appellate Panel reviews pure questions of law de novo on appeal from bankruptcy court's decision.

Cases that cite this headnote

[2] **Bankruptcy**

☞ Conclusions of law;de novo review

De novo review is independent review, that gives no deference to lower court's conclusions.

Cases that cite this headnote

[3] **Bankruptcy**

☞ Property pledged or encumbered; redemption rights

Debtor's pre-foreclosure right to redeem is a property right which, if it has not expired prior to commencement of bankruptcy case, is included in "property of the estate." 11 U.S.C.A. § 541(a)(1).

Cases that cite this headnote

[4] **Bankruptcy**

☞ Property pledged or encumbered; redemption rights

Rights that debtor retains in her pawned property as of commencement of bankruptcy case are included in "property of the estate." 11 U.S.C.A. § 541(a)(1).

Cases that cite this headnote

[5] **Bankruptcy**

☞ Property pledged or encumbered; redemption rights

All of Chapter 13 debtor's interests in jewelry that she had pawned prepetition, including any unexpired redemption rights, became part

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of Chapter 13 estate as of commencement of her bankruptcy case. 11 U.S.C.A. § 541(a)(1).

Cases that cite this headnote

Automatic stay does not toll state law redemption periods. 11 U.S.C.A. § 362(a).

Cases that cite this headnote

[6] **Finance, Banking, and Credit**

↔ Rights and liabilities as to goods pawned

Right to redeem pawned property under California law does not expire until ten days after the pawnbroker gives proper notice to the pledgor of termination of loan. Cal. Fin. Code § 21201(d, f).

Cases that cite this headnote

[7] **Bankruptcy**

↔ Proceedings, Acts, or Persons Affected

Bankruptcy

↔ Validity of acts in violation of injunction or stay

Notice of termination of loan which pawnbroker issued postpetition, only after the debtor-pledgor had filed for Chapter 13 relief, and which pawnbroker had to issue under California law in order to start the ten-day time limit on debtor-pledgor's state law right to redeem jewelry that she had pawned prepetition, was act "to exercise control over property of the estate," which, having been taken postpetition without moving for relief from automatic stay, was void ab initio as violative of stay and ineffective to start this redemption period running. 11 U.S.C.A. § 362(a)(3); Cal. Fin. Code § 21201(d, f).

Cases that cite this headnote

[8] **Bankruptcy**

↔ Validity of acts in violation of injunction or stay

Actions taken in violation of automatic stay are void. 11 U.S.C.A. § 362(a).

Cases that cite this headnote

[9] **Bankruptcy**

↔ Redemption period

[10] **Bankruptcy**

↔ Effect of state law in general

Property interests in bankruptcy are created and defined by state law.

Cases that cite this headnote

[11] **Bankruptcy**

↔ Effect of state law in general

Unless some federal interest requires a different result, there is no reason why property interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding.

Cases that cite this headnote

[12] **Bankruptcy**

↔ Effect of state law in general

Undefined considerations of equity provide no basis for adoption of a uniform federal rule displacing state property law, as applied to property interests in bankruptcy.

Cases that cite this headnote

*328 Appeal from the United States Bankruptcy Court for the Northern District of California, Honorable Stephen J. Johnson, Bankruptcy Judge, Presiding

Attorneys and Law Firms

Jon Webster, The Law Offices of Jon Webster, Concord, argued on behalf of appellant Schmitzel, Inc., dba R & J Jewelry & Loan; David A. Boone, The Law Offices of David A. Boone, San Jose, argued on behalf of appellee Sydney Eileen Sorensen.

Before: FARIS, BRAND, and TAYLOR, Bankruptcy Judges.

OPINION

FARIS, Bankruptcy Judge:

*329 INTRODUCTION

Appellant Schnitzel, Inc., dba R & J Jewelry & Loan (“R & J”), appeals from the bankruptcy court’s ruling prohibiting R & J from disposing of chapter 13¹ debtor Sydney Eileen Sorensen’s pawned jewelry. R & J argues that the bankruptcy court erred because the jewelry was excluded from Ms. Sorensen’s estate by § 541(b)(8), and she could not extend her right to redeem the property through the bankruptcy process. We AFFIRM.

FACTUAL BACKGROUND

R & J is a licensed pawnbroker in the state of California. In March 2016, Ms. Sorensen pledged five pieces of jewelry as collateral for five pawn loans with R & J. Four months later, she obtained replacement loans that had a termination date of November 18, 2016.

Prior to the termination date of the loans, Ms. Sorensen filed for chapter 13 bankruptcy protection. Her schedules identified R & J as a creditor holding claims secured by the pawned jewelry. Her proposed chapter 13 plan listed R & J as a secured creditor and sought to repay the loans and retain the jewelry.

On November 18, 2016, R & J issued a notice of loan termination, providing a ten-day right to redemption required by state law. Ms. Sorensen did not redeem the jewelry during the ten-day period.

Ms. Sorensen filed an amended chapter 13 plan,² which again identified R & J as a secured creditor and proposed to make \$50 monthly payments on each of the five loans. R & J did not oppose plan confirmation.

Meanwhile, counsel for R & J and Ms. Sorensen communicated about the status and characterization of the pawn loans. R & J offered Ms. Sorensen two more extensions of her redemption rights; the final deadline was March 3, 2017.

On March 1, Ms. Sorensen filed an adversary proceeding complaint for injunctive and declaratory relief against R & J. She requested that the court issue an injunction preventing R & J from disposing of the jewelry, which she contended was part of the bankruptcy estate and therefore subject to the automatic stay.

Ms. Sorensen also filed an application for a temporary restraining order (“TRO Motion”) to prevent R & J from disposing of the jewelry. She argued that she satisfied the standard for a temporary restraining order (“TRO”) because she had “every intention to retain the liens and make payment on those liens to redeem possession of her jewelry, [and] she had clearly stated her intentions to retain the liens and redeem the property in her Chapter 13 Plan”

In opposition to the TRO Motion, R & J argued that Ms. Sorensen was unlikely to succeed on the merits because the jewelry was excluded from the bankruptcy estate pursuant to § 541(b)(8). It contended that, under § 541(b)(8)(C) and § 108(b), the redemption period relevant to a pawn loan expires on the later of (1) the loan termination date under state or local law or (2) *330 sixty days from the date of the bankruptcy filing. Under California law, Ms. Sorensen had four months (until November 18, 2016) to redeem her jewelry; R & J then issued the statutorily-required grace notice extending the right of redemption until November 28. It contended that, because Ms. Sorensen did not redeem her property within the statutory period, the jewelry was excluded from the bankruptcy estate under § 541(b)(8), and the automatic stay never applied to the jewelry.

On March 28, 2017, the bankruptcy court confirmed Ms. Sorensen’s amended plan. Later that same day, the bankruptcy court heard Ms. Sorensen’s TRO Motion. In light of the earlier plan confirmation and additional arguments raised by Ms. Sorensen, the bankruptcy court ordered supplemental briefing and continued the hearing.

On March 31, R & J filed a motion to dismiss the adversary complaint (“Motion to Dismiss”) under Civil Rules 12(b)(1) and (b)(6), made applicable in bankruptcy by Rule 7012(b), arguing that the bankruptcy court lacked subject matter jurisdiction over the pawned jewelry because it was excluded from the bankruptcy estate. It repeated that, under § 541(b)(8), the jewelry was not part

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of the bankruptcy estate: due to Ms. Sorensen's and "the Trustee's failure to redeem the property in the statutorily prescribed time limit, the property never entered the bankruptcy estate. If Plaintiff wished to include the pledged items in the estate, Plaintiff was required to redeem them pursuant to Section 541(b)(8)(C) and Section 108(b)." It also argued that Ms. Sorensen failed to state a claim upon which relief could be granted: the "automatic stay does not in any way affect the statutory redemption period of Section 108 and Section 541(b)(8)(C). Plaintiff has not alleged, and cannot allege, that Debtor-Plaintiff or the Trustee attempted to redeem the property within the time prescribed by Section 108."

Following a hearing on the continued TRO Motion and the Motion to Dismiss, the bankruptcy court orally held that (1) R & J's notice of loan termination was likely void for violating the automatic stay; and (2) Ms. Sorensen's confirmed chapter 13 plan—including its treatment of the jewelry—was binding on the parties. It considered the interplay between three factors: state law, bankruptcy law, and the confirmed plan.

First, the court noted that California law allows a four-month loan period that expired on November 18, 2016. At that time, if R & J properly provided statutory notice and a ten-day redemption period to Ms. Sorensen, then, "[p]ursuant to California Finance Code Section 21201, R & J would be vested with all right, title, and interest in the jewelry after the expiration of the ten-day period."

Second, the bankruptcy court considered how Ms. Sorensen's bankruptcy case affected the parties' rights. It stated that, when she filed her petition, her estate included her option to redeem the jewelry. However, under § 541(b)(8), certain tangible property pledged to pawnbrokers is excluded from property of the estate unless the debtor redeems the property within the time allowed under § 108(b). That section provides that the redemption period is the later of sixty days after the petition is filed or the period set by state law. But the bankruptcy court noted that the time period under state law had not expired because the ten-day notice that R & J sent violated the automatic stay:

Here, R & J never sent a proper notice of loan termination. Section 362(a)(6) enjoins any act to collect, [assess], or recover a claim against the debtor that arose before the property of the—the commencement of the case. *331 Nothing in 541(b)(8), which is the section

that talks about ownership[] of these assets[,] creates an exception to the automatic stay. So relief from stay is required before any collection action can begin. And the reference here is 5 Collier on Bankruptcy, at 541—paragraph 541.24.

R & J never moved for relief from stay, which likely would have been granted in view of Section 541(b)(8). And it would have allowed R & J to send the notice required by California law. As everyone knows, actions taken in violation of the stay are void. So it is as if R & J never sent the notice and the ten-day redemption period never began. Accordingly, title to the property was never vested in R & J.

Third, the bankruptcy court considered the effect of Ms. Sorensen's confirmed plan. It stated that the plan controlled the disposition of the jewelry under § 1327(a) and *Espinosa v. United Student Aid Funds, Inc.*, 553 F.3d 1193 (9th Cir. 2008), *aff'd*, 559 U.S. 260, 130 S.Ct. 1367, 176 L.Ed.2d 158 (2010). The court entered an order granting the TRO Motion and denying the Motion to Dismiss ("Order").

R & J filed a timely notice of appeal from the Order and a motion for leave to appeal. The BAP motions panel remanded the case to the bankruptcy court for a determination whether the Order granted a TRO, and is thus interlocutory, or whether the Order granted a preliminary injunction and is immediately reviewable on appeal. The bankruptcy court clarified that, despite language indicative of a TRO, the Order constituted a preliminary injunction. The bankruptcy court also supplemented the reasoning behind the Order, stating that Ms. Sorensen sought to retain ownership of the jewelry through a confirmed plan that "treated the Property as collateral for a secured claim held by R & J and called for payment of that secured claim over time. R & J did not object to any of Plaintiff's Chapter 13 plans.... The Court continues to believe the confirmed Chapter 13 plan controls the Property."

JURISDICTION

The bankruptcy court had jurisdiction pursuant to 28 U.S.C. §§ 1334 and 157(b)(1) and (b)(2)(B). We have jurisdiction under 28 U.S.C. § 158.

ISSUE

Whether the bankruptcy court erred in denying R & J's Motion to Dismiss and granting Ms. Sorensen a preliminary injunction preventing R & J from disposing of the jewelry.

STANDARD OF REVIEW

[1] [2] The issues before the Panel are purely questions of law, which we review de novo. Great Lakes Higher Educ. Corp. v. Pardee (In re Pardee), 218 B.R. 916, 919 (9th Cir. BAP 1998), aff'd, 193 F.3d 1083 (9th Cir. 1999) (“We review conclusions of law, including the bankruptcy court's interpretation of the Bankruptcy Code, de novo.”). De novo review is independent and gives no deference to the trial court's conclusion. Roth v. Educ. Credit Mgmt. Corp. (In re Roth), 490 B.R. 908, 915 (9th Cir. BAP 2013).

DISCUSSION

A. R & J did not validly terminate Ms. Sorensen's right to redeem the jewelry.

The overarching question before the Panel is whether the pawned jewelry is still property of the bankruptcy estate. This appears to be a question of first *332 impression in this circuit. We agree with the bankruptcy court's reasoning.

1. When Ms. Sorensen filed for bankruptcy protection, her interest in the jewelry became part of the bankruptcy estate.

We must first decide how Ms. Sorensen's bankruptcy petition affected the parties' respective interests in the jewelry.

[3] [4] Under § 541(a), an estate is created at the filing of a bankruptcy petition that contains, subject to certain exceptions, “all legal or equitable interests of the debtor in property as of the commencement of the case.” § 541(a) (1). “[A] pre-foreclosure right to redeem is a property right under section 541” Harsh Inv. Corp. v. Bialac (In re Bialac), 712 F.2d 426, 431 (9th Cir. 1983). This includes rights that a debtor retains in her pawned property. See Title Max v. Northington (In re Northington), 876 F.3d

1302, 1309–10 (11th Cir. 2017) (agreeing that the debtor “retained property interests in the [pawned property] that became ‘property of the estate’ under 11 U.S.C. § 541. In particular, the parties agree that the car, which remained in [the debtor's] possession, as well as the associated right to redeem it—which at that time had not yet expired—entered the estate with the filing of his petition”).

[5] In the present case, when Ms. Sorensen filed her bankruptcy petition, all of her interests in her jewelry at that time became part of her bankruptcy estate. See Cty. of Imperial Treasurer–Tax Collector v. Stadtmueller (In re RW Meridian LLC), 564 B.R. 21, 28 (9th Cir. BAP 2017) (“The nature and extent of the debtor's interests in property must be determined by nonbankruptcy law.”); Cal. Fin. Code. § 21201(a), (f). The bankruptcy court correctly held that her estate included her right to redeem her jewelry.

2. Under California law, § 541(b)(8) does not automatically exclude pawned property from the bankruptcy estate without notice to the pawnor.

R & J argues that the plain language of § 541(b)(8) automatically exempts the pawned property from the bankruptcy estate. That subsection provides that:

(b) Property of the estate does not include—

...

(8) subject to subchapter III of chapter 5, any interest of the debtor in property where the debtor pledged or sold tangible personal property (other than securities or written or printed evidences of indebtedness or title) as collateral for a loan or advance of money given by a person licensed under law to make such loans or advances, where—

(A) the tangible personal property is in the possession of the pledgee or transferee;

(B) the debtor has no obligation to repay the money, redeem the collateral, or buy back the property at a stipulated price; and

(C) neither the debtor nor the trustee have exercised any right to redeem provided under the contract or State law, in a timely manner as provided under State law and section 108(b)[.]

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§ 541(b)(8). The parties do not dispute that subsections (A) and (B) are satisfied; only (C) is at issue in this appeal. We thus look to § 108(b) and the relevant state law.

Section 108(b) provides:

(b) Except as provided in subsection (a) of this section, if applicable nonbankruptcy law, an order entered in a nonbankruptcy proceeding, or an agreement fixes a period within which the debtor or *333 an individual protected under section 1201 or 1301 of this title may file any pleading, demand, notice, or proof of claim or loss, cure a default, or perform any other similar act, and such period has not expired before the date of the filing of the petition, the trustee may only file, cure, or perform, as the case may be, before the later of—

- (1) the end of such period, including any suspension of such period occurring on or after the commencement of the case; or
- (2) 60 days after the order for relief.

§ 108(b).

In this case, California law provides the longer period for redemption of pawned property. California Financial Code section 21201 provides that, if a pawned item is not redeemed before the end of the loan period, the pawnbroker must give notice of the loan termination and provide a ten-day redemption period:

(d) If any pledged article is not redeemed during the loan period as provided herein, and the pledgor and pawnbroker do not mutually agree in writing to extend the loan period, **the pawnbroker shall notify the pledgor within one month after expiration of the loan period.** If the pawnbroker fails to notify the pledgor within one month after the expiration of the loan period, the pawnbroker shall not charge interest from the day after the expiration of the one-month period. **The pawnbroker shall notify the pledgor at his or her last known mailing or electronic address of the termination of the loan period,** by

a means for which verification of mailing or, at the sole option of the pledgor, electronic transmission of the notification can be provided by the pawnbroker, **and extending the right of redemption, during posted business hours, for a period of 10 days from date of mailing or electronic transmission of that notice.**

Cal. Fin. Code § 21201(d) (emphases added). California law specifies that the pawnbroker only becomes vested with full ownership of the property after the ten-day period expires:

(f) If any pledged article is not redeemed within the 10-day notice period, **the pawnbroker shall become vested with all right, title, and interest of the pledgor,** or his or her assigns, **to the pledged article,** to hold and dispose of as his or her own property.

Cal. Fin. Code § 21201(f) (emphases added); see Cal. Fin. Code § 21002(b) (“ ‘Vested property’ is property the title to which has been transferred from the pledgor to the pawnbroker pursuant to Section 21201. Vested property is not pledged property.”).

[6] In other words, the right to redeem pawned property under California law does not expire until ten days after the pawnbroker gives proper notice to the pledgor.

In the present case, Ms. Sorensen filed for bankruptcy protection on August 9, 2016. The replacement loans terminated on November 18, 2016. Pursuant to California Financial Code section 21201(d), R & J then issued the notice of the ten-day right of redemption. Ms. Sorensen did not redeem the jewelry during the ten-day period.

R & J contends that, because Ms. Sorensen failed to redeem the jewelry during the ten-day period, the pawned jewelry was excluded from the bankruptcy estate under § 541(b)(8)(C). But as we explain in the next section, the ten-day notice was void because R & J issued it in violation of the automatic stay.

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***334 3. The statutory redemption notice was void because R & J failed to seek relief from stay.**

[7] The automatic stay prevents a creditor from taking certain actions against property of the bankruptcy estate. In relevant part, § 362 provides:

(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title ... operates as a stay, applicable to all entities, of—

...

(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;

...

(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;

(6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title[.]

§ 362(a)(3), (5), (6).

[8] R & J's issuance of the ten-day notice was an act "to exercise control over property of the estate[.]"³ to "enforce a lien [that] ... secures a claim[.]" and "to collect, assess, or recover a claim against the debtor[.]"⁴ It thus violated § 362(a). "Actions taken in violation of the automatic stay are void." *In re RW Meridian LLC*, 564 B.R. at 28. Because the ten-day notice was void ab initio, R & J did not satisfy the notice requirement in California Financial Code section 21201(d).

Accordingly, the ten-day redemption period never began to run under subsection (d), Ms. Sorensen's redemption right was never extinguished, R & J never took title to the jewelry under subsection (f), and § 541(b)(8) did not remove the jewelry from the estate.

This case is distinguishable from cases decided in other jurisdictions with different state statutes. For example, in *Northington*, the Eleventh Circuit held that, under state law automatically vesting title in the pawnbroker at the expiration of the redemption period, the pawned

property "dropped out" of the estate pursuant to § 541(b)(8). 876 F.3d at 1306. In that case, the debtor failed to redeem prepetition pawned property, and the pawnbroker sought relief from stay and argued that the property was excluded from the estate pursuant to § 541(b)(8). The Eleventh Circuit started with the proposition that the debtor's interest in the pawned property became property of the estate when he filed his bankruptcy petition. *Id.* at 1309. But it stated that "an estate is not necessarily 'frozen in time,' but rather can, in certain circumstances, expand or contract in accordance with the operation of underlying state-law property rules." *Id.* at 1314. The court held that, by operation of state law, the pawned property "dropped out" of the estate:

***335** Properly understood, the Bankruptcy Code takes an estate's constituent property interests as it finds them. If an asset is by its state-law nature static, then it remains so in the bankruptcy estate. **If, by contrast—as is often the case—state law imbues an estate asset with a sort of internal dynamism, then that characteristic will follow the asset into the estate...**

But increase will not always be the result—sometimes the dynamism will reduce (or even eliminate) an asset's value. Think, for instance, about a debtor whose bankruptcy estate includes an option contract. If the debtor fails to exercise the option in accordance with state law, then the right to buy disappears. This case reflects the same basic phenomenon. Under Georgia's pawn statute, following his loan's maturity date, Wilber had a conditional right to possess the Charger as well as a right to redeem it during the statutory period. But after the expiration of the prescribed period, Wilber had no rights in the car, possessory or otherwise. Rather, his rights had been "automatically ... extinguished" and "automatically forfeited to [TitleMax]."

Id. at 1314–15 (emphasis added).

[9] We agree with the *Northington* court's analysis,⁵ but the result here is different because Georgia's pawnshop law differs from California's. In Georgia, following a statutory redemption period, the interest in the pawned property is **automatically** vested in the pawnbroker; the pawnbroker does not need to take any action. Ga. Code Ann. § 44-14-403(b)(3) ("Pledged goods not redeemed within the grace period shall be automatically forfeited to the pawnbroker by operation of this Code section, and any ownership interest of the pledgor or seller shall

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automatically be extinguished as regards the pledged item.”). In contrast, California Financial Code section 21201(d) required R & J to send notice to Ms. Sorensen before it obtained legal title to the jewelry. That notice, as discussed above, was void because it violated the automatic stay.⁶

*336 [10] [11] [12] R & J points out that this analysis treats California pawnshops differently from pawnshops in other states that do not require the pawnbroker to give notice of termination of the redemption right.⁷ R & J argues that this result is unfair and inappropriate. We agree that application of state law in this context produces different results in different states, but this is neither wrong nor even unusual. “Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding.” *Butner v. United States*, 440 U.S. 48, 55, 99 S.Ct. 914, 59 L.Ed.2d 136 (1979). “[U]ndefined considerations of equity provide no basis for adoption of a uniform federal rule” displacing state property law. *Id.* at 56, 99 S.Ct. 914.

Accordingly, Ms. Sorensen's redemption rights did not terminate because R & J did not obtain relief from the

automatic stay before giving the ten-day notice. The bankruptcy court did not err.

B. We need not decide whether the plan has preclusive effect.

The bankruptcy court alternatively held that R & J was bound by the terms of the confirmed plan, which treated R & J as a secured creditor and provided for redemption of the pawned jewelry. We do not reach this issue on appeal because we are affirming the decision on another, independently sufficient ground.

CONCLUSION

The bankruptcy court did not err when it denied the Motion to Dismiss and granted the TRO Motion. We AFFIRM.

All Citations

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Footnotes

- 1 Unless specified otherwise, all chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101–1532, all “Rule” references are to the Federal Rules of Bankruptcy Procedure, and all “Civil Rule” references are to the Federal Rules of Civil Procedure.
- 2 The chapter 13 trustee raised several objections to the original plan, including whether R & J had properly received notice of the plan. The amended plan addressed the trustee's concerns, including notice to R & J.
- 3 R & J already had “control” of the jewelry in the sense of physical possession. The notice (if effective) would have given it complete control by permitting it to sell the jewelry and keep the proceeds. Cal. Fin. Code § 21201(d), (f). Therefore, the notice violated § 362(a)(3).
- 4 R & J's loans were nonrecourse, meaning that if the proceeds of sale of the jewelry were insufficient to repay the loans in full, R & J had no recourse against Ms. Sorensen for the deficiency. This is immaterial, because § 102(2) provides that “ ‘claim against the debtor’ includes claim against property of the debtor” In other words, nonrecourse claims are “claims” for bankruptcy purposes.
- 5 In particular, we agree that pawned property “drops out” of the estate if the redemption right is not timely exercised. R & J argues that pawned property does not enter the estate at all unless and until the debtor or trustee timely exercises the redemption right. The *Northington* court's view is more consistent with the language and structure of § 541(b)(8). That section expressly permits the debtor or the trustee to redeem the property. If the redemption right were not property of the estate, the trustee could not exercise it.
- 6 This is not to say that § 362(a), rather than § 108(b), controls the redemption period. We agree with other courts in our circuit that have held that § 362(a) does not toll redemption periods. *See, e.g., In re York*, No. 16-01964-FPC13, 2016 WL 6157432, at *3 (Bankr. E.D. Wash. Oct. 21, 2016) (“This court finds more persuasive courts finding that § 362(a) does not toll the running of the time period for redemption, and that the only available extension of time for such periods is

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the 60 days provided for in § 108(b)..."); In re Mosher, No. 07-60007-13, 2007 WL 1487399, at *7 (Bankr. D. Mont. May 17, 2007) ("Debtors' argument that their redemption period was tolled by the automatic stay is contradicted by the plain language of § 541(b)(8)(C) which specifically invokes § 108(b) for determining whether a debtor or trustee has exercised any right to redeem in a timely manner."); see also In re Northington, 876 F.3d at 1313 (rejecting the notion that "the automatic-stay provision applies to toll an as-yet-unexpired state-law redemption period indefinitely, thereby preventing the period from lapsing and (in effect) keeping pawned assets in the estate"). Section 362(a) is still relevant, however, in cases like this one, where a redemption period does not start running until the creditor gives a notice, and the automatic stay prevents the creditor from giving that notice.

- 7 Pawnshop laws vary widely from state to state. See, e.g., Del. Code Ann. § 2307(b) (prohibiting the pawn of prosthetic limbs); Clark County, Nev. Ord. 6.24.150 (stating that it is illegal to accept pawned goods from someone known to be a "habitual drunkard" or "an insane person"). Most state laws provide that pawned property "automatically" vests in the pawnbroker when the redemption period expires, but a minority (including California) require the pawnbroker to give notice to the pawnor before the pawnbroker acquires full title to the property or sells the property. Thirteen jurisdictions (California, Kentucky, Massachusetts, New Jersey, New Mexico, New York, Ohio, Oregon, Pennsylvania, South Carolina, Wisconsin, District of Columbia, and Guam) require notice. See, e.g., Ohio Rev. Code Ann. § 4727.11 ("the licensee shall notify the pledgor ... [that] the pledged property shall be forfeited to the licensee"); Or. Rev. Stat. § 726.400(3) ("the pawnbroker may not deem a pledge to be forfeited until: (a) The pawnbroker notifies the pledgor that the pledge is at risk of forfeiture ..."); Wis. Stat. Ann. § 138.10 ("A pawnbroker shall not sell any pledge unless due notice of such contemplated sale has been forwarded to the pledgor"). A few other jurisdictions require that the pawnshop give public notice of the upcoming sale. See 19 R.I. Gen. Laws Ann. § 19-26-10; V.I. Code Ann. tit. 9 § 228. Still others have no pawnshop laws or leave the regulation up to local government. But the majority of jurisdictions do not require further notice or simply do not speak to any further notice requirement prior to the pawnshop acquiring full interest in the pawned property. Our holding here only applies where applicable nonbankruptcy law requires the pawnbroker to give notice in order to terminate the pawnor's rights in the property.

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Bankruptcy Law Letter

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THE AUTOMATIC STAY UNDER § 362(a)(3)— ONE MORE TIME

By Eugene R. Wedoff

One of most significant issues in consumer bankruptcy currently in dispute is whether § 362(a)(3) of the Bankruptcy Code requires creditors to return to a debtor any collateral—most commonly automobiles—that they repossessed before the bankruptcy filing. In 1984, subsection (a)(3) was amended. Before the amendment, it only applied the automatic stay to “any act to obtain possession of property of the estate or of property from the estate,” and so only prevented creditors from seizing a debtor’s property during the bankruptcy case. The 1984 amendment expanded the provision by extending the stay to apply to any act “to exercise control over property of the estate.” Debtors used this amendment to argue that after the filing of a bankruptcy case, § 362(a)(3) not only prevented creditors from seizing the debtor’s property, but also prohibited them from continuing to hold whatever property they had seized earlier, since by retaining what was now estate property, they would be exercising control over it.

The initial response to this argument was a string of circuit court and BAP decisions agreeing with the debtors, establishing a majority rule that creditors were indeed stayed by § 362(a)(3) from continuing to hold estate property repossessed before a debtor’s bankruptcy filing and that they were required to return that property to a debtor otherwise entitled to it.¹ This string was unbroken until last year,² when the Tenth Circuit issued *WD Equipment v. Cowen*, holding § 362(a)(3) imposes no duty on creditors to return repossessed collateral.³

One notable aspect of the new circuit split is that *Cowen*’s rejection of the majority rule cites a *Bankruptcy Law Letter* written by Professor Ralph Brubaker in 2013.⁴ With the issuance of *Cowen*, and a set of related questions about the automatic stay, another look at the issues raised in that *Law Letter* may be timely.

THE MAJORITY RATIONALE

The majority interpretation of § 362(a)(3) is based on plain language. The Second Circuit’s decision made the point this way:

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[S]ection 362 forbids any act to . . . “exercise control” over the property of the estate. We need consult only an ordinary dictionary to confirm that a typical definition of “control” is: “To exercise authority over; direct; command.” Webster’s New World College Dictionary (4th ed. 2002). In light of that definition, we see no way to avoid the conclusion that, by keeping custody of the vehicle and refusing [the debtor] access to or use of it, [the secured creditor] was “exercising control” over the object in which the estate’s equitable interest lay, and its retention of the vehicle violated the stay.⁵

The decision found additional linguistic support in the nature of the 1984 amendment, pointing out that “obtaining possession” of estate property held by the debtor had already been stayed, so that

“exercising control” had to mean something more. “This significant textual enlargement is consonant with our understanding . . . that Congress intended to prevent creditors from retaining property of the debtor . . . without regard to what party was in possession of the property in question when the petition was filed.”⁶

THE MINORITY RATIONALE

The 2013 *Law Letter* is probably the most complete statement challenging the majority interpretation of § 362(a)(3).⁷ The *Law Letter* sets out four grounds for questioning the majority interpretation. Each of these grounds, however, can itself be questioned.

1. Upholding established law

The *Law Letter*’s initial argument is based on the Supreme Court’s *Dewsnup* rationale: that an established principle of bankruptcy law should not be interpreted as changed by an amendment unless the change is set out unambiguously or supported by legislative history.⁸ This approach to statutory construction has been widely criticized, as even the Supreme Court has noted.⁹ But applying the approach here is problematic in any event, since it is difficult to see the bankruptcy principle that is contradicted by interrupting a creditor’s exclusive possession of estate property. The *Letter* suggests that creditors were only required to return collateral to debtors after a court determined that their interests would be adequately protected: “adequate protection before turnover.”¹⁰ But under the Bankruptcy Code, adequate protection was not automatically required. It always had to be requested.¹¹

Before the 1984 expansion of § 362(a)(3), if a creditor was unwilling to return collateral, the debtor would have to seek a court order requiring turnover under § 542(a), and in response the creditor could request adequate protection under § 363(e). Only if the creditor made that request could it be said that adequate protection was a prerequisite for turnover.¹² The 1984 amendment, in prohibiting a creditor from retaining collateral sought by a debtor, did not change the secured creditor’s right to adequate protection under § 363(e), it only changed the party with possession of the prop-

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erty during the time that the court considered a creditor's request for protection.

That change can be seen as consistent with the general operation of the automatic stay. Before the 1984 amendment, the stay took away a creditor's nonbankruptcy right to repossess collateral when the debtor was in default under a secured loan; the debtor was allowed to keep collateral until the court determined, in ruling on a creditor's motion for relief from the stay, that there was a lack of adequate protection. The amendment resulted in the same status being applied to property that was repossessed before the bankruptcy. Rather than changing a fundamental bankruptcy policy, the amendment can be seen as extending the basic policy underlying the stay: that the debtor should be able to use all estate property until the creditor requests relief.

The majority decisions reflect this understanding, as set out in the Seventh Circuit's *Thompson* decision:

The primary goal of reorganization bankruptcy is to group all of the debtor's property together in his estate such that he may rehabilitate his credit and pay off his debts; this necessarily extends to all property, even property lawfully seized prepetition. See *Whiting Pools, Inc.*, 462 U.S. at 203-04, 103 S.Ct. 2309; see also *In re Yates*, 332 B.R. 1, 5 (10th Cir. BAP 2005) ("As a practical matter, there is little difference between a creditor who obtains property of the estate before bankruptcy is filed, or after bankruptcy is filed. The ultimate result is the same—the estate will be deprived of possession of that property. This is precisely the result § 362 seeks to avoid."). An asset actively used by a debtor serves a greater purpose to both the debtor and his creditors than an asset sitting idle on a creditor's lot.¹³

2. The meaning of an "act to exercise control"

The *Law Letter* next suggests that the phrase "acts to exercise control over estate property" is in fact ambiguous—"extremely vague"—and cites in support the *Inslaw* decision of the D.C. Circuit.¹⁴ But the ambiguity addressed by *Inslaw* was whether, by refusing to pay damages on a claim asserted by the debtor, a creditor was engaging in an exercise of control.¹⁵ *Inslaw* found this application of § 362(a)(3) unworkable.¹⁶ But this is not an indication of a difficulty in understanding the

meaning of exercising control over property; rather, the question was the nature of the property involved. An estate's cause of action is property of the estate; the recovery that a debtor hopes to obtain from the cause of action is not estate property. In *Citizens Bank v. Strumpf*, the Supreme Court made exactly this distinction in holding that a bank's temporary freeze on a depositor's account did not violate § 362(a)(3). The provision might have been violated, the Court said, if the bank had "exercised dominion over property" as it would have "if a bank account consisted of money belonging to the depositor and held by the bank."¹⁷

In fact, however, [a bank account] consists of nothing more or less than a promise to pay, from the bank to the depositor, and [the bank's] temporary refusal to pay was neither a taking of possession of [the debtor's] property nor an exercising of control over it, but merely a refusal to perform its promise.¹⁸

Inslaw, then, gives no basis for finding that § 362(a)(3) is ambiguous.

But even if there were some difficulty in measuring the full extent of exercising control over estate property, the question would remain: why is a creditor holding exclusive possession of estate property not exercising control over it? The *Law Letter* answers this question by quoting dicta in *Inslaw*: "The automatic stay, as its name suggests, serves as a restraint only on acts to gain possession or control over property of the estate," and suggests that § 362(a)(3) cannot apply if "a creditor does nothing and simply retains possession of property that the creditor already has in its possession."¹⁹ The difficulty with this argument is apparent from the *Inslaw* quotation, which speaks of "gaining" rather than "exercising" control. While "gain" refers to a past achievement ("[t]o come into possession or use of; acquire"), "exercise,"-the statutory term-refers to ongoing activity ("[t]o put into play or operation, employ").²⁰ The plain meaning of exercising control in § 362(a)(3) applies to continuing exclusive possession of collateral.

The Tenth Circuit's *Cowen* decision not only accepts the limitation of § 362(a)(3) suggested in the *Law Letter* but adds another argument about the provision's meaning, asserting that because the word "act" means "doing something," § 362(c)(2) "stays entities from doing something to obtain pos-

session of or to exercise control over the estate's property" rather than "passively holding onto an asset," as the Seventh Circuit stated in *Thompson*.²¹ But, of course, the creditors in each of the majority decisions did "do something"—they prevented the debtors from obtaining access to the collateral. Although each creditor's action was not new, it was an ongoing, continuing exercise of control, and so proscribed by the statutory language.

Moreover, if exercising control over estate property did not include maintaining exclusive possession of the property, there would be the question of what it does include. It cannot mean selling the property or otherwise using it to reduce the creditor's claim, since § 362(a)(6) separately stays any act "to collect, assess, or recover a claim against the debtor." The *Law Letter* suggests that if the nondebtor party to an executory contract terminates the contract of the estate, it will be exercising control over estate property, and cites a Ninth Circuit decision, *In re Computer Communications*, in support of that interpretation.²² However, *Computer Communications* held that terminating the contract was an "act to obtain possession of property of the estate," not an act to exercise control.²³

Finally, the *Law Letter* suggests that if someone not in possession of estate assets files a lawsuit that belongs to the estate, the filing could be seen as exercising control over an estate asset. Again, though, this is more likely to be seen as obtaining possession of the asset. And even if one or more of these hypothetical applications of exercising control were reasonable, it is difficult to imagine that they were a significant enough problem in 1984 that Congress would specially legislate to address them. The common meaning of exercising control over a piece of property—holding it to the exclusion of others—is not only the plain meaning of the amendment but is the only meaning addressing an issue significant enough to prompt legislation.

3. The meaning of "property of the estate"

The *Law Letter* continues its statutory construction by turning to the meaning of "property of the estate." It cites an article by Professor Thomas Plank arguing that when the Bankruptcy Code uses the term "property of the estate," it does not mean

"property" in the ordinary sense—individual items or pieces of property—but rather the particular property interests that the debtor holds at the time the bankruptcy case is filed.²⁴ With this understanding, the *Law Letter* reasons (1) that the "property of the estate"—over which a creditor may not exercise control under § 362(a)(3)—does not include the right of possession, since the debtor did not have that right at the time the case was filed and (2) that to bring that right into the estate, the debtor would have to obtain turnover under § 542(a).²⁵

The difficulty with this argument is in its premise. Apart from the bankruptcy court decision in *Hall*, which cites the *Law Letter* extensively,²⁶ no judicial decision appears to accept Professor Plank's understanding of "property of the estate," and this understanding is inconsistent with the manner in which the Bankruptcy Code uses the term. One example of the difficulty is § 363(f), which allows the sale of property under § 363(b) and (c), free and clear of "any interest in such property of an entity other than the estate" if one of a set of conditions is met, including that the interest of the other party is in bona fide dispute.²⁷ Subsections (b) and (c) only provide for sales of "property of the estate," and so, at least in § 363, the Code uses that term to mean the entire property to which the debtor claims title, even if another party is in possession at the time of filing or holds a bona fide claim of interest adverse to the debtor. With this understanding of property of the estate, the debtor's entire property is similarly subject to the protection of § 362(a)(3).

4. The balance of harms

Finally, the *Law Letter* compares the different costs imposed on debtors and creditors under the conflicting interpretations of § 362(a)(3).²⁸ For creditors, it says, returning collateral on demand by a debtor, as required by the majority interpretation, will likely result in—

- (a) the complete loss of any possessory lien,
- (b) the risk of full loss of value in uninsured collateral through theft or accidental damage, and
- (c) the deprivation of compensation for the value

lost through depreciation or the expense of seeking an order granting adequate protection.

These costs would be removed under the minority interpretation because it requires the debtor to file a turnover proceeding to regain possession of collateral, and, if demanded by the creditor, the debtor would have to prove adequate protection before turnover was granted.

For debtors, the *Law Letter* acknowledges the cost imposed by the minority interpretation: they will be unable to use a vehicle (or other collateral) that may be needed for work, schooling, and health care until the court rules on turnover, and the period of deprivation may be a long one—the time needed to file and obtain emergency relief in the adversary proceeding mandated by Fed. R. Bankr. P. 7001(1) for turnover under § 522(a). The majority interpretation of § 352(a)(3), by allowing debtors to obtain immediate return of the collateral without a turnover proceeding, removes this cost.

Although this balance shows harm to parties under both interpretations, the *Law Letter* suggests that the greater harm is imposed by the majority interpretation:

A well-advised debtor . . . would *never* offer *any* adequate protection in demanding turnover and would *always* put the secured creditor to the burden of moving for stay relief/adequate protection before the bankruptcy court, or use the prospective burden of doing so as leverage in adequate protection negotiations, but only *after* securing turnover *without* providing *any* adequate protection, which (as we've seen) holds the (not unrealistic) prospect of entirely eviscerating the secured creditor's right to receive adequate protection.²⁹

Accordingly—and consistent with its view of the difficulties it sees with the majority interpretation—the only recommendation that *Law Letter* makes for improving the law on return of collateral is a rule change that would allow debtors prompt access to turnover.³⁰

The balance set out by the *Law Letter*, however, may need adjustment. Although its description of harm to debtors is accurate, its view of the harm to creditors appears to be overstated in each of the respects it discusses.

(a) *Possessory liens are not eliminated by § 362(a)(3).*

Possessory liens generally terminate when the creditor holding the lien loses possession of the collateral.³¹ For this reason the *Law Letter* sees the majority interpretation of § 362(a)(3)—requiring creditors to give up the collateral they possess—as resulting in the loss of any possessory lien.³² It criticizes the Eighth Circuit BAP's opinion in *In re WEB2B Payment Solutions, Inc.*, which deals with a possessory lien, for bending the majority rule by suggesting that a possessory lien holder could withhold surrender of the collateral “until the bankruptcy court is able to make a determination as to whether, and to what extent, the creditor is entitled to adequate protection.”³³ That suggestion, the *Law Letter* states, cannot be reconciled with the majority decisions, including the Eighth Circuit's opinion in *Knaus*, which allow for no exceptions to return of collateral under § 362(a)(3).³⁴

But there are two problems with the idea that § 362(a)(3) would cause the loss of a possessory lien. The first is that, under the common law, a possessory lien only terminates when the creditor loses possession if the creditor gives up possession voluntarily. The Restatement of Security explains this in a comment:

The lien is a legal interest dependent upon possession. Where the lienor voluntarily gives up the possession, his lien, at least so far as it is a legal interest, is gone. The lienor . . . does not lose his legal interest if he is deprived without his consent of his possession either by the bailor [owner] or a third person. If the lienor's surrender of possession is voluntary but obtained by fraud, the lienor can recover the chattel unless third persons in the meantime have acquired interests. Where possession is taken without the consent of the lienor, even a bona fide purchaser is subject to the lien, provided the chattel is non-negotiable.³⁵

Accordingly, a retention lien continues to apply to collateral even if a legal obligation required the creditor to return it.³⁶

The *WEB2B* decision reflects this rule. The collateral in the case was cash of a Chapter 7 debtor that a creditor had received subject to a possessory lien. The trustee requested that the creditor turnover all of the cash. Under an agreement with the

trustee, and without any proceeding in the bankruptcy court, the creditor retained what it considered a sufficient amount of cash to satisfy its claims against the debtor and gave the balance to the trustee. Later, the retained collateral proved insufficient to cover these claims, and the creditor argued that the transferred collateral had been given to the trustee under compulsion, so that the possessory lien should continue to apply to it, citing the Supreme Court's *Whiting Pools* decision under § 542(a) to argue that the Bankruptcy Court should have determined what adequate protection would apply to the continuing lien. The BAP rejected this argument, holding that the transfer was voluntary, so that the possessory lien terminated when the collateral was transferred.³⁷ The BAP did suggest that the creditor could have requested a court determination of adequate protection before turning over the property, but this was plainly dicta. If payment to the trustee had actually been compelled, rather than voluntary, so that the possessory lien continued in place, the creditor would have been able to seek a ruling on adequate protection after the transfer. The BAP, however, had no reason to consider the effect of an involuntary transfer on possessory liens, whether made pursuant to § 362(a)(3) or any other provision of law; indeed, § 362(a)(3) is not mentioned in the decision.

The second problem with the *Law Letter's* treatment of possessory liens is that if nonbankruptcy law did result in termination of the lien after an involuntary transfer, an exception to the automatic stay—§ 362(b)(3)—would prevent § 362(a)(3) from going into effect, and the creditor would not be required to give up possession. This exception to the stay was explained in a decision of the Ninth Circuit BAP, *Hayden v. Wells*.³⁸ In that case, Chapter 13 debtors relied on § 362(a)(3) to obtain the return of their vehicle from a company with a possessory lien for its services in towing and storing the automobile. The BAP held that the § 363(b) stay exception required denial of the debtors' request, and explained the exception's effect:

[I]f state law provides that a creditor's security interest is superior to the rights of any entity obtaining its interest in the property prior to the date the creditor takes action to maintain or continue perfection

of its lien, the creditor's post-petition act to maintain or continue perfection of the lien does not violate the automatic stay. *Boggan v. Hoff Ford, Inc. (In re Boggan)*, 251 B.R. 95, 99 (9th Cir. BAP 2000) (holding that automobile dealership that retained possession of debtor's automobile as security for repayment of unpaid repair bill pursuant to Idaho law did not violate automatic stay).³⁹

A recent decision by the Bankruptcy Court for the Northern District of Illinois, *In re Avila*, cited *Hayden* in holding that § 362(b)(3) permits the City of Chicago to retain vehicles impounded for traffic violations because return of the vehicle under § 362(a)(3) would terminate the City's possessory lien for the impounding; the Seventh Circuit's *Thompson* decision was held inapplicable because of the § 363(b)(3) stay exception.⁴⁰ No appeal was taken from this order, but other judges in the Northern District of Illinois have disagreed with its holding, one ruling that the municipal ordinance granting the City's lien exceeds the City's police power,⁴¹ and the other ruling that § 363(b)(3) "applies only to 'acts' taken by creditors" and "passive possession of a debtor's property for the purposes of maintaining possession does not constitute an 'act.'"⁴² These decisions have been appealed, and the appeals are pending in the district court.

But the *Hayden* and *Avila* decisions can be questioned on grounds other than those set out in the Chicago appeals. If applicable nonbankruptcy would not result in termination of a possessory lien after the lienholder was compelled to surrender possession, then there would be no need for the lienholder to retain possession in order to maintain or continue perfection of its lien, and the stay exception would not apply. The possessory lien would be given no different treatment than a purchase money lien. But in determining the effect of § 362(a)(2) on possessory liens, it is plain that regardless of whether the lien remains effective under the common law or under the § 362(b)(3) stay exception, the creditor does not lose its lien.

(b) *Transfers of uninsured vehicles may be prevented by annulment of the automatic stay.*

It is also unlikely that § 362(a)(3) will require creditors to return uninsured vehicles to debtors. In addition to allowing a creditor to seek termination or modification of the automatic stay for a lack

of adequate protection, § 362(d)(1) allows the stay to be annulled. Annulment has been consistently understood as retroactively terminating the stay, and so validating whatever action would otherwise have been a stay violation.⁴³ Although there is a lack of consistency in the language used by the courts discussing the grounds for stay annulment, there is general agreement that a balancing of the interests of the parties is required.⁴⁴ Among the factors that have generally been considered in this balancing are the good faith of the debtor in seeking enforcement of the stay and the harm to the creditor if the stay is enforced.⁴⁵ Courts may also grant annulment “if grounds for relief from the stay existed and a motion, if filed, would likely have been granted prior to the automatic stay violation [and] if failure to grant retroactive relief would cause unnecessary expense to the creditor.”⁴⁶

Under this precedent, if a creditor that had repossessed an uninsured car was faced with a demand by a Chapter 13 debtor to return the car under § 362(a)(2), the creditor could refuse until the debtor obtained insurance, and if the debtor sought to hold the creditor in violation of the automatic stay, the creditor could file a motion for annulment of the stay and almost certainly prevail.⁴⁷ By attempting to obtain use of a vehicle without insurance, the debtor would be acting in bad faith; if the creditor had been able to present a motion for stay relief, it would have been granted; and the harm to the creditor if the stay were enforced would be the potential loss of the full value of its security interest.⁴⁸

Of course, the creditor would still have to incur the expense of seeking stay annulment if the debtor charged the creditor with a stay violation. But since the courts would routinely grant such annulment motions, the debtor would have little reason to seek enforcement of § 362(a)(3); the cost of drafting and presenting the motion for stay enforcement would be wasted.

(c) *Chapter 13 provides substantial protection against declines in the value of collateral, without the need for creditor action.*

The remaining harm that the *Law Letter* sees imposed by the majority interpretation of § 362(a)(3) is the loss of value in a repossessed ve-

hicle that would occur while the debtor uses the vehicle without having to provide adequate protection that could have been ordered by the court, without a motion by the creditor, if the debtor had been required to seek a turnover under § 524(a). In Chapter 13, however, adequate protection is automatically required of any debtor holding collateral from the outset of the case; no creditor action is required. Section 1326(a)(1)(C) requires adequate protection payments to the secured creditor, unless the court orders otherwise, commencing no later than 30 days after the case is filed. It is unlikely that if debtors were required to file adversaries seeking turnover, the courts would order more in adequate protection than such payments. And to comply with the payment requirement would be grounds for stay relief and even dismissal of the case.⁴⁹

All of this suggests that the balance of harms resulting from the two interpretations of § 362(a)(3) is different from that set out in the 2013 *Law Letter*. While the minority interpretation does indeed impose substantial costs on debtors unable to use their vehicles, the majority interpretation does not impose costs on creditors to the extent that the *Law Letter* suggests.

POTENTIAL RESOLUTION OF THE CIRCUIT CONFLICT

Because the *Cowen* case was remanded for further proceedings (which could involve the imposition of sanctions on the creditors) there is no possibility, at least immediately, of Supreme Court review. The *Cowen* interpretation of § 362(a), however, might be subject to fuller consideration by the Tenth Circuit itself. In a Chapter 7 case in the District of Kansas, *Davis v. Tyson Prepared Foods*, an issue arose that the bankruptcy judge found similar to the question in *Cowen*.⁵⁰ In *Davis*, a worker was injured on the job and sought workers compensation benefits, but after filing a bankruptcy case, also filed a state court complaint against the company that supplied the item that caused her injury and obtained a judgment against that supplier. Under Kansas law, the employer was subrogated to the worker's right to recover from the supplier to the extent of the employer's work-

ers compensation payments to her, and a lien supporting this subrogation attaches to the judgment against the supplier.⁵¹

Does the attachment of this lien violate the automatic stay? If so, the estate would be entitled to the judgment, and the trustee has so argued. The bankruptcy court, however, held that the lien did not violate the automatic stay, because though the lien attached postpetition, it did so automatically, with no “act” violating the stay. The Tenth Circuit has granted direct review of this decision, and a decision applying *Cowen* is likely, but whatever decision is reached by the panel, a petition for en banc review or certiorari, challenging *Cowen*, seems likely.

CONCLUSION

Because of the large number of Chapter 13 cases in which an automobile of the debtor has been repossessed, the question whether the automatic stay requires return of vehicle will remain an important one. As set out in the 2013 *Law Letter* and in this one, it is also a complicated one.

ENDNOTES:

¹See *In re Knaus*, 889 F.2d 773, 775, 19 Bankr. Ct. Dec. (CRR) 1691, Bankr. L. Rep. (CCH) P 73117 (8th Cir. 1989); *In re Del Mission Ltd.*, 98 F.3d 1147, 1151-52, 29 Bankr. Ct. Dec. (CRR) 1155, 36 Collier Bankr. Cas. 2d (MB) 1658, Bankr. L. Rep. (CCH) P 77176, 36 Fed. R. Serv. 3d 512 (9th Cir. 1996) (expressly adopting the reasoning of *In re Abrams*, 127 B.R. 239, 241-43, 21 Bankr. Ct. Dec. (CRR) 1283, 25 Collier Bankr. Cas. 2d (MB) 15, Bankr. L. Rep. (CCH) P 74023 (B.A.P. 9th Cir. 1991), holding that failure to return a repossessed car after receiving notice of the debtor’s bankruptcy violated § 362(a)(3)); *Thompson v. General Motors Acceptance Corp., LLC*, 566 F.3d 699, 703, 61 Collier Bankr. Cas. 2d (MB) 1611, Bankr. L. Rep. (CCH) P 81490 (7th Cir. 2009); and *In re Weber*, 719 F.3d 72, 81, 69 Collier Bankr. Cas. 2d (MB) 1168, Bankr. L. Rep. (CCH) P 82484 (2d Cir. 2013). Accord, *In re Yates*, 332 B.R. 1, 54 Collier Bankr. Cas. 2d (MB) 1901, 8 A.L.R. Fed. 2d 837 (B.A.P. 10th Cir. 2005) (abrogated by, *In re Cowen*, 849 F.3d 943, 63 Bankr. Ct. Dec. (CRR) 211, 77 Collier Bankr. Cas. 2d (MB) 438 (10th Cir. 2017)); *In re Sharon*, 234 B.R. 676, 1999 FED App. 0009P (B.A.P. 6th Cir. 1999); *In re Carrigg*, 216 B.R. 303, 31 Bankr. Ct. Dec. (CRR) 1324, Bankr. L. Rep. (CCH) P 77657 (B.A.P. 1st Cir. 1998). See also *In re Rozier*, 348 F.3d 1305 (11th

Cir. 2003), certified question answered, 278 Ga. 52, 597 S.E.2d 367, 54 U.C.C. Rep. Serv. 2d 31 (2004), and *In re Rozier*, 376 F.3d 1323, 1324, Bankr. L. Rep. (CCH) P 80137 (11th Cir. 2004) (requiring return of collateral obtained prepetition as long as the collateral remained estate property after repossession).

Because § 362(a)(3) applies only to estate property, however, these decisions do not require return of collateral to debtors who are not entitled to possess estate property—including all Chapter 7 debtors. Any right to receive repossessed property in Chapter 7 cases would belong to the trustee. In *re Perry*, 540 B.R. 710, 725 (Bankr. C.D. Cal. 2015), *aff’d in part, rev’d in part*, 2017 WL 1276075 (C.D. Cal. 2017) (“If a creditor fails to turn over the debtor’s property, the [Chapter 7] debtor cannot bring actions under § 362(a)(3) prior to the debtor’s exemption in the assets being perfected, because such actions may only be brought by the trustee. After the exemption reverts the property in the debtor, the debtor cannot bring a § 362(a)(3) action because the asset is then no longer property of the estate.”). In this *Law Letter*, “debtor” is used to mean a debtor entitled to possession of estate property.

²The only arguably inconsistent circuit decision issued before 2017 is *U.S. v. Inslaw, Inc.*, 932 F.2d 1467, 21 Bankr. Ct. Dec. (CRR) 1077, Bankr. L. Rep. (CCH) P 74056, 37 Cont. Cas. Fed. (CCH) P 76104 (D.C. Cir. 1991), which held that a creditor—the United States Department of Justice—was not required to return to the debtor computer programming material whose ownership was in dispute, reasoning that a party claiming ownership of property could not be required to surrender the property to a debtor with a competing ownership claim before the ownership dispute was adjudicated. In that context, the court stated both that “it is difficult to believe that Congress intended a [stay] violation whenever someone already in possession of property mistakenly refuses to capitulate to a bankrupt’s assertion of rights in that property” and that the stay “serves as a restraint only on acts to gain possession or control over property of the estate,” rather than “creat[ing] an affirmative duty to remedy past acts of fraud or bias or harassment.” *Id.* at 1473-74. *Inslaw* did not consider whether § 362(a)(3) requires the return of collateral when the debtor’s ownership of the property is undisputed, and indeed cites *Knaus*, the leading case so holding, for the rule that “turnover of property admitted to belong to the debtor is required.” 932 F.2d at 1472.

³*In re Cowen*, 849 F.3d 943, 63 Bankr. Ct. Dec. (CRR) 211, 77 Collier Bankr. Cas. 2d (MB) 438 (10th Cir. 2017). The facts in *Cowen* make it a somewhat unattractive case for upsetting the rule requiring repossessed collateral to be returned to debtors. The vehicle involved in the case was a truck that a Chapter 13 debtor used in his business

and was subject to a purchase money security interest held by another individual, Bert Dring. The circuit court opinion explains how the truck came to be repossessed:

Mr. Dring lured Mr. Cowen under false pretenses to his place of business to repossess the Kenworth [truck]. Mr. Dring asked Mr. Cowen, who had brought along his young son, to leave the keys in the ignition, engine running, and to step out of the truck. As Mr. Cowen exited the vehicle, Mr. Dring jumped in, grabbed the keys, and declared the truck “repossessed.” When Mr. Cowen asked what was going on, Mr. Dring told him to take his son and leave—immediately. A group of five men gathered around Mr. Dring while he brandished a can of mace above his head and threatened to use it if Mr. Cowen did not leave. Mr. Cowen pushed his young son behind him to protect him, and the two left the lot on foot.

Id. at 945. After Cowen filed a Chapter 13 bankruptcy case, Dring objected to any bankruptcy treatment of the truck. The decision explains:

Mr. Dring claimed that he sold the Kenworth sometime prior to the bankruptcy filing. (Initially, he claimed he had sold the Kenworth to an unknown Mexican national for cash in an undocumented sale just days before Mr. Cowen filed for bankruptcy. Later, Mr. Dring produced bill of sale, purporting to show that he sold the Kenworth to a Mr. Garcia for \$16,000 in cash on August 4 [two days before the bankruptcy filing].

Id. at 946. The bankruptcy court found that Dring (and a relative involved in the repossession of another of Cowen’s trucks) had probably forged documents, given perjured testimony, and coached witnesses during a hearing on the adversary proceeding that Cowen brought to enforce the automatic stay. Id.

⁴Cowen, 849 F.3d at 949-50, quoting Ralph Brubaker, Turnover, Adequate Protection, and the Automatic Stay (Parts I and II): Who Is “Exercising Control” Over What?, 33 Bankr. L. Letter Nos. 8-9 (Sept. & Aug. 2013).

⁵Weber v. SEFCU (In re Weber), 719 F.3d at 79. See also, Thompson, 566 F.3d at 702 (making the same point, citing a different dictionary).

⁶Weber v. SEFCU (In re Weber), 719 F.3d at 80.

⁷The 2013 *Law Letter* gives a much fuller set of reasons than *Cowen* does for rejecting the majority interpretation. For a judicial decision discussing these reasons and extensively citing the *Law Letter*, see In re Hall, 502 B.R. 650, 59 Bankr. Ct. Dec. (CRR) 6 (Bankr. D. D.C. 2014).

⁸Brubaker, 33 Bankr. L. Letter No. 9 at 8-9, citing *Dewsnup v. Timm*, 502 U.S. 410, 419, 112 S. Ct. 773, 116 L. Ed. 2d 903, 22 Bankr. Ct. Dec. (CRR) 750, 25 Collier Bankr. Cas. 2d (MB) 1297, Bankr. L. Rep. (CCH) P 74361A (1992).

⁹See *Bank of America, N.A. v. Caulkett*, 135 S.

Ct. 1995, n.1, 192 L. Ed. 2d 52, 61 Bankr. Ct. Dec. (CRR) 31, 73 C.B.C. 1485, Bankr. L. Rep. (CCH) P 82807 (2015):

From its inception, *Dewsnup v. Timm*, 502 U.S. 410, 112 S. Ct. 773, 116 L. Ed. 2d 903 (1992), has been the target of criticism. See, e.g., id., at 420-436, 112 S. Ct. 773 (Scalia, J., dissenting); In re Woolsey, 696 F. 3d 1266, 1273-1274, 1278 (CA10 2012); In re Dever, 164 B. R. 132, 138, 145 (Bkrcty. Ct. CD Cal. 1994); Carlson, Bifurcation of Undersecured Claims in Bankruptcy, 70 Am. Bankr. L. J. 1, 12-20 (1996); Ponoroff & Knippenberg, The Immovable Object Versus the Irresistible Force: Re-thinking the Relationship Between Secured Credit and Bankruptcy Policy, 95 Mich. L. Rev. 2234, 2305-2307 (1997); see also *Bank of America Nat. Trust and Sav. Assn. v. 203 North LaSalle Street Partnership*, 526 U.S. 434, 463, 119 S. Ct. 1411, 143 L. Ed. 2d 607, and n. 3 (1999) (Thomas, J., concurring in judgment) (collecting cases and observing that “[t]he methodological confusion created by *Dewsnup* has enshrouded both the Courts of Appeals and . . . Bankruptcy Courts”).

¹⁰Brubaker, 33 Bankr. L. Letter No. 9 at 2.

¹¹See 11 U.S.C.A. § 363(e), providing for adequate protection “on request of an entity that has an interest in [estate] property”; *U.S. v. Whiting Pools, Inc.*, 1983-2 C.B. 239, 462 U.S. 198, 204, 103 S. Ct. 2309, 2313, 76 L. Ed. 2d 515, 10 Bankr. Ct. Dec. (CRR) 705, 8 Collier Bankr. Cas. 2d (MB) 710, Bankr. L. Rep. (CCH) P 69207, 83-1 U.S. Tax Cas. (CCH) P 9394, 52 A.F.T.R.2d 83-5121 (1983) (“At the secured creditor’s insistence, the bankruptcy court must place such limits or conditions . . . as are necessary to protect the creditor.”).

¹²See In re R. Purbeck & Associates, Ltd., 12 B.R. 406, 408 (Bankr. D. Conn. 1981) (“[A] secured creditor may insist upon adequate protection as a condition precedent to the turnover of property since the property may not be used, sold or leased under section 363 without it.”).

¹³Thompson, 566 F.3d at 702.

¹⁴Brubaker, 33 Bankr. L. Letter No. 9 at 3, citing *Inslaw*, 932 F.2d at 1474. The clarity of the 1984 amendment to § 362(a)(3) is a critical question under the *Dewsnup* approach to statutory construction. There is no relevant legislative history for the 1984 amendment to § 362(a)(3), but *Dewsnup* recognizes that this cannot defeat the effect of clear statutory language. See *Dewsnup*, 502 U.S. at 419-20, 112 S. Ct. at 779 (“Of course, where the language is unambiguous, silence in the legislative history cannot be controlling.”).

¹⁵*Inslaw*, 932 F.2d at 1472 (defining the “property” at issue as the debtor’s “intangible trade secret rights” and the asserted “exercise of control” as the use of these rights contrary to the parties’ contract).

¹⁶*Inslaw*, 932 F.2d at 1472 (“Whenever a party against whom the bankrupt holds a cause of action

(or other intangible property right) acted in accord with his view of the dispute rather than that of the debtor-in-possession or bankruptcy trustee, he would risk a determination by a bankruptcy court that he had ‘exercised control’ over intangible rights (property) of the estate.”)

¹⁷Citizens Bank of Maryland v. Strumpf, 516 U.S. 16, 21, 116 S. Ct. 286, 290, 133 L. Ed. 2d 258, 28 Bankr. Ct. Dec. (CRR) 97, 33 Collier Bankr. Cas. 2d (MB) 869, Bankr. L. Rep. (CCH) P 76666A (1995).

¹⁸Strumpf, 516 U.S. 16, 21, 116 S. Ct. 286, 290 (1995).

¹⁹Brubaker, 33 Bankr. L. Letter No. 9 at 3, quoting Inslaw, 932 F.2d at 1474.

²⁰American Heritage College Dictionary 556, 479 (3d ed. 1997)

²¹Cowen, 849 F.3d at 949, quoting New Oxford American Dictionary 15 (3d ed. 2010) and Thompson, 566 F.3d at 703.

²²Brubaker, 33 Bankr. L. Letter No. 9 at 4, citing In re Computer Communications, Inc., 824 F.2d 725, 16 Bankr. Ct. Dec. (CRR) 615, 17 Collier Bankr. Cas. 2d (MB) 556, Bankr. L. Rep. (CCH) P 71933 (9th Cir. 1987).

²³Computer Communications, 824 F.2d at 728.

²⁴Brubaker, 33 Bankr. L. Letter No. 9 at 4-5, citing Thomas E. Plank, The Outer Boundaries of the Bankruptcy Estate, 47 Emory L.J. 1194, 1209, 1213 (1998).

²⁵Brubaker, 33 Bankr. L. Letter No. 9 at 5.

²⁶Hall, 502 B.R. at 667.

²⁷Precision Industries, Inc. v. Qualitech Steel SBQ, LLC, 327 F.3d 537, 544, 41 Bankr. Ct. Dec. (CRR) 65, 49 Collier Bankr. Cas. 2d (MB) 1765, Bankr. L. Rep. (CCH) P 78836 (7th Cir. 2003) summarizes the operation of § 362(f) this way:

Section 363 generally provides for the use, sale, or lease of property belonging to the bankruptcy estate. [S]ubsections (b) and (c) permit the trustee of a bankruptcy estate to sell estate property either within the normal course of a debtor’s business (in which case the sale may take place without prior notice and a hearing) or outside the normal course of business (in which case . . . notice and hearing are mandatory). Subsection (f) makes clear that the property, under specified conditions, may be sold unencumbered of interests held by others

²⁸Brubaker, 33 Bankr. L. Letter No. 9 at 6-9.

²⁹Brubaker, 33 Bankr. L. Letter No. 9 at 7-8.

³⁰Brubaker, 33 Bankr. L. Letter No. 9 at 9.

³¹In re Borden, 361 B.R. 489, 494, 62 U.C.C. Rep. Serv. 2d 158 (B.A.P. 8th Cir. 2007) (“[P]ossession is generally required for a possessory lien.”).

³²Brubaker, 33 Bankr. L. Letter No. 9 at 6-7.

³³In re WEB2B Payment Solutions, Inc., 488 B.R. 387, 393, 57 Bankr. Ct. Dec. (CRR) 202, Bankr. L. Rep. (CCH) P 82449 (B.A.P. 8th Cir. 2013).

³⁴Brubaker, 33 Bankr. L. Letter No. 9 at 8.

³⁵Restatement of Security § 80 cmt. c (1941). Among the decisions applying this common law rule is *Finch v. Miller*, 531 P.2d 892, 893 (Or. 1975)(en banc) (holding that a possessory lien was not lost by the debtors’ removing the collateral from the creditor’s possession without the creditor’s consent).

³⁶See *Gangloff Industries, Inc. v. Generic Financing and Leasing, Corp.*, 907 N.E.2d 1059, 69 U.C.C. Rep. Serv. 2d 113 (Ind. Ct. App. 2009) (holding that a possessory lien continued in effect after the secured creditor had given up possession of the collateral pursuant to an erroneous court order).

³⁷WEB2B, 488 B.R. at 393.

³⁸In re Hayden, 308 B.R. 428, 51 Collier Bankr. Cas. 2d (MB) 1688, Bankr. L. Rep. (CCH) P 80084 (B.A.P. 9th Cir. 2004).

³⁹Hayden, 308 B.R. at 432.

⁴⁰In re Avila, 566 B.R. 558, 560, 77 Collier Bankr. Cas. 2d (MB) 709 (Bankr. N.D. Ill. 2017).

⁴¹In re Howard, 584 B.R. 252 (Bankr. N.D. Ill. 2018).

⁴²In re Fulton, 2018 WL 2392854 (Bankr. N.D. Ill. 2018), opinion amended and superseded, 2018 WL 2570109 (Bankr. N.D. Ill. 2018)

⁴³See, e.g., In re Siciliano, 13 F.3d 748, 751, 30 Collier Bankr. Cas. 2d (MB) 667, Bankr. L. Rep. (CCH) P 75656 (3d Cir. 1994) In re Schwartz, 954 F.2d 569, 573, 22 Bankr. Ct. Dec. (CRR) 845, 26 Collier Bankr. Cas. 2d (MB) 649, Bankr. L. Rep. (CCH) P 74539, 92-1 U.S. Tax Cas. (CCH) P 50069, 69 A.F.T.R.2d 92-548 (9th Cir. 1992); *Sikes v. Global Marine, Inc.*, 881 F.2d 176, 178-79, 19 Bankr. Ct. Dec. (CRR) 1224, Bankr. L. Rep. (CCH) P 73061 (5th Cir. 1989) (rejected by, In re Servizio, Inc., 144 B.R. 933, 23 Bankr. Ct. Dec. (CRR) 687, 27 Collier Bankr. Cas. 2d (MB) 1239, Bankr. L. Rep. (CCH) P 74936 (Bankr. S.D. Fla. 1992)); In re Albany Partners, Ltd., 749 F.2d 670, 675, 12 Bankr. Ct. Dec. (CRR) 787, 12 Collier Bankr. Cas. 2d (MB) 244, Bankr. L. Rep. (CCH) P 70184 (11th Cir. 1984) (rejected by, In re Victoria Ltd. Partnership, 187 B.R. 54, 27 Bankr. Ct. Dec. (CRR) 1210, Bankr. L. Rep. (CCH) P 76666 (Bankr. D. Mass. 1995)).

⁴⁴See In re Myers, 491 F.3d 120, 129, 48 Bankr. Ct. Dec. (CRR) 133, Bankr. L. Rep. (CCH) P 80962 (3d Cir. 2007) (“Even those cases that have subscribed to a narrow conception of the power to retroactively annul the stay have affirmed that balancing the equities is the appropriate test.”)

⁴⁵See In re National Environmental Waste Corp., 129 F.3d 1052, 1055, 31 Bankr. Ct. Dec. (CRR) 876, Bankr. L. Rep. (CCH) P 77541 (9th Cir. 1997); *Easley v. Pettibone Michigan Corp.*, 990 F.2d

905, 911, 28 Collier Bankr. Cas. 2d (MB) 1002 (6th Cir. 1993).

⁴⁶In re Stockwell, 262 B.R. 275, 281, 37 Bankr. Ct. Dec. (CRR) 244 (Bankr. D. Vt. 2001).

⁴⁷The Bankruptcy Court for the District of New Jersey appears to have had a practice that informally came to this result without requiring the filing of a motion to annul the stay. See *In re Denby-Peterson*, 576 B.R. 66, 81, 93 U.C.C. Rep. Serv. 2d 1367 (Bankr. D. N.J. 2017) (“For at least the last 20 years . . . the practice in this district has been that a creditor holding a car repossessed prepetition may request proof of insurance naming it as loss payee prior to turnover without violating the stay. But once proof of insurance has been produced, the creditor violates the stay by not returning the car.”). The court questioned the basis for this practice and suggested that the minority interpretation of § 362(a)(3) is preferable, at least if there is a dispute about the debtor’s ownership of the vehicle, but that for personal property free of liens, the creditor may violate the automatic stay by failing to return the property to the debtor on request. *Id.* at 82-83.

⁴⁸One court has treated the lack of vehicle insurance as grounds for automatically annulling the

automatic stay. The Bankruptcy Court for the Western District of Missouri has adopted a local rule, Rule 4070-1, prohibiting a debtor from operating an uninsured vehicle and giving the secured creditor, after notice to the debtor and an opportunity to obtain insurance, the right to repossess the vehicle without seeking relief from the automatic stay. When this rule was challenged, the court found that it was supported by annulment under § 362(d)(2). *In re Suggs*, 354 B.R. 903, 912 (Bankr. W.D. Mo. 2006), rev’d and remanded, 377 B.R. 198 (B.A.P. 8th Cir. 2007) (The Court . . . essentially annuls the automatic stay and retroactively validates the repossession. A rule authorizing the creditor’s action and the entry of such an order is therefore not inconsistent with § 362.”).

⁴⁹See *In re Hicks*, 2011 WL 2414419 (Bankr. N.D. Ala. 2011).

⁵⁰*In re Garcia*, 2017 WL 2951439 (Bankr. D. Kan. 2017).

⁵¹K.S.A. § 44-504.

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*Student Debt and Chapter 13 Eligibility**

By:

Judge Deborah L. Thorne
Northern District of Illinois

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Class of 2020

I. Background Information

- One of the main purposes of individual bankruptcy is to provide a debtor with a “fresh start.”¹ However, student loan debt is one type of debt that is not dischargeable.²
- According to at least one source, the United States’ total outstanding loan debt exceeds \$1.5 trillion.³
- Some believe that the student loan debt problem will cause a similar bubble to the housing market bubble.⁴
- At least two sources estimate that roughly 28–29% of all student loan borrowers ultimately default on their loans at some point.⁵
- There are forgiveness programs, but these programs only apply to loans from the government.⁶
 - The ordinary forgiveness programs result in taxable income being recognized to the extent of the forgiveness.⁷ Depending on the circumstances surrounding the forgiveness (e.g., insolvency), the recognition of taxable income may be deferred depending on the status of the borrower’s favorable tax attributes (if any) and the basis in the property that she holds in the taxable year immediately following the taxable year in which the debt forgiveness occurs.⁸
 - The Public Service Loan Forgiveness program, a program in which a borrower works for 10 years in qualifying employment,⁹ does not result in taxable income being recognized upon debt forgiveness.¹⁰
- For-profit higher education students only account for 11% of the higher education population.¹¹

¹ See *Lamar, Archer & Cofrin, LLP v. Appling*, 138 S. Ct. 1752, 1758 (2018).

² 11 U.S.C. § 523(a)(8).

³ Zack Friedman, *Student Loan Debt Statistics in 2018: A \$1.5 Trillion Crisis*, FORBES (June 13, 2018, 8:32 A.M.), <https://www.forbes.com/sites/zackfriedman/2018/06/13/student-loan-debt-statistics-2018/#5e4e7c867310>.

⁴ See Jim Rogers & Robert Craig Baum, *This Economic Bubble Is Going to Wreak Havoc When It Bursts*, FORTUNE (July 10, 2017), <http://fortune.com/2017/07/10/higher-education-student-loans-economic-bubble-federal/>.

⁵ Judith Scott-Clayton, *The Looming Student Loan Default Crisis is Worse than We Thought*, BROOKINGS (Jan. 11, 2018), <https://www.brookings.edu/research/the-looming-student-loan-default-crisis-is-worse-than-we-thought/>. By 2023, the default rate may be as high as 40%. *Id.*

⁶ See 20 U.S.C. § 1098e(b).

⁷ I.R.C. § 61(a)(12).

⁸ I.R.C. §§ 108(a)–(b), 1017(a); *Comm’r v. Tufts*, 461 U.S. 300, 319 (1983) (O’Connor, J., concurring) (noting that sections 108 and 1017 allow a taxpayer to defer the recognition of income due to the forgiveness of indebtedness). If a borrower (1) takes advantage of one of the circumstances found in section 108(a)(1), (2) possesses none of the favorable tax attributes describe in section 108(b)(2)(A)–(D), (F)–(G), and (3) has no assets or has zero tax basis in any assets she does own, then it seems as though income tax on debt forgiveness could be avoided *entirely*. I.R.C. §§ 108(b)(2), (3)(A), 1017(a)(2); Treas. Reg. § 1.1017–1(a) (noting that basis in property may not be reduced below zero).

⁹ 34 C.F.R. § 685.219.

¹⁰ I.R.C. § 108(f)(2).

¹¹ Note, *Forgive and Forget: Bankruptcy Reform in the Context of for-Profit Colleges*, 128 HARV. L. REV. 2018, 2019 (2015).

- For-profit institution student loan default rates are universally higher than the default rates for other types of institutions; “[m]ost students who defaulted between three and five years in repayment attended a for-profit college.”¹²

II. The Statute – History and Qualifying “Debts”

1. Section 523(a)(8)
 - a. Excludes public and private student loans from discharge in bankruptcy unless “excepting such debt from discharge . . . would impose an undue hardship on the debtor or the debtor’s dependents.”¹³
2. History
 - a. The present statute is the product of a series of amendments to Bankruptcy Code that roughly parallels the development of the modern student loan industry.¹⁴
 - b. Before 1976, educational loans were completely dischargeable in bankruptcy courts.¹⁵ The first provision that restricted student loan debt appeared in 1976, when the Bankruptcy Act was amended to make government-backed loans non-dischargeable for the first five years after the first loan payment was due. During the five-year period, student loans only became dischargeable if the debtor could present an undue hardship.¹⁶
 - c. When the Bankruptcy Code was adopted in 1978, the limitation to the dischargeability of student loans was expanded to include any educational loan debt owed to a governmental unit or to a nonprofit institution of higher education.¹⁷
 - d. In 1979, the statute was amended to include private loans insured or guaranteed by a governmental unit or nonprofit institution of higher education.¹⁸
 - e. In 1984, the words “of higher education” were removed, “effectively exempting from discharge all non-profit student loans, regardless of who made the loan.”¹⁹
 - f. The five-year limit was increased to seven in 1990 by Congress.²⁰ The term limit was abolished in 1998, leaving undue hardship as the only avenue for student loan dischargeability.²¹
 - g. In 2005, BAPCA extended the application of the statute to all private student loans, as long as the loans were made in order to enable attendance at a qualifying

¹² Ben Miller, *The Student Debt Problem is Worse than We Imagined*, N.Y. TIMES (Aug. 25, 2018), <https://www.nytimes.com/interactive/2018/08/25/opinion/sunday/student-debt-loan-default-college.html>.

¹³ 11 U.S.C. § 523(a)(8).

¹⁴ See, e.g., Frank T. Bayuk, *The Superiority of Partial Discharge for Student Loans Under 11 U.S.C. § 523(a)(8): Ensuring A Meaningful Existence for the Undue Hardship Exception*, 31 FLA. ST. U. L. REV. 1091, 1094–96 (2004) (describing the legislative history behind section 523(a)(8)).

¹⁵ *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440, 449 (2004).

¹⁶ Comment, *Student Loans: Path to Success or Road to the Abyss? An Argument to Reform the Student Loan Discharge Exception*, 89 TEMP. L. REV. 155, 164 (2016).

¹⁷ *Id.* at 167.

¹⁸ Preston Mueller, *The Non-Dischargeability of Private Student Loans: A Looming Financial Crisis?*, 32 EMORY BANKR. DEV. J. 229, 233 (2015).

¹⁹ *Id.*

²⁰ *Id.*

²¹ *Id.*

institution, with qualification determined by reference to various provisions in the Internal Revenue Code and the Higher Education Act.²²

3. The Current Statute:²³

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt—

(8) unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor’s dependents, for—

(A)

(i) an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution; or

(ii) an obligation to repay funds received as an educational benefit, scholarship, or stipend; or

(B) any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual

4. Section 523(a)(8)(A)(i)

a. In the main, this sub-section is aimed at loans made, insured, or guaranteed by a governmental unit or made under some program that is at least partially funded by a governmental unit or nonprofit institution. Importantly, “loan” is not defined. The following definition is widely adopted:

i. “To constitute a loan there must be (i) a contract, whereby (ii) one party transfers a defined quantity of money, goods, or services, to another, and (iii) the other party agrees to pay for the sum or items transferred at a later date.”²⁴

ii. Thus, a school does not make a “loan” to a student if it extends educational services on credit and the student later fails to pay the school when the debt comes due.²⁵

b. “Educational” is similarly not defined.

i. At least some courts look to the *purpose* of the loan when it was made

²² *Id.* at 233–34. For statutory guidance on when a student is an “eligible student,” as is necessary for the loan to be a “qualifying education loan,” see I.R.C. §§ 221(d)(1), (d)(1)(C), (d)(3), 25A(b)(3)(A); 20 U.S.C. §§ 1091(a)(1), 1001(a), 1002(a)(1), 1094. For statutory guidance on when a loan is made to cover “qualified higher education expenses,” as is *also* necessary for the loan to be a “qualifying education loan,” see I.R.C. §§ 221(d)(1), (d)(2), (d)(2)(B), 25A(f)(2)(B).

²³ 11 U.S.C. § 523(a)(8).

²⁴ *Cazenovia College v. Renshaw (In re Renshaw)*, 222 F.3d 82, 88 (2d Cir. 2000) (citing *In re Grand Union Co.*, 219 F. 353, 356 (2d Cir. 1914)); *see also In re Chambers*, 348 F.3d 650, 657 (7th Cir. 2003) (adopting this definition).

²⁵ *See, e.g., Chambers*, 348 F.3d at 657–58.

to determine whether or not it is “educational,” rather than the manner in which the funds were actually used by the borrower following disbursement.²⁶

5. Section 523(a)(8)(A)(ii)
 - a. While some courts have held otherwise, the better view is that this section excepts from discharge only educational debts *other than loans*.²⁷
 - i. Applying this section to ordinary private student loans (not falling within either section 523(a)(8)(A)(i) or (a)(8)(B)) renders section 523(a)(8)(B) superfluous and of no application whatsoever, since any loan possibly insulated from discharge under section 523(a)(8)(B) would also necessarily be insulated under section 523(a)(8)(A)(ii) if that section were to be read to cover private loans.²⁸
 - ii. Thus, private lenders who do not otherwise fit within section 523(a)(8)(B) should not be able to take shelter under this provision; the section generally insulates only debts owing on account of some type of educational grant the conditions of which had not been complied with by the grantee.²⁹
 1. Funding in the nature of a scholarship or grant can be distinguished from funding in the nature of a loan or extension of credit in that, at the outset of the financial relationship between the grantor and the grantee, there is no intent to create a debtor-creditor relationship; that relationship only arises after the fact based on non-compliance with the conditions of the funding. Obviously if there are no conditions whatsoever to the funding, then no “debt” owing back to the grantor can ever be created.
6. Section 523(a)(8)(B)
 - a. Added in 2005 and expanded the scope of the statute to cover private student loans.³⁰
 - b. Covers private student loans as long as the institution being attended meets the requirements of various provisions of Title IV of the Higher Education Act.³¹

²⁶ See, e.g., *In re Sokolik*, 635 F.3d 261, 266–67 (7th Cir. 2011). “We need only ask whether the lender’s agreement with the borrower was *predicated on the borrower being a student who needed financial support to get through school*.” *Id.* at 266 (emphasis added). “Permitting students to discharge student loans in bankruptcy because the student spent the money on social uses, alcohol, or even drugs would create an absurd result. Students who used the loan proceeds to finance an education would retain the burden of paying them even after a chapter 7 discharge; irresponsible students who abused the loans would gain the benefits of discharge.” *In re Murphy*, 282 F.3d 868, 873 (5th Cir. 2002).

²⁷ See 4 COLLIER ON BANKRUPTCY ¶ 523.14[2] (16th ed. 2018).

²⁸ See *Nunez v. Key Educ. Res./GLESI (In re Nunez)*, 527 B.R. 410, 415 (Bankr. D. Or. 2015) (“Such an interpretation would render § 523(a)(8)(B), the provision that Congress added to § 523(a)(8) in BAPCPA, superfluous and makes no sense.”); *In re Decena*, 549 B.R. 11, 19 (Bankr. E.D.N.Y.) (“It defies logic to suggest that Congress added subsection 523(a)(8)(B) in 2005 to encompass a subset of loans already covered under subsection 523(a)(8)(A)(ii).”), *rev’d on other grounds, Citizens Bank v. Decena*, 562 B.R. 202 (E.D.N.Y. 2016).

²⁹ *In re Campbell*, 547 B.R. 49, 55 (Bankr. E.D.N.Y. 2016) (“The concept which unites the three separate terms in the list in § 523(a)(8)(A)(ii) is that they all refer to types of conditional grants.”).

³⁰ *In re Engen*, 561 B.R. 523, 531 (Bankr. D. Kan. 2016).

³¹ *In re Wiley*, 579 B.R. 1, 11 (Bankr. D. Me. 2017) (“By linking section 523(a)(8)(B) to section 221 of the IRC, Congress ensured that the credit extended was for purposes of attending an institution that is

- c. Private lenders who lent funds to students who were not attending Title IV-qualified institutions should not fit in under this subsection.³²

III. The Statute – Assuming that a Debt Fits within the Reach of 523(a)(8), when may it be Discharged in Bankruptcy?

1. Only when it presents an “undue hardship.”³³
2. There are two widely accepted tests; one is the *Brunner* test and the other is a general “totality of the circumstances” test.³⁴
3. The *Brunner* test:
 - (1) The debtor cannot maintain, based on current income and expenses, a “minimal” standard of living for herself and her dependents if forced to repay the loans;
 - a. This is extremely fact sensitive. It was error, for instance, to utilize IRS standards in applying this part of the test.³⁵ Another court concluded that the availability of income-based repayment programs meant that the debtor’s projected student loan payments could be reduced to \$0 for the purposes of running this part of the *Brunner* test.³⁶ Having no disposable income can serve to satisfy this part of the test.³⁷ Debtors should be allowed to use some money for recreation without failing this part of the test.³⁸
 - (2) Additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and
 - a. “Additional circumstances”: [(1)] Serious mental or physical disability of the debtor or the debtor's dependents which prevents employment or advancement; [(2)] The debtor's obligations to care for dependents; [(3)] Lack of, or severely limited education; [(4)] Poor quality of education; [(5)] Lack of usable or marketable job skills; [(6)] Underemployment; [(7)] Maximized income potential in the chosen educational field, and no other more lucrative job skills; [(8)] Limited number of years remaining in [the debtor's] work life to allow payment of the loan; [(9)] Age or other factors that prevent retraining or relocation as a means for payment of the loan; [(10)] Lack of assets, whether or not exempt, which could be used to pay the loan; [(11)] Potentially increasing expenses that outweigh any potential

eligible to offer programs under Title IV of the Higher Education Act of 1965.”) (quoting *In re Essangui*, 573 B.R. 614, 625 (Bankr. D. Md. 2017)); see also *supra* note 22.

³² See *In re Essangui*, 573 B.R. 614, 616, 620–26 (Bankr. D. Md. 2017) (case where a private lender stipulated that the institution for which it had lent funds to the debtor did not qualify as a Title IV institution; lender then unsuccessfully argued to the court that it fit within the section 523(a)(8)(A)(ii) exception); see also *supra* note 28.

³³ *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260, 263 (2010).

³⁴ Ben Wallen, *One Standard to Rule Them All: An Argument for Consistency in Education Debt Discharge in Bankruptcy Proceedings*, 16 HOUS. BUS. & TAX L. J. 232, 238–39 (2016).

³⁵ *In re Howe*, 319 B.R. 886, 894 (B.A.P. 9th Cir. 2005).

³⁶ *In re Murphy*, 535 B.R. 97, 109 (Bankr. W.D. Pa. 2015).

³⁷ *In re Johnson*, 550 B.R. 874, 880 (Bankr. M.D. Ala. 2016) (“Considering that she has no disposable income, the Court has little difficulty concluding that Johnson will be unable to maintain a minimal standard of living if forced to repay her student loan debt.”).

³⁸ *In re Gubrath*, 526 B.R. 863, 869–70 (D. Colo. 2014).

appreciation in the value of the debtor's assets and/or likely increases in the debtor's income; [(12)] Lack of better financial options elsewhere.³⁹

- (3) The debtor has made good-faith efforts repay the loan.⁴⁰
 - a. Courts use a variety of factor-analyses to run this part of the test. *E.g.*, “1) whether the debtor has made any payments on the loan prior to filing for discharge; 2) whether the debtor has sought deferments or forbearances; 3) the timing of the debtor's attempt to have the loan discharged; and 4) whether the debtor's financial condition resulted from factors beyond her reasonable control, as a debtor may not willfully or negligently cause her own default.”⁴¹
4. Eight other circuits outside of the Second generally apply the *Brunner* test, though not always without modification.⁴²
5. The Eighth Circuit has adopted a totality of the circumstances test.⁴³
 - a. “In evaluating the totality-of-the-circumstances, our bankruptcy reviewing courts should consider: (1) the debtor's past, present, and reasonably reliable future financial resources; (2) a calculation of the debtor's and her dependent's reasonable necessary living expenses; and (3) any other relevant facts and circumstances surrounding each particular bankruptcy case.”⁴⁴
 - b. Examples:
 - i. *In re Walker*, 650 F.3d 1227 (8th Cir. 2011).
 - A debtor established undue hardship when she was a mother of five, had two children with autism, and had to leave employment to care for the two with autism.
 - ii. *In re Abney*, 540 B.R. 681 (Bankr. W.D. Mo. 2015).
 - A debtor with the only job skill of being a driver was discharged.
 - iii. *In re Hurst*, 553 B.R. 133 (B.A.P. 8th Cir. 2016).
 - A 66-year old debtor who could afford to make minimal payments was not exempt because she never made any attempt to pay or address the student loan debt in 20 years.

6. Partial Discharge

- a. Sixth Circuit has held that partial discharge is permitted under section 105(a).⁴⁵ The debtor must still satisfy each prong of the Brunner test with

³⁹ *In re Nys*, 446 F.3d 938, 947 (9th Cir. 2006).

⁴⁰ *Brunner v. New York State Higher Educ. Servs. Corp.*, 831 F.2d 395, 396 (2d Cir. 1987).

⁴¹ *In re Roth*, 490 B.R. 908, 917 (B.A.P. 9th Cir. 2013)

⁴² *In re Frushour*, 433 F.3d 393, 400 (4th Cir. 2005); *Educ. Credit Mgmt. Corp. v. Polleys*, 356 F.3d 1302, 1309 (10th Cir. 2004); *United States Dep't of Educ. v. Gerhardt (In re Gerhardt)*, 348 F.3d 89, 91 (5th Cir. 2003); *Hemar Ins. Corp. of Am. v. Cox (In re Cox)*, 338 F.3d 1238, 1241 (11th Cir. 2003); *United Student Aid Funds, Inc. v. Pena (In re Pena)*, 155 F.3d 1108, 1114 (9th Cir. 1998); *Penn. Higher Educ. Assistance Agency v. Faish (In re Faish)*, 72 F.3d 298, 306 (3d Cir. 1995); *Cheesman v. Tenn. Student Assistance Corp. (In re Cheesman)*, 25 F.3d 356, 359–60 (6th Cir. 1994); *In re Roberson*, 999 F.2d 1132, 1135–36 (7th Cir. 1993).

⁴³ *In re Long*, 322 F.3d 549, 554 (8th Cir. 2003).

⁴⁴ *Id.*

⁴⁵ *In re Oyler*, 397 F.3d 382 (6th Cir. 2005).

- respect to the portion of the debt to be discharged, and the discharge is allocated pro rata among the debtor's loan.
- b. Courts in the Ninth, Tenth, and Eleventh Circuits have also granted partial discharge using the *Brunner* Test.
 - i. *In re Jorgensen*, 2012 Bankr. LEXIS 254 (Bankr. D. Haw. Jan. 20, 2012).
 1. When a debtor had cancer, and it was likely to persist throughout a debtor's life, the court discharged all but \$8,045.02.
 - ii. *In re Metz*, No. 12-13120, 2018 WL 4656186 (Bankr. D. Kan. Sept. 25, 2018).
 1. Debtor borrowed \$16,613 from 1989 to 1991, and by the time of the case owed \$67,277.88 due to accumulated interest. The court found that she could pay the original principal amount without suffering an undue hardship, but that to pay the accumulated interest would result in an undue hardship. Specifically, she could not maintain a minimal standard of living while paying the interest and principal (a ~\$550/mo. payment vs. a ~\$200/mo. payment for just principal). Her financial condition was unlikely to improve, and was in fact likely to deteriorate as she reached a point at which her primary source of income would be social security and some modest retirement savings. She had made good faith efforts to repay, namely she had paid over \$14,000 on the loan, none of which had gone to principal. So the court granted a partial discharge of just the accumulated interest portion of the debt.
 - c. The Seventh Circuit has not explicitly ruled on the issue,⁴⁶ but there are opinions discussing the issue.
 - i. At least one court has questioned its authority to grant a partial discharge.⁴⁷
 - ii. Another has granted a partial discharge, discharging that part of the loan that could not be paid even after the debtor's expenses had been properly reduced from the face amounts that the debtor had claimed.⁴⁸

IV. Distinguishing *Brunner*

Then and Now

- *Brunner* was decided in 1985, and in 1990 with the Student Loan Default Prevention Initiative Act government student lending began to be shaped at least in part by reference to default rates.⁴⁹ In the Act, Congress amended the Higher Education Act to include default rates as a restriction to access

⁴⁶ See *In re Modeen*, 586 B.R. 298, 308 (Bankr. W.D. Wis. 2018); *In re Shirzadi*, 269 B.R. 664, 667 (Bankr. S.D. Ind. 2001).

⁴⁷ *In re Armstrong*, No. 10-82092, 2011 WL 6779326, at *9 n.12 (Bankr. C.D. Ill. Dec. 27, 2011).

⁴⁸ *Modeen*, 586 B.R. at 308. The court, in discussing the partial discharge, noted that it is appropriate only for that portion of the debt that meets section 523(a)(8)'s undue hardship standard. *Id.* at 306.

⁴⁹ *Forgive and Forget*, supra note 11, at 2030.

funding.⁵⁰ For the first time, institutions’ access to federal loan programs was based on graduates’ success on repaying student loans.⁵¹ In 2014, the policies became more stringent.⁵² “[T]he debt-to-earnings requirement in the October 2014 regulations considers exactly what the Brunner court assumed the government as a lender could not: likelihood of payment. The new regulations provide a more sophisticated measure of risk assessment than previous regulations. Unlike the cohort default rates [in 1990], which simply measured the number of students avoiding default, the gainful-employment requirement actually looks at the expected ability of a graduate to actively repay loan debt based on earnings and disposable income. This practice of using ratio of income debt burden is similar to underwriting standards employed in mortgage lending decisions. . . . Here, the Department of Education has likewise decided to limit the access of for-profit institutions to Title IV funding under a similar rationale. And the actual ratios and percentages of the debt-to-earnings requirement can function as a more objective filter than the first prong of the Brunner test. By looking at loan payments as a percentage of discretionary income and annual earnings, the Department has in part qualified the subjective ‘minimal standard of living’ analysis”⁵³

- This state of affairs might be compared to the original legislative history from 1978, which states that “educational loans are *different from most loans. They are made without business considerations, without security, without cosigners, and relying for repayment solely on the debtor’s future increased income resulting from the education. In this sense, the loan is viewed as a mortgage on the debtor’s future.*” *Matter of Roberson*, 999 F.2d 1132, 1135–36 (7th Cir. 1993) (quoting H.R. Rep. No. 595 (1977), as reprinted in 1978 U.S.C.C.A.N. 5963, 6094) (emphasis added).

V. *Krieger* and *Roth*

1. “Two recent bankruptcy cases indicate that the judiciary might, in incremental fashion, be reintroducing a debtor’s ability to discharge student loans. Specifically, in 2013, the Seventh Circuit and Ninth Circuit Bankruptcy Appellate Panel (BAP) issued decisions that were critical of *Brunner* in *Krieger v. Educational Credit Management Corp.* and *Roth v. Educational Credit Management Corp. (In re Roth)*, respectively. *Krieger* and *Roth* have widened a decade-long circuit split that now threatens to compromise *Brunner*’s hold on the majority.”⁵⁴
 - a. In *Krieger*, the court referred to the language of *Brunner* (adopted by the Seventh Circuit in *In re Roberson*, 999 F.2d 1132, 1135 (7th Cir. 1993)) as a “judicial gloss” on the text of § 523(a)(8), and it cautioned against any judicial interpretation that supersedes the statute itself.⁵⁵ The court also explained that

⁵⁰ *Id.*

⁵¹ *Id.*

⁵² *Id.*

⁵³ *Id.* at 2030–31.

⁵⁴ Michael J. Fletcher et al., *Student Loan Discharge Decisions Poke Holes in the Brunner Test*, AM. BANKR. INST. J., Feb. 2014, at 42.

⁵⁵ *Krieger v. Educ. Credit Mgmt. Corp.*, 713 F.3d 882, 884 (7th Cir. 2013).

withholding discharge based on a debtor’s unwillingness to agree to *future* income-based repayment is improper as a matter of law “because it is *always* possible to pay in the future should prospects improve,” and section 523(a)(8) does not flatly forbid discharge in all cases.⁵⁶ It further noted that successive cases adopting *Brunner* have turned an “undue hardship” standard into one requiring an extraordinary showing of a “certainty of hopelessness.”⁵⁷

- Also noteworthy is the court’s emphasis that a bankruptcy court enjoys wide latitude in applying the three-part *Brunner* test. “[A] judge asked to apply a multi-factor standard interpreting an open-ended statute necessarily has latitude; the more vague the standard, the harder it is to find error in its application.”⁵⁸
- The court in *Krieger* did not abrogate *Roberson*, the case that had adopted as law in the Seventh Circuit the “gloss” articulated by the Second Circuit in *Brunner*.⁵⁹ The Seventh Circuit, for instance, recently applied the *Brunner/Roberson* standard in the aftermath of *Krieger*.⁶⁰ One aspect of *Krieger* relied upon by the court in *Tetzlaff* was the rule articulated in *Krieger* that the second prong of the *Brunner/Roberson* test (the additional circumstances prong) is a factual finding and is reviewed on appeal under a clearly erroneous standard.⁶¹ The court also noted that the same is generally true of the third *Brunner/Roberson* prong, namely good faith; that is, a determination that good faith efforts to repay the loan were either made or not made will be reviewed under a clearly erroneous standard in the usual case, just like a lower court finding on the additional circumstances prong.⁶² The court affirmed the Bankruptcy Court’s determination on both prongs (additional circumstances and good faith): “*With such deference in mind*, we find that the bankruptcy court’s conclusions on the additional circumstances prong and the good faith prong must both be affirmed.”⁶³

⁵⁶ *Id.* at 884.

⁵⁷ *Id.*

⁵⁸ *Id.* at 885.

⁵⁹ *In re Roberson*, 999 F.2d 1132 (7th Cir. 1993).

⁶⁰ *Tetzlaff v. Educ. Credit Mgmt. Corp.*, 794 F.3d 756 (7th Cir. 2015) (upholding Bankruptcy Court’s determination that a student loan debt was not dischargeable under section 523(a)(8); reviewing only the second two prongs of the *Brunner/Roberson* test; applying a clearly erroneous standard in reviewing the Bankruptcy Court’s determination).

⁶¹ *Id.*

⁶² *Id.* (emphasis added).

⁶³ *Id.* As to additional circumstances, the Debtor had a couple of advanced degrees, was not mentally ill, and seemed to be something of a “malingerer” based on evaluations and assessments. The lower court therefore found that additional circumstances did not exist, and this factual finding was affirmed by the Court of Appeals as not having been clearly erroneous. *Id.* at 759–60. As to good faith, the Court of Appeals upheld the lower court’s determination overall that good faith efforts at repayment had not been

- This sentiment regarding open-ended standards and the high degree of deference due to the fact-finder (the lower court) is borne out in *In re Acosta-Conniff*, where the Eleventh Circuit reversed a District Court decision that had reversed a Bankruptcy Court’s decision applying section 523(a)(8): “The district court did not, however, indicate whether it was applying a clear error or a *de novo* standard of review when it considered the bankruptcy court’s finding as to the second prong of the *Brunner* test, which is the only prong the district court examined. From our review of the district court order, we cannot confidently conclude that the court was applying a clear error standard. Given this uncertainty, we remand the case to the district court with instructions to apply clear-error review to the bankruptcy court’s factual findings as to each prong of the *Brunner* test and *de novo* review to any of the bankruptcy court’s legal conclusions. If the district court concludes that it lacks sufficient factual findings to review the bankruptcy court’s decision as to any of the three prongs, the district court may remand the matter to the bankruptcy court for further factual findings as it deems necessary.”⁶⁴
- b. In *Roth*, in his concurring opinion, Judge Pappas stated that the *Brunner* test “is too narrow, no longer reflects reality, and should be revised by the Ninth Circuit when it has the opportunity to do so.”⁶⁵ Judge Pappas further noted that student borrowing has changed significantly since 1987 when *Brunner* was decided and students now must “borrow heavily to finance their futures” due to the “mammoth costs of a modern education.”⁶⁶ Given these obstacles, Judge Pappas suggests that bankruptcy courts should “be free to consider the totality of a debtor’s circumstances in deciding whether a discharge of student loan debt for undue hardship is warranted.”⁶⁷ He acknowledged that Congress left the crafting of a working definition of undue hardship justifying discharge of educational debt under section 523(a)(8) up to bankruptcy courts and conceded that the *Brunner* test “might have been appropriate and helpful when adopted,” but it has now become a “relic of times long gone.”⁶⁸

VI. Can a chapter 13 debtor place the student loan debt in a separate class with treatment different than other unsecured debt?

made (the debtor had paid **\$0** on the loan at issue) and ruled that it was *not* legal error for the court to have disregarded payments made on a *separate educational loan* in considering whether or not good faith efforts at repayment had been made as to the *loan subject to the 523(a)(8) adversary*. *Id.* at 760–61.

⁶⁴ *In re Acosta-Conniff*, 686 F. App’x 647, 649–50 (11th Cir. 2017).

⁶⁵ *In re Roth*, 490 B.R. 908, 920 (B.A.P. 9th Cir. 2013).

⁶⁶ *Id.* at 922.

⁶⁷ *Id.* at 920.

⁶⁸ *Roth*, 490 B.R. at 920.

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1. Section 1322(b)(1) provides that a plan is not confirmable where a class is discriminated against unfairly.
2. Section 1322(b)(5) provides that a chapter 13 plan may “provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due”
3. Section 1322(b)(10) provides that payment of interest accruing after the date of the filing of the petition on unsecured claims that are nondischargeable under section 1328(a), except that such interest may be paid only to the extent that the debtor has disposable income available to pay such interest after making provision for full payment of all allowed claims (added in 2005 in BAPCPA)
4. Yes: Student loan debt may be separately classified.
 - a. *In re Engen*, 561 B.R. 523 (Bankr. D. Kan. 2016).
 - i. Court applied the “baseline test” which considers (1) equality of distribution; (2) nonpriority of student loans;(3) mandatory versus optional contributions; and (4) the debtor’s fresh start.
 - ii. Separate classification was approved even though on its face the separate classification was discriminatory. The proposed plan pays the student loan claims without post-petition interest prior to other general unsecured claims. Despite the distribution (with an unknown amount going to GUC, the proposed plan was found to be fair as the debtor’s non-student loan unsecured creditors received a significant prepetition dividend of 83% that discriminated against the student loan claims.
 - iii. Court also acknowledged the uniqueness that is student loan debt, distinguishing it from other 523(a) debts that are nondischargeable. Student loan debts are the only 523(a) debts that are “incurred for a supposedly socially beneficial purpose.” Student loans are nondischargeable because the “Congress wishes to protect the government’s fiscal health as a guarantor (or lender) of these loans.” *In re Knowles*, 501 B.R. 409, 418 (Bankr. D. Kan. 2013)
 - iv. Court was also mindful that without separate classification and treatment, the debtor would leave chapter 13 with more student loan debt than when he entered chapter 13. Separate classification was also proper under section 1322(b)(5).
 - b. *In re Truss*, 404 B.R. 329 (Bankr. E.D. Wis. 2009).
 - i. Plan placed long-term student loan debt in separate class and maintain payments under the terms of the nondischargeable note. Trustee objected stating that this is unfair discrimination under 1322(b)(1).
 - ii. Judge McGarity held that because Congress provided different treatment from other creditors in 1322(b)(5) just as it did for loans different treatment for other types of claims including those where the debtor is liable on a consumer debt along with another co-debtor, the specific provisions of 1322(b)(5) allow separate classification of long-term student loans.
 - iii. In *Truss*, the debtor’s plan paid the student loan creditor a dividend of 60 – 79% and the remaining unsecured creditors were projected to receive a dividend of 2.44%. If the funds were distributed pro rata, all unsecured

creditors would receive a dividend of 23.5%. Judge McGarity held that when Congress provides a bright-line rule such as 1322(b)(5), “it is not for the court to determine whether this is fair to the other creditors or not. Such a provision is authorized by statute.”

- c. *In re Johnson*, 446 B.R. 921 (Bankr. E.D. Wis. 2011).
 - i. Judge Kelley held that a student loan borrower could also place student loan debt in a separate class. The student loans were paid at the repayment rate during the plan.
 - ii. Judge Kelley found that section 1322(b)(5) which provides for cure and payment of longterm debts where the maturity date is beyond the final plan payment does not conflict with section 1322(b)(1). Judge Kelley followed Judge McGarity’s opinion in *In re Truss* adopting Judge Martin’s earlier position that the specific treatment provided for in (b)(5) trumps the (b)(1) requirement. (2011) 446 B.R. 921.
 - d. *In re Boggan*, 125 B.R. 533 (N.D. Ill. 1991).
 - i. Judge Barliant approved confirmation of a chapter 13 plan that provided for a greater percentage payment to an educational lender where the other unsecured creditors were receiving an amount that exceeded the amount they would get in a chapter 7 case. Barliant relies upon 1325(a)(4) in that the proposed plan passes the best interest test in that it provides each creditor at least what it would receive as a distribution in a chapter 7 case.
5. No, A chapter 13 plan may not separately classify student loan claims
- a. *McCullough v. Brown*, 162 B.R. 506 (N.D. Ill. 1993)
 - i. District Court Judge Shadur reversed Judge Wedoff after the chapter 13 trustee objected to a confirmation of a chapter 13 plan that provided that nondischargeable student loans would be paid in full while other unsecured claims would be paid between 10 and 20 percent of their allowed amount.
 - b. *In re Belda*, 315 B.R. 477 (N.D. Ill. 2004)
 - i. District Court reversed Judge Doyle who had held that a student loan borrower could separately classify student loan debt and pay 62% to the student loan lender while paying 10% to other unsecured creditors. District Judge Pallmeyer found that this was unfair discrimination, stating this is the majority view and that any discrimination between the amount of debt recovered by a student loan creditor and the amount recovered by unsecured creditors is improper. Pallmeyer suggests a “balanced approach” and would allow the student loan creditor to receive the same percentage payment as the rest of the unsecured creditors.
 - c. *In re Quinn*, 586 B.R. 1 (E.D. Mich. 2018)
 - i. Proposed chapter 13 plan discriminated unfairly by proposing to pay nondischargeable student loan obligations \$850 and as much as \$1,112.40 per month while paying remaining unsecured creditors nothing (which is what they would have received in a chapter 7).
 - ii. Court held that a totality of the circumstances inquiry was appropriate when examining the disparity in treatment

- iii. Under the proposed plan there was a slight benefit to debtor which did not offset the discrimination against the remaining unsecured creditors. This court suggests that it would approve some disparity of treatment between the nondischargeable student loan and the GUC, but the proposed plan was too unfair and the trustee's objection was sustained.

VII. *In re Pratola*

1. Even though the debtor owed close to \$600,000 in student loans, and thus was an ineligible chapter 13 debtor under section 109(e), “cause” did not exist to dismiss the case.⁶⁹
 - a. The court found sections 109(e) and 1307(c) ambiguous and then looked to legislative history.⁷⁰
 - b. The court found that the legislative history indicated that Congress's intent in passing the debt limit provision found in section 109(e) was to prevent sole proprietors with large businesses from filing for chapter 13, which would constitute an abuse of their creditors given the more creditor-friendly features of chapter 11.⁷¹ The debt limits were not intended to apply to educational debt.⁷²
 - c. The court also concluded that that the debt limits have not kept pace with rising educational costs.⁷³
 - d. The court ultimately concluded that there was no cause for dismissal of the case: “The express language of § 1307(c) does not require the Court to dismiss a case in which a debtor exceeds the § 109(e) unsecured debt limit. Nor does case law suggest that the Court must dismiss absolutely every case in which a debtor exceeds the limit. Here, Pratola exceeds the unsecured debt limit solely as a result of his educational debt. Dismissing his case would not advance the Congressional intent behind the debt limits, and doing so would hinder the principal purpose of the Bankruptcy Code—to grant a fresh start to the honest but unfortunate debtor.”⁷⁴
2. The Bankruptcy Court was subsequently reversed by the District Court in *In re Pratola*, No. 18-CV-213, 2018 WL 4181498 (N.D. Ill. Aug. 31, 2018). There, the court found that section 109(e)'s plain meaning prohibited the Debtor from being eligible for chapter 13 protection, and that such ineligibility constituted “cause” for dismissal or conversion under section 1307(c). It found the Bankruptcy Court's reliance on policy considerations to have been inappropriate in light of section 109(e)'s plain requirements. It remanded the proceeding back down to the Bankruptcy Court to determine which of either dismissal or conversion would be in the best interests of creditors and the estate.

⁶⁹ *In re Pratola*, 578 B.R. 414, 422 (Bankr. N.D. Ill. 2017).

⁷⁰ *Id.* at 419.

⁷¹ *Id.* at 420.

⁷² *Id.* at 421.

⁷³ *Id.* at 421–22.

⁷⁴ *Id.* at 422 (internal citations and quotations omitted).

VIII. The ABI's *recommended* interpretation of the *Brunner* test:⁷⁵

1. *Brunner Test*. The three-factor *Brunner* test should be understood to require the debtor to establish only that:
 - a. The debtor cannot pay the student loan sought to be discharged according to its standard ten-year contractual schedule while maintaining a reasonable standard of living;
 - b. The debtor will not be able to pay the loan in full within its initial contractual payment period (10 years is the standard repayment period) during the balance of the contractual term, while maintaining a reasonable standard of living; and
 - c. The debtor has not acted in bad faith in failing to pay the loan prior to the bankruptcy filing.
2. *Standard of Proof*. Each of these factors should be understood to require proof by a preponderance of the evidence.
3. *Appellate Review*. The determination of the bankruptcy court as to each of the factors should be recognized as a finding of fact subject to deference in appellate review and in the consideration of appeal by the Department of Education, any guaranty agency, eligible lender, or holder of a federal student loan, and any agent of these parties.

IX. Income Based Repayment Program Discharge and the Bankruptcy Discharge

1. Outside of bankruptcy, a student loan borrower with federal loans may take advantage of programs wherein the borrower pays only a percentage of their income – roughly 10-15 percent – for anywhere from 20-25 years.⁷⁶ At the end of the 20-25 year period, the loan debt is forgiven and the borrower is relieved from any obligation to pay it, much as they would be if the debt had been discharged in bankruptcy.
2. The discharge differs only in the tax consequences. The amount of the debt forgiven will be taxable income recognized in the year that the debt is forgiven under the income-based repayment program (IBR program), unless the individual is insolvent.⁷⁷ If the individual is insolvent, the tax is effectively deferred and is treated as reduction in the basis of any assets that the taxpayer holds in the tax year immediately following the tax year in which the remaining loan balance had been discharged.⁷⁸
3. Other than the insolvency exception, an exception also exists for a discharge of indebtedness that “occurs in a title 11 case.”⁷⁹ It works the same way; instead of owing tax in the year of discharge, other favorable tax attributes (such as capital loss carryovers or tax basis in assets) are reduced. How can forgiveness under an IBR program also result in a discharge that “occurs in a title 11 case”?
4. It is possible for a debtor to enter into a stipulated or agreed order in a section 523(a)(8) adversary proceeding whereby the debtor and the government lender agree that the debtor

⁷⁵ AMERICAN BANKRUPTCY INSTITUTE’S COMMISSION ON CONSUMER BANKRUPTCY, RECOMMENDATIONS TO THE DEP’T OF EDUCATION: EVALUATING UNDUE HARDSHIP CLAIMS IN ADVERSARY ACTIONS SEEKING STUDENT LOAN DISCHARGE IN BANKRUPTCY PROCEEDINGS 2 (2018).

⁷⁶ See generally 20 U.S.C. § 1098e.

⁷⁷ I.R.C. §§ 61(a)(12), 108(a)(1)(B).

⁷⁸ I.R.C. §§ 108(b)(1), (b)(2)(E), 1017(a). If the borrower has other favorable tax attributes such as capital loss carryovers from prior tax years or net operating losses, those will be reduced in the order provided for, and in the amounts provided for, in section 108. See I.R.C. § 108(b)(2)(A)–(D), (F)–(G), (b)(3).

⁷⁹ I.R.C. § 108(a)(1)(A).

will use an IBR program to pay off the debt, but that the debt, when discharged in 20-25 years under the IBR program, will be “deemed” to have been discharged in the debtor’s bankruptcy.⁸⁰

- a. The government lender ostensibly wants to avoid a hardship discharge in the bankruptcy, and the debtor wants to avoid the “tax bomb” that comes along with using an IBR program. Both sides are happy if the debtor is ordered to participate in an IBR program with the benefit that the discharge at the end of the long 20–25 year road will be “deemed” to have occurred in the debtor’s bankruptcy case, thus avoiding the IBR “tax bomb.”
- b. “For purposes of this section, the term ‘title 11 case’ means a case under title 11 of the United States Code (relating to bankruptcy), but only if the taxpayer is under the jurisdiction of the court in such case and the discharge of indebtedness is granted by the court or is pursuant to a plan approved by the court.”⁸¹
 - i. Is the discharge “granted by the court” if a stipulated judgment is entered in the 523(a)(8) adversary proceeding stating that the IBR discharge will be “deemed” to have occurred in the debtor’s bankruptcy case? The Supreme Court has stated that section 523(a)(8) debts may only be discharged if the court affirmatively makes a hardship determination, though that determination may be made based off of stipulated facts if there is no contest.⁸²
 - ii. Would such a stipulated judgment, entered into by, *e.g.*, the Department of Education, bind the IRS if it is not made a party to the adversary proceeding?⁸³

X. Discharge in Bankruptcy at the Conclusion of IBR.

1. *In re Brunell*, 356 B.R. 567 (Bankr. D. Mass. 2006).
 - a. Bankruptcy court held that highly educated, 41-year-old chapter 7 debtor who was in good health and gainfully employed was not entitled to “undue hardship” discharge of her more than \$200,000 student loan debt, but that at the conclusion of her Income Contingent Repayment Plan the income tax liability owing on account of the IBR discharge would be discharged under section 105, as the income tax consequences at that time in the Debtor’s life (at or nearing retirement) would be an “undue hardship”.
 - b. See also, attached stipulation in *Garner v. United States Department of Education*.

⁸⁰ See Attachment # 2. In particular, see ¶¶ 9 & 14.

⁸¹ I.R.C. § 108(d)(2).

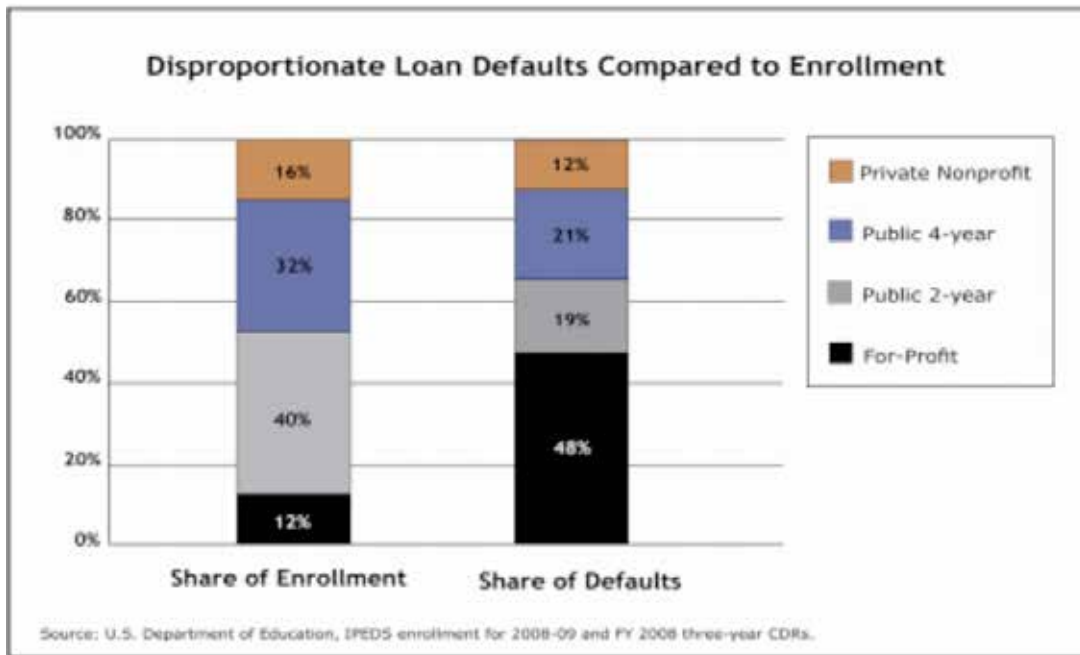
⁸² *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440, 450 (2004) (“Unless the debtor affirmatively secures a *hardship determination*, the discharge order will not include a student loan debt.”) (emphasis added); *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260, 278 (2010) (“Neither the Code nor the Rules prevent the parties from stipulating to the underlying facts of undue hardship, and neither prevents the creditor from waiving service of a summons and complaint. . . . But, to comply with § 523(a)(8)’s directive, the bankruptcy court *must make an independent determination of undue hardship* . . .”) (emphasis added).

⁸³ 18A WRIGHT & MILLER, FEDERAL PRACTICE & PROCEDURE § 4458 (2d ed. 2018) (“The general rule is that litigation by one agency is binding on other agencies of the same government, but exceptions may be warranted if there are important differences in the authority of the respective agencies.”).

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- XI. At Least One Other Way to Discharge Student Debt Outside of Bankruptcy
 - 1. Borrower Defense to Repayment:
 - a. If the borrower of a federal loan can show that they would have a successful cause of action under state law against the school they attended, the government will forgive part or all of the loan and may then recoup the money from the school.⁸⁴
 - b. These regulations are the subject of a proposed revision substituting a new, somewhat more onerous uniform federal standard requiring a showing of a misrepresentation and that the school had some knowledge or acted recklessly regarding the truth of its representation.⁸⁵

Attachment # 1:



⁸⁴ 34 C.F.R. § 685.206(c).

⁸⁵ 83 Fed. Reg. 37242-01 (July 31, 2018).

Attachment # 2:

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DISTRICT OF OREGON

FILED

August 03, 2016

Clerk, U.S. Bankruptcy Court

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Below is a Judgment of the Court. If the judgment is for money, the applicable judgment interest rate is: Not applicable.


TRISH M. BROWN
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
DISTRICT OF OREGON

<p>In re LORETHA GARNER, Debtor</p>	<p>Case No. 15-34733-tmb7 Adv. Proc. No. 16-03002-tmb</p>
<p>LORETHA GARNER, Plaintiff, vs. UNITED STATES DEPARTMENT OF EDUCATION, NELNET Defendants.</p>	<p>STIPULATED JUDGMENT</p>

It is hereby stipulated and agreed, by and between Loretha Garner ("Ms. Garner") ("Plaintiff") and Defendant United States Department of Education ("DOE"), that the following facts are true:

1. On October 8, 2015, Plaintiff filed a voluntary petition for relief under Chapter 7 of the

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1 United States Bankruptcy Code, and a discharge of eligible debts was entered on March 16,
2 2015.

3 2. Plaintiff commenced this adversary proceeding on January 7, 2016, naming, *inter alia*, DOE
4 as a defendant, by filing a complaint to discharge her student loan debt on the ground that it
5 imposes an undue hardship pursuant to 11 U.S.C. § 523(a)(8).

6 3. Plaintiff is indebted to DOE pursuant to the following Loan Applications and Promissory
7 Notes ("Notes") executed by Plaintiff;

- 8 a. June 24, 2012 Federal Direct Stafford Master Promissory Note.
- 9 b. September 22, 2015 Federal Direct PLUS Loan Master Promissory Note.

10 4. On the following loans were consolidated pursuant to the Notes, in the principal amounts of,
11 interest rates, and loan types ("Student Loans");

	Disbursement Date	Amount	Interest Rate	Loan Type
12 1.	8/23/2012	\$23,798.95	5.75	Direct Consolidation
13 2.	8/23/2012	\$46,784.49	5.75	Direct Consolidation
14 3.	12/25/2015	\$2,126.00	4.66	Direct Plus

15
16 Certain interest that has accrued on the Student Loans has been capitalized. As of June 30,
17 2016, the total amount due in principal and interest on the Student Loans is \$84,966.21. This
18 amount does not take into account the Direct Plus Loan which is specifically exempt from
19 this stipulation and proceeding.

20 5. In order to resolve this matter without the need for further litigation, the parties agree that
21 Plaintiff will make payments to DOE pursuant to the repayment plan described herein on her
22 Student Loan obligations and that dismissal with prejudice of the adversary proceeding
23 against DOE is appropriate under the circumstances set forth below.

24 6. Within 30 days of entry of a Court order approving this Stipulation, Plaintiff shall apply for
25 repayment of her Student Loans under DOE's Revised Pay As You Earn ("REPAYE") plan.
26 In applying for REPAYE, Plaintiff shall complete all necessary income-related
27 documentation. Plaintiff must provide this documentation to DOE within 30 days of entry of
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- 1 a Court order approving this Stipulation.
- 2 7. Commencing on September 1, 2016, or a later date if additional information is needed,
- 3 Plaintiff's monthly payment will be calculated pursuant to the terms of REPAYE presently
- 4 set forth in 34 C.F.R. Part 685.209(c). Specifically, Plaintiff's monthly payment amount will
- 5 be calculated based upon Plaintiff's discretionary income, limited to no more than 10 percent
- 6 of the amount by which Plaintiff's adjusted gross income exceeds 150 percent (150%) of the
- 7 poverty guideline applicable to Plaintiff's family size, divided by 12, as set forth in 34 C.F.R.
- 8 Part 685.209(c)(2).
- 9 8. Each monthly payment must be made no later than the first (1st) day of each month
- 10 ("Monthly Payment Due Date"), with an allowance of a thirty (30) day grace period for each
- 11 such monthly payment.
- 12 9. The term of Plaintiff's REPAYE plan is 20 years or 240 separate qualifying monthly
- 13 payments not to include periods of deferment or forbearance. If Plaintiff complies with all
- 14 terms and conditions of this Stipulation and the REPAYE plan, including, but not limited to,
- 15 providing requested information, timely recertifying her income annually as required under
- 16 34 C.F.R. Part 685.209(c)(4), timely making the requisite payments, and not defaulting on
- 17 her Student Loan, then at the end of the term of Plaintiff's REPAYE plan, a more favorable
- 18 plan, or variant thereof, any remaining obligation on her Student Loans will be deemed
- 19 discharged in bankruptcy.
- 20 10. Payment default will occur if DOE receives any monthly payment in excess of thirty (30)
- 21 days after its Monthly Payment Due Date or if Plaintiff fails to comply with the annual
- 22 recertification guidelines of REPAYE as outlined in 34 C.F.R. Part 685.209(c)(4). If this
- 23 occurs, Plaintiff ceases to be eligible for discharge after 240 qualifying payments. In the
- 24 event Plaintiff defaults on her Student Loan or any term of this Stipulation, then this
- 25 Stipulation shall become null and void, and all of the original terms of the Student Loan shall
- 26 again be in effect and DOE will be entitled to recover the original amount of the Student
- 27 Loan, including unpaid interest, accrued interest, and regulatory collection costs if
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- 1 applicable, less any payments Plaintiff has made.
- 2 11. Should DOE fail to provide a monthly reminder notice or receipt for payment to Plaintiff,
3 this does not relieve Plaintiff of her obligation and agreement to make consecutive, timely,
4 monthly payments under REPAYE.
- 5 12. Plaintiff may at any time choose to repay her student loan obligations to DOE in full or in
6 part ahead of schedule without prepayment penalty.
- 7 13. Should a more favorable plan, or variant thereof, become available for Plaintiff via DOE,
8 Plaintiff may apply for that program. If Plaintiff does apply for, and is accepted to, a more
9 favorable plan, all payments made pursuant to this stipulation will not count toward payment
10 period requirements for successful completion of any new plan or variant thereof.
- 11 14. Should Plaintiff apply for, or be accepted to, a more favorable plan via DOE, and if Plaintiff
12 complies with all terms and conditions of this Stipulation and the more favorable plan,
13 including, but not limited to, providing requested information, timely recertifying her income
14 annually as required, timely making the requisite payments, and not defaulting on her
15 Student Loans, then at the end of the term of Plaintiff's more favorable plan, or variant
16 thereof, any remaining obligation on her Student Loans will be deemed discharged in
17 bankruptcy.
- 18 15. If any provision of this Stipulation is held invalid, illegal, or unenforceable, the validity,
19 legality, and enforceability of the remaining provisions shall not in any way be affected or
20 impaired thereby.
- 21 16. This Stipulation may not be altered, modified or otherwise changed in any respect except in
22 writing, duly executed by all of the parties or their authorized representatives. Any attempted
23 oral or implied amendment, modification, or waiver shall be null and void.
- 24 17. Except as provided in this Stipulation, all other terms of the Student Loans remain in effect
25 and are hereby incorporated by reference. To the extent that the terms of the Student Loans
26 conflict with the terms of this Stipulation, the terms in this Stipulation control.
- 27 18. The parties to this Stipulation acknowledge that they have been represented by independent
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counsel of their own choice or have chosen to not have their own counsel throughout all of the negotiations that have preceded the execution of this Stipulation.

19. This Stipulation shall constitute the entire agreement between the parties, and it is expressly understood and agreed that this Stipulation has been freely and voluntarily entered into by the parties hereto. The parties further acknowledge that no warranties or representations have been made on any subject other than as set forth in this Stipulation.

20. Each person signing this Stipulation warrants that he or she is fully authorized to sign this Stipulation on his or her behalf and on behalf of his or her respective predecessors, transferors, and/or assignors, and that the Stipulation is therefore binding upon and enforceable against the same.

21. The Stipulation is binding upon and inures to the benefit of the parties hereto and their respective heirs, executors, administrators, successors, and assigns.

22. The parties stipulate that this adversary proceeding be dismissed without prejudice, with each party to bear their own attorney's fees, costs and expenses. If Plaintiff's application for the REPAYE plan, is rejected or denied, or if Plaintiff's required initial payments under REPAYE are significantly in excess of the parties projected monthly payments of \$0.00, the parties agree that this adversary proceeding may be re-opened.

The parties to this Stipulation certify that they have read and fully understand its terms.

Based upon the stipulation of the parties set forth above, good cause having been shown,

IT IS HEREBY ORDERED AS FOLLOWS:

- 1. Ms. Garner's DOE Loan debt is not dischargeable pursuant to 11 U.S.C. § 523(a)(8) except as stipulated in the above paragraph nine (9) and fourteen (14), DOE is dismissed as a party to this action, and this action is dismissed without prejudice.
- 2. The parties shall bear their own costs and fees incurred in this proceeding.

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IT IS SO STIPULATED:

/s/ Kathleen L. Bickers
Kathleen L. Bickers
Attorney for Defendant, United States Department of Education

/s/ Loretha Garner
Loretha Garner
Plaintiff- Pro Se