INDEX OF MATERIALS BY PANEL

Thursday July 2, 2015

9:15-10:30 **The Supreme Court, Bankruptcy Courts' Authority and Jurisdiction:**
Recent Decisions of the U.S. Supreme Court and Their Impact on Bankruptcy Law Practice.
G. Eric Brunstad, Jr., Dechert LLP (Hartford, CT)

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Stern, _Arkison_, _Wellness_, Bankruptcy Jurisdiction, and the Requirements of Article III

Outline of History and Issues

I. Article III of the Federal Constitution

a. General provisions of Article III

1. Life-time tenure
2. Irreducible salary

b. History of Article III

1. English practice
2. The Constitutional Convention
3. The Federalist Papers

II. Bankruptcy Court Jurisdiction

a. Jurisdiction under the Bankruptcy Code as enacted in 1978 was initially vested in the bankruptcy courts under 28 U.S.C. § 1471; bankruptcy judges were not given life-time tenure or irreducible salary, but were given broad authority to decide all matters that (1) arise under the Code, (2) arise in a bankruptcy case, or (3) are related to a case.

b. *Northern Pipeline Constr. Co. v. Marathon*, 458 U.S. 50 (1982)

1. Breach of contract action
2. Exceptions to Article III

i. Territorial courts
ii. Courts martial
iii. Public-rights controversies

3. The Supreme Court determined that section 1471 was unconstitutional; the breach of contract action was a private-right controversy, not a dispute over a matter of public right, and so the bankruptcy judge could not finally decide it.
4. The decision articulated the idea that certain matters are "core" to the administration of bankruptcy cases, and others not.

c. Jurisdiction under the 1984 Amendments, 28 U.S.C. §§ 1334 & 157

1. Bankruptcy jurisdiction is vested in the district courts under section 1334, delegable to the bankruptcy judges in the district under section 157(a); bankruptcy judges are not given life-time tenure or irreducible salary.
2. Under section 157(b)(1), bankruptcy judges may finally decide "core" matters subject to ordinary appellate review under section 158; "core" matters are listed in section 157(b)(2).
3. Under section 157(c), bankruptcy judges may hear, but not finally determine "non-core" matters, absent the consent of the parties; in "non-core" matters where there is no consent, bankruptcy judges may issue proposed findings of fact and conclusions of law subject to *de novo* review in the district courts.
4. Section 157 is patterned after 28 U.S.C. § 636, governing the jurisdiction of magistrate judges.

d. The era of lingering doubts, 1984-2011

1. *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833 (1986)

   i. The case involved proceedings before the Commodity Futures Trading Commission; a litigant sought to proceed before the CFTC instead of the district court, then later asserted a right to an Article III judge after he was unhappy with the CFTC's determination.
   ii. The Supreme Court determined that a right to an Article III judge is primarily a personal right that may be waived.
   iii. As part of the Court's analysis, it indicated that the requirements of Article III also implicate inter-branch "structural" considerations.

2. *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989)

   i. In a bankruptcy action, the trustee sued the defendant for receipt of a fraudulent transfer; the defendant asserted a right to a jury trial.
   ii. The Supreme Court determined that a defendant who has not filed a proof of claim in the bankruptcy case has a right to a jury trial in a fraudulent transfer action.
   iii. As part of its reasoning, the Court stated that the constitutional analysis under the Seventh Amendment and the analysis under Article III is one and the same, suggesting that, if a litigant has a right to a jury trial under the Seventh Amendment, the litigant also has a right to an Article III judge.
   iv. Fraudulent transfer matters are listed as "core" under section 157(b)(2); the decision did not address directly whether a bankruptcy judge may finally determine a fraudulent transfer action consistent with the requirements of Article III, but the Court's reasoning suggested that a bankruptcy judge may not do so if, indeed, the analysis under Article III and the Seventh Amendment is the same, at least absent the parties' consent.

3. *Gomez v. United States*, 490 U.S. 858 (1989); *Peretz v. United States*, 501 U.S. 923 (1991)

    i. In *Gomez*, the Court addressed whether magistrate judges may conduct felony *voir dire*; to avoid a potential constitutional problem, the Court construed the relevant statutory authority not to include the power to conduct felony *voir dire.*
    ii. In *Peretz*, the Court considered whether magistrate judges may conduct felony *voire dire* with the consent of the parties: the Court concluded that they may.

4. *Langenkamp v. Culp*, 498 U.S. 42 (1989)

    i. The trustee asserted a bankruptcy preference action against a creditor in the bankruptcy court; preference actions are listed as "core" matters under section 157(b)(2).
    ii. The Supreme Court determined that the creditor waived any right to a jury trial in the action by filing the proof of claim.

5. *Roell v. Withrow*, 538 U.S. 58 (2003)

    i. A litigant waited until after losing his case before a magistrate judge to challenge the judge's exercise of jurisdiction based on an adversary's failure to consent to the judge's jurisdiction in the manner prescribed by the relevant rules.
    ii. The Supreme Court determined that the litigant waived any objection by failing to assert it until the end of the litigation; the Court determined that the relevant statutory provision required only consent, not express consent, and thus implied consent by conduct was sufficient.

e. *Stern v. Marshall*, 131 S. Ct. 2594 (2011)

1. The case involved the saga of the late Anna Nicole Smith (a/k/a Vickie Lynn Marshall); Vickie filed for bankruptcy in California.
2. Pierce Marshall filed a proof of claim in the bankruptcy court for a state-law defamation liability; Vickie filed a state-law counterclaim against Pierce for alleged tortious interference with a gift.
3. A counterclaim against a creditor who has filed a proof of claim is listed as a "core" matter under section 157(b)(2).
4. The bankruptcy judge finally decided the matter; the district court, however, vacated the final judgment, and the Ninth Circuit affirmed the vacatur.
5. The Supreme Court determined that the bankruptcy judge had statutory authority to finally decide the matter, but not constitutional authority because Vickie's state-law tortious interference claim was essentially the same for Article III purposes as

the breach of contract action in *Marathon*; the claim did not "stem from" the bankruptcy.

6. The Court reaffirmed *Granfinanciera*.
7. The Court distinguished *Langenkamp*; filing a proof of claim only supports implied consent with respect to necessarily intertwined counterclaims; Vickie's counterclaim was independent of Pierce's claim.

f. *Executive Benefits Ins. Agency v. Arkison*, 134 S. Ct. 2165 (2014)

1. The trustee brought a fraudulent transfer action against the defendant in the bankruptcy court.
2. A fraudulent transfer action is listed as a "core" matter under section 157(b)(2).
3. After losing on summary judgment in the bankruptcy court and losing his appeal in the district court, the defendant asserted unsuccessfully in the Ninth Circuit that the bankruptcy judge could not finally decide the matter under *Stern*; the Ninth Circuit determined that:

    i. Although a fraudulent transfer action is listed as a "core" matter under section 157(b)(2), a bankruptcy judge may not finally decide it consistent with the requirements of Article III because, following *Granfinanciera* as reaffirmed in *Stern*, a fraudulent transfer action does not involve a matter of public right, but rather constitutes a private-right controversy.
    ii. Even though the bankruptcy judge should not have finally decide the matter, the district judge's exercise of *de novo* review (standard in the summary judgment context) cured any Article III problem.
    iii. In addition, the defendant impliedly consented to the adjudication of the matter in the bankruptcy court by his litigation conduct, thereby foregoing any Article III objection.
    iv. There is no "statutory gap" in section 157—a private-right controversy designated as a "core" matter under section 157(b)(2) that a bankruptcy judge may not finally decide consistent with the requirements of Article III may be treated as a "non-core" matter under section 157(c) and the bankruptcy judge's judgment and opinion may be treated as proposed findings of facts and conclusions of law subject to *de novo* review.

3. The Supreme Court determined that:

    i. So-called "*Stern* claims"—matters designated as "core" under section 157(b)(2) that a bankruptcy judge may not finally decide consistent with the requirements of Article III, may be treated as "non-core" matters under section 157(c), and thus there is no "statutory gap" in section 157.
    ii. Assuming without deciding that a fraudulent transfer action constitutes a "*Stern* claim," the district court's *de novo* review of the bankruptcy court's summary judgment determination cured any problem under Article III.

iii. The Court did not reach the consent issue.

g. *Wellness Internat'l Network, Ltd. v. Sharif*, no. 13-935 (2015)

1. The Circuits are divided on whether a litigant's consent, express or implied, is sufficient to permit a bankruptcy judge to finally decide a "*Stern* claim" consistent with the requirements of Article III.
2. In *Wellness*, the debtor disputed whether certain property in his possession constituted property of his bankruptcy estate, claiming that he did not own it, but rather held it in trust for someone else; the bankruptcy judge entered a default judgment, determining that the property belonged to him and was thus property of his bankruptcy estate, and the judge also entered an order denying the debtor a bankruptcy discharge.
3. The determination of matters regarding the administration of the estate and affecting the assets of the estate is designated as "core" under section 157; likewise the determination of the debtor's right to a discharge is designated as "core."
4. The Seventh Circuit determined:

    i. The denial of the debtor's discharge was a matter that "stemmed from" the bankruptcy itself and was thus something the bankruptcy judge could finally decide consistent with the requirements of Article III.
    ii. Whether property in the debtor's possession belonged to him, and thus passed to his bankruptcy estate, turned on consideration of state law, and constituted a "*Stern* claim."
    iii. Litigant consent is insufficient to waive a right to an Article III judge in federal court because the requirements of Article III are primarily structural in nature and cannot be waived.

4. The Supreme Court granted certiorari to address:

    i. Whether the bankruptcy court could finally decide that property in the debtor's possession constituted property of his bankruptcy estate consistent with the requirements of Article III.
    ii. If not, whether a litigant may consent to the bankruptcy court's final determination of the matter, subject to ordinary appellate review, and whether the necessary consent may be express or implied.

Thursday July 2, 2015

11:00-12:00 **Things Learned From the Practice of Law with Emphasis on Ethics and Professionalism.**

Honorable Ralph R. Mabey (Retired), Kirton McConkie/Professor of Law, University of Utah S.J. Quinney College of Law (Salt Lake City, UT)

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Life's Lessons from the Law: Ethics, Justice and Mercy

Hon. Ralph R. Mabey (Ret.)

Kirton McConkie

Professor of Law, University of Utah,
S.J. Quinney College of Law

NACTT 50th Anniversary Educational Program 2015

Salt Lake City

Les Miserables

by

Victor Hugo

- Javert: the straight line of the law
- Jean Valjean: the straight line of mercy

On the facts presented to Javert, justice and mercy were irreconcilable

In the teeth of the irreconcilable demands of justice and mercy Javert took his own life

Balancing Mercy and Justice is An Ennobling Endeavor:

- “Mercy does not destroy Justice, but achieves its perfect fulfillment. Mercy without Justice is the mother of chaos; Justice without Mercy is the father of cruelty.”
  Thomas Aquinas

Justice & Mercy by Glynn Acree at Cumberland School of Law. [The statue grew out of a phrase, "Seek wisdom to temper justice with compassion". The concept is the Angel of Mercy is encouraging Lady Justice to stay the sword from being used too swiftly, tempering it with compassion.]

Chapter 13:

An imperfect congressional mandate to reconcile justice and mercy--or as BAPCPA puts it reconciling:

Bankruptcy Abuse Prevention and Consumer Protection

Chapter 13

JUSTICE

Creditors

- All income and assets accounted for to maximize return to creditors
- Secured creditor's right to value-equivalence of collateral
- Home mortgage and 910-car lenders protected from modification
- Taxes and DSO paid in full
- Unsecured creditor's right to projected disposable income
- Debtor's increase in income over 3-5 years may be required to increase return to creditors.
- Relief from stay or dismissal for failure to comply with plan
- Non-dischargeability protection against dishonesty

MERCY

Debtors

- Relief from collection pressures
- Protection of home & cars as necessary for family & work
- Protection of income that is reasonably necessary for maintenance & support of household
- Protection of expenses for care of aged, ill, or disabled family members
- Protection of children's school expenses
- Protection of Social Security income
- Possible protection of retirement contributions
- Protection of charitable contributions
- Honesty and good faith rewarded
- Fresh start

Chapter 13 Trustee

JUSTICE

- Investigate Debtor's financial affairs
- Verify and account for Debtor's income and assets
- Ensure Debtor's compliance with Code & plan requirements
- Distribute to unsecured creditors all of Debtor's projected disposable income
- Assess and monitor Debtor's compliance, honesty and good faith
- Where appropriate enforce the law <u>against</u> the Debtor

MERCY

- Advise the Debtor (other than on legal matters)
- Assist the Debtor in performance under the plan
- Provide Debtor with the resources and information necessary to successfully complete the plan
- Review creditors' claims for accuracy
- Ensure Creditors properly apply plan payments.
- Verify the Debtor obtains financial management instruction
- Where appropriate enforce the law <u>for</u> the Debtor

Chapter 13 Debtor's Counsel

JUSTICE

- Co-guarantor of Debtor's honesty and good faith
- Ensure Debtor's compliance with required plan provisions and budget allotments
- Financial management training
- Reality, moderation and prudence

MERCY

- Help Debtor make hard choices for long-term benefit
- Advocate for the best deal with creditors & trustee
- Carefully protect the Debtor's interests in:
  - Assets
  - Income
  - Fresh start

Chapter 13 Creditor's Counsel

JUSTICE

- Extract the uttermost farthing
- Advocate Debtor's accountability
- Advocate Creditor's repayment
- Enforce the law against the Debtor

MERCY

- Accept plan modifications so debtor can continue with payments & retain collateral
- Balance plan repayment against repo of collateral
- Weigh long term economic gain over short term economic gain
- Weigh rehabilitation of a customer, entrepreneur, or a family

The Law of Chapter 13:

Reconciling and Unifying the Interest of Debtors, Creditors, and the Nation's Economic Prosperity

Just One More Meaning of Our Nation's Motto: *E Pluribus Unum/OUT OF MANY ONE*

And perhaps not coincidentally, the motto that appears on all US coinage.

Life's Lessons from the Law: Personal Characteristics

An arrogant lawyer is a loaded revolver, a humble lawyer is a problem solver.

- Pride obscures judgment and weakens our ability to listen, analyze and assess.
- Humility sharpens our observations, strengthens our judgment and gets our egos out of the way.
- "The…qualities which I am groping to characterize are…what compendiously might be called dominating humility."

  Justice Felix Frankfurter

A lawyer's rhetoric is more likely to impress herself than anybody else.

- It just sounds so clever when we say it ourselves.
- But lucidity trumps loquacity.
- And joke-telling is dangerous: The safest joke to tell is the one on you.

Exceptional preparation beats exceptional intellect.

- Good lawyering is earned not bequeathed.

Prompt disclosure is often the best disinfectant.

- Prompt disclosure of your shortcomings to your client minimizes the risk of being sued.
- Prompt disclosure to the court minimizes the risk of being held in contempt.
- Prompt disclosure to the public minimizes the risk of being held in public contempt.

Fiduciary Duty is easier to offend than it is to define

- Courts have 20-20 hindsight
- A “punctilio of an honor most sensitive”?!
- You and yours vs me and my fee
- Are you practicing law or is your paralegal?
- When in doubt, be your better self

Human justice is imperfect justice

- While it is our job to improve it, human justice may fall short.
- Those despitefully used are not promised treble damages.
- Consider settling.

A lawyer's fear of leaving a dollar on the table usually costs his client more than a dollar.

- As a result, to measure your success by your opponent's failure is a double-negative: hers and yours.

The Constitution and the law only recite our rights and freedoms; the lawyer earns them

- Constitutional and legal rights are not self-executing.
- We must often earn the benefits of the Constitution and the law for our clients.

A lawyer who files a responsive pleading a day early is a lawyer who miscounted.

- Lawyer procrastination is endemic and epidemic

Lawyers are an insecure lot

- either their practice is too busy and they fear malpractice or too slow and they fear unemployment.
- A law practice breeds insecurity because outcomes and opportunities are sometimes hard to predict.

Scheduling a law practice is as difficult as scheduling the weather; it is going to snow you in at the wrong time.

- Since you can't change the weather, enjoy it. Being snowed in can be pretty, and pretty exciting.

Practicing law is like fasting: it can be good for the soul-until it kills you

- Balance is the point. Avoid too much of a good thing.

Thursday July 2, 2015

1:30-2:30 **Who, What, When, Where? Notice Issues and Developments in Chapter 13 Procedure.**

Moderator: Elizabeth F. Rojas, Chapter 13 Standing Trustee for the Central District of California, Northern Division (Sherman Oaks)

Honorable R. Kimball Mosier, United States Bankruptcy Judge for the District of Utah (Salt Lake City)

Lawrence R. Ahern, III, Brown & Ahern (Nashville, TN)

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1. Who, What, When, Where? Notice Issues and Developments in Chapter 13 Procedure

B. Implementation by the rules
C. Notice by publication and disposition without a hearing
D. Service on attorneys

VII. Ex parte communications
VIII. Notices after conversion

Appendices Rules of Procedure

A. Rule 2002
B. Rule 7004 and Civil Rules 4 and 4.1
C. Rule 7005 and Civil Rule 5
D. Rule 9006

2. PowerPoint Presentation in PDF Format

WHO, WHAT, WHEN, WHERE?

Notice Issues and Development in Chapter 13 Procedures

NACTT Salt Lake City
Panel 14
July 2, 2015
1:30pm-2:30pm

Introduction

- Elizabeth F. Rojas, Chapter 13 Trustee, Moderator
- Lawrence R. Ahern III, Attorney at Law
- Honorable R. Kimball Mosier, United States Bankruptcy Judge

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An Overview of Different Types of Proceedings

Lawrence, R. Ahern III
Attorney at Law

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Main Sources of Rules Governing Chapter 13 Procedures

- Due Process
  - U.S. Constitution, Amendment V
- Statues – Bankruptcy Code
  - Rules of Construction
  - Notice
  - Debtor's Duties

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Main Sources of Rules Governing Chapter 13 Procedures

- Federal Rules of Bankruptcy Procedure
  - Lists, Schedules, Statements, and Other Documents; Time Limits
  - Dismissal or Conversion of Case; Suspension
  - Conversions to Chapter 7 Liquidation Case
  - Notices to Creditors, Equity Security Holders, Administrators in Foreign Proceedings, Persons Against Whom Provisional Relief is Sought in Ancillary and Other Cross-Border Cases, United States, and United States Trustee
  - Objections to Claims
  - Use, Sale, or Lease of Property
  - Process; Service of Summons, Complaint
  - Service and Filing of Pleadings and Other Papers
  - Prohibition of Ex Parte Contacts
  - Computing and Extending Time; Time for Motion Papers
  - General Authority to Regulate Notices
  - Service or Notice by Publication
  - Representation and Appearances; Powers of Attorney
  - Motions: Form and Service
  - Contested Matters

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Main Sources of Rules Governing Chapter 13 Procedures

- Federal Rules of Civil Procedure
  - Summons
  - Serving and Filing Pleadings and Other Papers
- Local Rules
- Case Law
  - City of New York v. New York (1953)
  - Mullane v. Central Hanover Bank & Trust Co. (1950)
  - Peralta v. Heights Medical Center, Inc. (1988)
  - Tulsa Professional Collection Services, Inc. v. Pope (1988)

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Overview of Basic Notice Rules

- Petition and related papers
  - Rule 2002 governs "notice" of general matters that typically concern all parties
- Adversary proceedings
  - Rule 7004 governs "service" of matters that typically involve only certain parties

7

Overview of Basic Notice Rules

- Contested matters
  - Rule 7004 is applied to contested matters by Rule 9014
  - Pursuant to Rule 9014(b), a "motion" must be served "in the manner provided for service of a summons and compliant to Rule 7004"
- Claim objections
  - The service requirements of Rules 9014(b), 7004, and claim objections

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A Judge's Perspective

Honorable R. Kimball Mosier
United States Bankruptcy Judge

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A Judge's Perspective

- Bankruptcy is a "notice" practice and an opportunity to be heard
- Specific issues and examples:
  - Lien strips
  - Plan modifications
  - Objections to plans
  - Objections to discharge
  - Objections to claims

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- Questions & Answers
- Scenarios
  - Who? 
  - What? 
  - When? 
  - Where? 

Elizabeth F. Rojas, Chapter 13 Trustee

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Thursday July 2, 2015

1:30-2:30 **Chapter 13 Trustee's Avoidance Powers - Preferences and Fraudulent Transfers:** What Do Trustees Look For, When Is Avoidance Worthwhile, and What Is the Debtor's Role?
Moderator: David G. Peake, Chapter 13 Standing Trustee for the Southern District of Texas (Houston)
Honorable John P. Gustafson, United States Bankruptcy Judge for the Northern District of Ohio (Toledo)
Cathy Moran, The Moran Law Group (Mt. View, CA)

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Avoidance Powers In Chapter 13

John P. Gustafson, United States Bankruptcy Judge, Northern District of Ohio, Western Division
Cathy Moran, Attorney at Law
David G. Peake, Chapter 13 Trustee

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Some Perspective: Chapter 7, Chapter 11 and Chapter 12

- In Chapter 7 cases, the avoidance rights generally have been under the exclusive control of the Chapter 7 Trustee. Debtors had rights under §522(f), because those avoidance rights are given to the debtors, and under the limited rights granted by §522(h).
- Historically, many courts limited §506 avoidance actions to the "reorganization" sections, based on the holding *in Dewsnup v. Timm*, 502 U.S. 401, 112 S.Ct. 773 (1992). That may change, depending on the Supreme Court's decision in the Chapter 7 lien stripping case *Caulkett/Toledo-Cardona*.

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- In contrast, in Chapter 11 cases, the Debtor-In-Possession is statutorily defined as having most of the rights and duties of a "trustee". See, §1107(a). Thus, the DIP is capable of using all of the avoidance rights that a "trustee" could use - at least until an actual trustee is appointed by the court. *See*, §1101(1); §1107(a).
- Similarly, in Chapter 12, Section 1203 confers avoidance powers on debtors by making a Chapter 12 debtor the equivalent (except for certain investigatory duties) to a debtor-in possession in Chapter 11.
- There is less statutory clarity in Chapter 13. "[N]either the trustee nor the debtor have explicit authority under Chapter 13 to bring avoidance actions." *In re Hansen*, 332 B.R. 8, 14 (10th Cir. BAP 2005). It has been held that a Chapter 13 Trustee "is no mere disbursing agent". *Matter of Maddox*, 15 F.3d 1347, 1355 (5th Cir. 1994). But the exact relationship, and division of powers, between the Chapter 13 Trustee and the Debtor, is less clear than in Chapter 7 and Chapter 11 cases.

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Looking At The Provisions Of Chapter 13

- **Section 1302(b) - Chapter 13 Trustee Duties.**
- Section 1302(b) states:

  (b) The trustee shall--

  (1) perform the duties specified in sections 704(a)(2), 704(a)(3), 704(a)(4), 704(a)(5), 704(a)(6), 704(a)(7), and 704(a)(9) of this title;
- However, the listed sections of §704 does not discuss the powers or duty of a trustee to prosecute avoidance actions. Arguably, that provision is found in §704(a)(1), which makes it a duty of a Chapter 7 trustee to "collect and reduce to money the property of the estate ...."
- Section 1302(b) does not make this one of the duties of a Chapter 13 Trustee- it is simply not on the list.

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Section 1303 -Debtor's Rights And Powers "Exclusive Of The Trustee".

- Section 1303, which defines the rights and powers of a Chapter 13 debtor, lists very specific provisions where debtors have exclusive rights.
  - Section 1303 states:
- Subject to any limitations on a trustee under this chapter, the debtor shall have, exclusive of the trustee, the rights and powers of a trustee under sections
- 363(b), 363(d), 363(e), 363(f), and 363(1), of this title.

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- "Section 1303, which defines the rights and powers of a Chapter 13 debtor, lists very specific provisions where debtors have exclusive rights. Avoiding powers are not among them." *In re Hansen*, 332 B.R. 8, 12 (10th Cir. BAP 2005).
- "In *Hartford Underwriters Ins. Co. v. Union Planters Bank*, the United States Supreme Court held that, in the context of the bankruptcy code, where a statute 'names the parties granted the right to invoke its provisions, ... such parties only may act.' 530 U.S. 1, 6, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000)." *In re Lee*, 432 B.R. 212, 215 (D.S.C. 2010); *see also*, *In re Wood*, 301 B.R. 558, 562 (Bankr.W.D. Mo. 2003)("Significantly, under the rule of *inclusio unius est exclusio alterius*, the plain language of §547(b) states the "trustee may avoid" preferential transfers-no mention is made in the statute about the debtor having similar rights.").

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- The way that Congress gave debtors the power to exercise the avoidance rights of a trustee in Chapter 11 and Chapter 12 were much more direct than the "inference" argument that can be made for debtor standing using §1303.
- Finally, because the rights of a Chapter 13 Debtor under §1303 are "exclusive of the trustee" - does a finding of Debtor standing to exercise avoidance powers mean that Chapter 13 trustees do NOT have avoidance powers?

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Working Backward From The Rest Of The Code To Chapter 13 Section 103(a)

The argument from §103(a) is: the avoidance sections state that they may be used by the "trustee". Nothing in Chapter 13 itself limits that power. And, §103(a) specifically makes the provision of Chapter 5- such as §§544, 547 and 548- applicable in Chapter 13 cases.

- This argument from Section 103(a) appears to be the dominant factor in the majority of case law that holds that Chapter 13 Trustees have standing to use avoidance powers.

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Case Law On Chapter 13 Trustees' Avoidance Powers

- **Chapter 13 Trustees Have The Power To Avoid Transfers Using 544-549.**
- "There is general agreement that the Chapter 13 trustee has standing to avoid transfers and recover property under §§ 544 (strong-arm power), 547 (preferences),' 548 (fraudulent conveyance) and 549 (post-petition transfers)."
- Keith M. Lundin & William H. Brown, *Chapter 13 Bankruptcy*, 4th Edition, §60.1, at1, Sec. Rev. June 10, 2004, www.Ch13online.com.
- Courts generally hold that a Chapter 13 Trustee can exercise avoidance powers:

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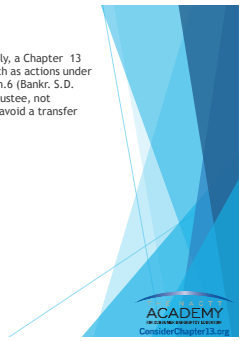
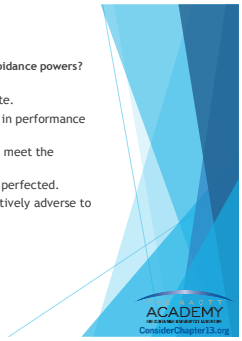
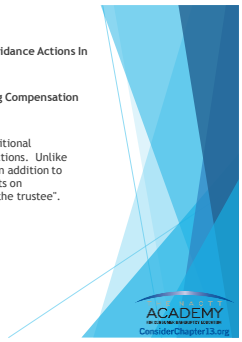
- *In re McCarthy*, 501 B.R. 89, 91 (8th Cir. BAP 2013)("Generally, a Chapter 13 trustee has standing to bring certain avoidance actions, such as actions under Bankruptcy Code §545(2)"); *In re Geraci*, 507 B.R. 224, 230 n.6 (Bankr. S.D. Ohio 2014)(Section 544(a) is "unambiguous and grants the trustee, not debtors, the powers and rights of a bona fide purchaser" to avoid a transfer of an interest in property or to defeat a mortgage.



- **When should Chapter 13 Trustees consider using their avoidance powers?**
- 1. Where the avoidance action will benefit the estate.
- 2. When the avoidance action will assist the Debtor in performance under the Plan.
- 3. If avoidance is necessary if the Debtor is going to meet the requirements of the Best Interest Test.
- 4. In cases where a security interest is not properly perfected.
- 5. When the Debtor has no incentive to act, or is actively adverse to the avoidance action.
- 6. Others?



- **Problems In Creating A Benefit To The Estate Through Avoidance Actions In Chapter 13.**
- **Problems Associated With Chapter 13 Trustees Obtaining Compensation For Work Done Litigating Avoidance Issues.**
- Chapter 13 Trustees face statutory barriers to receiving additional compensation for work undertaken in pursuing avoidance actions. Unlike Chapter 7 Trustees, where there are structural incentives (in addition to statutory duties) to bring avoidance actions, there are limits on compensation in Chapter 13 for work done as "attorney for the trustee".



The Statutory Basis For, And Against, A Chapter 13 Debtor Exercising Avoidance Powers.

- **Where There** Is No **Question** Re: **Debtor's Standing- Section 522(h)** & (g).
- **1. The Elements Of Section 522(h)**
- "Some courts have described §522(h) as being composed of five (5) elements: (1) the transfer was not a voluntary transfer of property by the debtor; (2) the debtor did not conceal the property; (3) the trustee did not attempt to avoid the transfer; (4) the transferred property is of a kind that the debtor would have been able to exempt from the estate if the trustee had avoided the transfer under §522(g); and (5) the debtor seeks to exercise one of the trustee's avoidance powers enumerated in §522(h); See *Matter of Hamilton*, 125 F.3d 292, 297 (5th Cir.1997); *In re DeMarah*, 62 F.3d 1248, 1250 (9th Cir.1995); *In re Steck*, 298 B.R. 244, 248-249 (Bankr.D.N.J.2003)." *In re Funches*, 381B.R. 471, 492 n.32 (Bankr. E.D. Pa. 2008).

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- **2. Does the Debtor have a right to claim an exemption in the property?**
- This will generally turn on two factors: I) is there an exemption applicable to the property in issue; and, 2) was the transfer of the property "voluntary"?
- **Debtors Have Standing To Litigate Non-522(h) Avoidance Actions - The "Holistic Approach" Of In re Cohen**
- At present, the leading case for Debtor standing, beyond that provided by Section 522(h), is *In re Cohen*, 305 B.R. 886 (9th Cir. BAP 2004).

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- **The Majority Of Courts Reject The Cohen Analysis.**
- 1. Why create that limited right if a larger general right to use avoidance powers was intended?
- 2. The plain language of the avoidance provisions apply to Trustees, not Debtors. And, unlike in Chapter 11 and 12, there is no similar clear provision (other than Section 522(h)) that gives Debtors the power to use those avoidance provisions.
- 3. *Hartford Underwriters Ins. Co. v. Union Planters Bank* held that, in the context of the bankruptcy code, where a statute "names the parties granted the right to invoke its provisions, ... such parties only may act." 530 U.S. 1, 6, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000). One of the most powerful criticisms of *Cohen* is its failure to address the *Hartford Underwriters* holding in the context of Sections 544 to 549 only providing avoidance rights to "trustees".

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Case Law On The Avoidance Powers of the Chapter 13 Debtors

- **Debtors do not have standing to use avoidance powers under Sections 544 - 549:**
- "The better reasoned decisions hold that, in contrast to the provisions authorizing a chapter 13 debtor to pursue causes of action that are property of the estate, none of the provisions of chapter 13 authorize a chapter 13 debtor to sue on a trustee's avoidance powers (under, for example, 11 U.S.C. §§544 (unperfected liens), 547 (preferences), or 548 (fraudulent conveyances)) other than pursuant to 11 U.S.C. §522(h)." *Dawson v. Thomas (In re Dawson)*, 411 B.R. 1, 24 (Bankr.D.D.C.2008)

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- **Debtors do have standing to use avoidance powers under Sections 544 - 549:**
- **The Supreme Court's Decision In Hartford Underwriters - Has The Old "Split" Changed To A Modern Trend?**
- **If The Chapter 13 Trustee "Unjustifiably Refuses" - Does That Give The Debtor The Right To Proceed Under "Derivative Rights"?**
- **Yes:**
- *Countrywide Home Loans v. Dickson (In re Dickson)*, 427 B.R. 399 (B.A.P. 6th
- Cir.2010), *aff'd on other grounds*, 655 F.3d 585, 593(6th Cir.2011); *In re Barbee*, 461 B.R. 711,714-715 (6th Cir. BAP 2011).

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- **No:**
- *In re Stewart*, 473 B.R. 612 (Bankr. W.D. Pa. 2012)(rejecting argument for derivative standing).
- *In re Hannah*, 316 B.R. 57, 61 (Bankr. D.N.J. 2004)(holding Chapter 13 Debtor did not have standing to bring an avoidance action under §544(a) in the context of a discussion of derivative standing).
- **Maybe, if there is a benefit to the estate, but "no" if there is not:**
- **Maybe, if a timely request is made to the court:**

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- **Can The Debtor Create Standing Through A Plan Provision And The Binding Effect Of Confirmation?**
- **Why Not Both? What About The Chapter 13 Trustee And The Debtor Bringing Avoidance Actions Jointly?**
- **Is The Trustee <u>Really</u> A Party?**
- The Third Circuit Court of Appeals was not impressed by the Debtor's apparent tactic of putting the Chapter 13 Trustee in the caption, where the Chapter 13 Trustee did not actually participate in the litigation. See, In re Knapper, 407 F.3d 573, 577 n.3 & 583 (3rd Cir. 2005).

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- **Timing- If The Debtor Wants The Chapter 13 Trustee To Join In Litigation: Ask Early:**
- *In re Merritt*, 2015 WL 1403093 (Bankr. E.D. Pa. March 25, 2015). Chapter 13 Trustee objected to joining with the Debtor, in part, because the Debtor approached the Trustee so close to the two year bar date that the Trustee could not get comfortable with filing an action that would comply with Rule 9011.
- **Can The Chapter 13 Trustee Intervene Or Be "Substituted In"?**
- Wood v. Mize (In re Wood), 301 B.R. 588, 562 (Bankr. W.D. Mo. 2003.
- *In re Huntzinger*, 268 B.R. 263, 265-266 (Bankr D. Kan. 2000).
- *In re Ryker*, 315 B.R. 664, 674 (Bankr. D.N.J. 2004).

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- **A Trap For The Unwary Chapter 13 Trustee/Debtor Failing To Object To Confirmation.**
- The Use of Avoidance Powers is Different Than A Chapter 13 Debtor Simply Pursuing Litigation On Behalf Of The Bankruptcy Estate.
- Lack Of Standing's Potential Bleed Over Into The Claims Objection Process.

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Does The Trustee Having Avoidance Powers Create A Corresponding Duty To Use Them?

- **Some Courts Say: "Generally, No".**
  In Re Engle, 496 B.R. 456, 464 (Bankr. S.D. Ohio 2013).
- **Some Courts Say: "Generally, Yes".**
  In re Johnson, 279 B.R. 218, 225 (Bankr. M.D. Tenn. 2002)

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- **But What About Trustee Liability?**
- One reason that a Chapter 13 Trustee might be motivated to pursue an avoidance action is because if, after the statute of limitations passes, the Chapter 13 case converts to a Chapter 7 -
- the Chapter 13 Trustee could be sued by the Chapter 7 Trustee for failing to avoid the transfer.

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- **Obtaining a waiver- the alternative to litigation.**
- If the main concern is protecting creditors from the possibility of conversion after the bar date for bringing an avoidance action, one of the most common ways to address that concern is by obtaining a waiver.
- A waiver saves the Chapter 13 trusteeship the time and expense of litigation, while still preserving the cause of action if it should need to be brought at a later date.
- The most important consideration in obtaining a waiver is making sure that it is effective in waiving the statute of limitations defense. That means: NOT getting a waiver from the Debtor-getting it, instead, from the potential preference/fraudulent transfer DEFENDANT. The Debtor is generally not going to be able to provide an effective waiver on behalf of a future defendant in an adversary proceeding.

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- Other Potential Negative Consequences To Chapter 13 Trustees Not Pursuing Avoidance Claims:
- Use Of Avoidance Powers As A Factor In Conversion To Chapter 7:
- Section 522(1) - Avoidance Powers That Primarily Belong To The Debtor.
- Section 522(£) specifically gives ***debtors*** the power avoid the fixing of certain liens.
- When a debtor seeks to avoid a lien to the extent that it impairs his permitted exemptions, he does not utilize any avoidance powers derived from the trustee. *In re Tash*, 80 B.R. 304, 306 (Bankr.D. .N.J.1987).
- Non-possessory, non-purchase money security interests in household goods, "tools of the trade" and professionally prescribed health aids [§522(f)(l)(B)].

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- Does a Chapter 13 Trustee also have standing to avoid liens under §522(f)?
- Yes. *Matter of Maddox*, 15 F.3d 1347, 13551356 (5th Cir. 1994); *In re Kennedy*, 139 B.R. 389, 390-392 (Bkrtcy.N.D. Miss.1992). However, a Chapter 13 Trustee does not generally take actions that will only benefit the Debtor - and, in most cases, Section 522(f) avoidance does not benefit the unsecured creditors in a Chapter 13 case.
- Avoidance You Can't Avoid- The Hypothetical Liquidation For The Best Interest Test.
- Under The "Best Interest" Test, The Chapter 13 Trustee Has To Look At A "Hypothetical Liquidation"

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- Avoidance Actions Are "Litigation Assets" For Purposes Of The Best Interest Of Creditors Test.
- The Best Interest Of Creditors Test - Deductions.
- The "cost of sale" is one expense that is often allowed.
- The Chapter 7 Trustee fee may also be included in the calculation.
- Taxes, such as capital gains taxes, that would have to be paid in the Chapter 7, are also deducted.
- Arriving At A Precise Number For Purposes Of Section 1325(a)(4) Is Hard So, Many Courts Use A Standard Discount.

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Thursday July 2, 2015

3:00 – 4:00 **Distinguishing Good Faith from Bad Faith at Confirmation and Dismissal.**
Moderator: Douglas B. Kiel, Chapter 13 Standing Trustee for the District of Colorado (Denver)
Honorable Rebecca B. Connelly, Chief Judge of the United States Bankruptcy Court for the Western District of Virginia (Harrisonburg)
Mary Beth Ausbrooks, Rothschild & Ausbrooks, PLLC (Nashville, TN)

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Distinguishing Good Faith From Bad Faith at Confirmation and Dismissal

Good Faith at Confirmation

Good faith is mentioned twice in 11 U.S.C. 1325. A debtor has the burden of proving that the petition was filed in good faith (section (a)(7)) and that the plan was been proposed in good faith (section (a)(3)). Bankruptcy courts across the country have adopted a "totality of circumstances" test when ruling on a good faith objection to confirmation. The determination is done on a case by case basis. Courts have, however, adopted factors to use in the good faith analysis.

First Circuit: ***Keach v. Boyajian***, 243 B.R. 851 (B.A.P. 1st Cir. 2000)

Honesty with respect to the debtor's post-filing conduct.
Simple honesty of purpose.

In re Torres Lopez, 138 B.R. 348 (D.P.R. 1992)

Whether the debtor's income was sufficient to fund the plan?
Whether the living expenses were modest?
Whether the attorney's fees are reasonable?
The duration of the plan.
The nature of the debts.
Previous filings.
Administrative burden on the Trustee.

Second Circuit: ***In re Paulson***, 170 B.R. 496 (Bankr. D. Conn. 1994)

Court should closely scrutinize the debtor's motivation and any other relevant factors in considering whether good faith exists.

In re Wrobel, 525 B.R. 211 (Bankr. W.D.N.Y. 2015).

Good Faith Means "Fundamentally Fair" Treatment of Creditors. Law firm helped the debtor obtain a $101,000 settlement in divorce action and obtained a $96,000 judgment for attorney's fees in state court. The debtor used part of the settlement to purchase a condominium and subsequently filed for bankruptcy claiming the condominium as exempt. The debtor's plan proposed to pay only 10% of the judgment while retaining the property purchased with the settlement funds. The court found that this treatment was not "fundamentally fair" to the law firm and thus that the debtor did not propose the plan in good faith.

Third Circuit: ***New Jersey Lawyers' Fund for Client Prot. V. Goddard***, 212 B.R. 233(D.N.J. 1997)

Whether the debtor has stated his debts and expenses accurately?
Whether he has made any fraudulent misrepresentations to mislead the bankruptcy court?
Whether he has unfairly manipulated the bankruptcy code?

In re Oglesby, 158 B.R. 602 (E.D. Pa. 1993) (Serial filings)

Whether the debtor has deliberately misinformed the court of facts material to confirmation of the plan?
Whether the debtor intends to effectuate the plan as proposed?
Whether the proposed plan is for a purpose not permitted under the Bankruptcy Code?

Fourth Circuit: ***Deans v. O'Donnell***, 692 F.2d 968 (4th Cir. 1982)

Amount proposed to pay back to unsecured creditors.
The debtor's financial situation.
Plan length.
The debtor's employment history and prospects.
The nature and amount of unsecured claims.
Past filings.
The debtor's honesty in representing facts.
Any unusual or exceptional problems facing the debtor.

In re Richey, 20 CBN 1070 (Bankr. E.D.N.C. 2010)

"Good faith does not require a debtor to be perfect, but it does require debtors to make complete and honest disclosures."

Fifth Circuit: ***In re McLaughlin***, 217 B.R. 772 (Bankr. W.D. Tex. 1998)

The debtor's pre-petition conduct leading to the debt.
The timing of the petition.
The treatment of the objecting creditor in the proposed plan.

Sixth Circuit: ***Metro Employees Credit Union v. Okoreeh-Baah***, 836 F.2d 1030 (6th Cir. 1988)

The amount of income of the debtor and spouse from all sources.
The regular and recurring living expenses of the debtor and his dependents.
The amount of attorney fees.
Plan length.
The motivations of the debtor and his sincerity in seeking relief.

The ability of the debtor to earn and the likelihood of future increase or diminution of earnings.
Special circumstances, such as medical expense or unusual care required for the debtor or his dependents.
Prior filings.
The circumstances under which the debtor has contracted his debts and his demonstrated bona fides, or lack of same, in dealing with his creditors.
Whether the amount or percentage of payment would operate or be a mockery of honest, hardworking, well intended debtors who pay a higher percentage of their claims consistent with the purpose and spirit of Chapter 13.
Administrative burden on the trustee.
The salutary rehabilitative provisions of the Code which are to be construed liberally in favor of the debtor.

Seventh Circuit: ***In re Love***, 957 F.2d 1350 (7th Cir. 1992)

Whether the filing is fundamentally fair?
Whether the filing is fundamentally fair to creditors?
Whether the filing is fundamentally fair in a manner that complies with the spirit of the Bankruptcy Code?

Ravenot v. Ringdale, 669 F.2d 426 (7th Cir. 1982)

Whether the debts are stated accurately in the schedules?
Whether expenses are accurately estimated?
The percentage of repayment proposed.
Inaccuracies in the plan or schedules.
Fundamental fairness.

Eighth Circuit: **Banks v. Vandiver**, *248 B.R. 799 (B.A.P. 8th Cir. 2000)*

Whether the debtor has stated his debts and expenses accurately?
Whether he has made any fraudulent misrepresentation to mislead the bankruptcy court?
Whether he has unfairly manipulated the Bankruptcy Code?
The nature of the debt sought to be discharged.
Whether the debt would be dischargeable in a Chapter 7?
The Debtor's motivation and sincerity in seeking Chapter 13 relief.
The Debtor's pre-filing conduct

Ninth Circuit: ***In re Leavitt***, 171 F.3d 1219 (9th Cir 1999)

Whether debtors misrepresented facts in their plan or unfairly manipulated the bankruptcy code?
The debtor's history of filings and dismissals.
Whether the debtor intended to defeat state court litigation?
Whether there is egregious behavior present.

In re Hogan, No. 14-10879, 2015 WL 1221579 (Bankr. N.D. Cal. Mar. 13, 2015).

Plan with "No Compelling Purpose" Was Filed in Bad Faith. The court found that the debtors were attempting "to use the bankruptcy court improperly to condition surrender of "property on payment of damages" despite the fact that state courts had ruled that the debtors had to surrender the property without the payment of such damages. The court further found that the purpose of the filing of their petition was "delay, designed to prolong their stay in the property, and not a good faith desire to reorganize." The "plan [had] no compelling purpose and [was] proposed only to allow [the debtors] to prosecute [a creditor] for their personal gain." The court denied confirmation.

Tenth Circuit: ***Flygare v. Boulden***, 709 F.2d 1344 (10th Cir. 1983)

The amount of the proposed payments and any surplus of income.
The debtor's employment history, ability to earn and likelihood of future increases in income.
Plan length.
Accuracy of the plan's statements of the debts, expenses and percentage repayment of unsecured debt and whether any inaccuracies are an attempt to mislead the Court.
Extent to which secured claims are modified.
The type of debt sought to be discharged and whether it is non-dischargeable in Chapter 7.
Special circumstances, such as medical expenses.
Prior filings.
Administrative burden on the Trustee.

Eleventh Circuit: ***Kitchens v. Georgia R.R. Bank & Trust Co***., 702 F.2d 885 (11th Cir. 1983)

The amount of the debtor's income from all sources.
The living expenses of the debtor and his dependents.
The amount of attorney fees.
The probable or expected duration of the plan.
The motivations of the debtor and his sincerity in seeking relief under the Code.
The debtor's degree of effort.
The debtor's ability to earn and the likelihood of fluctuation in his earnings.

Special circumstances, such as inordinate medical expense.
Prior filings.
The circumstances under which the debtor has contracted his debts and his demonstrated bona fides, or lack thereof, in dealing with his creditors.
Administrative burden on the Trustee.

Other Considerations in Good Faith:

Serial filings:

In re Oglesby, 158 B.R. 602 (E.D. Pa. 1993)

Length of time between the prior case and the present one.
Whether the successive cases were filed to obtain the favorable treatment of the automatic stay.
The effort made to comply with the prior case's plan.
The fact that Congress intended the debtor to achieve its goals in a single case.
Any other facts the Court finds relevant relating to the debtor's purposes in making successive filings

There are consequences of filing a series of bankruptcy cases. However, it is not a per se bad faith filing. ***In re Smith***, 20 CBN 109 (Bankr. D.S.C. 2009)

Chapter 20 cases:

It is not per se bad faith. ***Johnson v. Home State Bank***, 501 U.S. 78 (1991).

There is an elevated good faith requirement. ***In re Taylor***, 261 B.R. 877 (Bankr. E.D. Va 2001)

There is nothing that precludes a debtor from filing a Chapter 13 after receiving a discharge in a Chapter 7; however, the filing must be in good faith. Here, the Court held that confirming the plan in this case would allow the debtor to manipulate the bankruptcy system. "Such treatment is neither fair nor equitable to creditors and would result in an abuse of the purpose and spirit of the bankruptcy process. ***In re Chanthaleeukay, Phonesavanh and Phoovieng***, 20 CBN 389 (Bankr. M.D.N.C 2010)

In ***In re Caldwell***, 151 B.R. 131 (Bankr. S.D. Ohio 1992), the court held that if the filing dates of the Chapter 7 and 13 cases occurred within 12 months, it is required to give notice to all of the creditors who held discharged debts in the prior Chapter 7, and give them an opportunity to object.

Factors to be considered: (***In re Cushman***, 217 B.R. 470 (Bankr. E.D. Va 1998))

Proximity of time between the Chapter 7 and the new Chapter 13.
Whether there has been a change in circumstances?

Whether the two filings accomplish a result that is not permitted in either chapter standing alone?
Whether the two filings treat creditors in a fundamentally fair and equitable manner or whether they are an abuse of the purpose and spirit of the Bankruptcy Code.

Luxury items:

Improper to examine the nature of the collateral securing loans to be paid into the plan for above median debtors. Above median debtors can pay for luxury items because Section 1325(b) directs the debtor to deduct secured debt payments without regard to the nature of the collateral. The fact that the above median debtor is keeping luxury items is irrelevant in a good faith analysis. ***In re Welsh*** (9th Cir. 2013)

Bad faith was found when the debtor proposed to keep and pay for an expensive Land Rover and pay for a housekeeper while paying 60% to unsecured creditors. ***In re Samadi***, 02-30336-H2-13 (Bankr. S.D. Tex. Sept. 30, 2002)

Debtors proposed to keep a boat while proposing a nominal dividend to unsecured creditors. Court held that their plan "demonstrates that they have placed their own recreational desires ahead of the legitimate claims of their unsecured creditors. This belies their assertion that they are motivated and sincere in their efforts at financial rehabilitation." ***In re Sandberg***, 20 CBN 1167 (Bankr. D. Kan. 2010)

Debtor proposed to pay 30% to her unsecured creditors and to pay in full two claims secured by CDs. Court held that the net effect was that, if confirmed, she would in essence pay herself back as a creditor. Court found that it violated the spirit of the Code. ***In re Tucker***, 220 B.R. 359 (Bankr. W.D. Tenn 1998)

Bad faith was found when debtor proposed to pay for a boat, and pay for a slip rental and insurance and pay 34.9% to unsecured creditors. ***In re Kasun***, 186 B.R. 62 (Bankr. E.D. Va 1995)

Debtors proposed to retain and pay for a 2010 Nissan Sentra, a 2006 Ford F-150 pickup, and a 2011 Harley Davidson motorcycle, the latter two having been purchased within 910 days prior to filing. The plan proposed to pay 0% to the general unsecured creditors. The trustee objected as lacking in good faith (as well as on a separate issue on unfair discrimination). The bankruptcy court found that the retention of the Harley Davidson motorcycle and no dividend to unsecured creditors was not good faith "but would instead be an unfair manipulation of the Bankruptcy Code." ***In re Knowles***, 501 B.R. 409 (Bankr. D. Kan. 2013).

Trustee objected on good faith grounds to confirmation of debtors' chapter 13 plan because debtors proposed to keep a large home valued at about $300,000 while paying 8% to unsecured creditors. The bankruptcy court acknowledged that the mortgage payments were almost a third of the debtors' income but declined to find bad faith based on a totality of the circumstances. The court found that the plan was filed in good faith, specifically noting that the debtors had not

previously filed for bankruptcy, that the bankruptcy was filed as a result of the male debtor's job loss, that the debtors went through their savings before filing instead of incurring new debt, and that the debtors were eligible for chapter 7 and had no non-exempt assets but filed chapter 13 to provide some payment. ***In re Sweet***, 428 B.R. 917 (Bankr. M.D. Ga. 2010); *see also* ***In re Roberts***, 493 B.R. 584 (Bankr. D. Kan. 2013) (refusing to find that a plan providing for payments of $3,658 on an underwater home and a 0% dividend to unsecured creditors was proposed in bad faith).

Bad faith was found in a 36 month plan that provided to pay a claim secured by a Cadillac. ***In re Jones***, 119 B.R. 996 (Bankr. N.D. Ind. 1990)

Debtors must tighten their belt and eliminate luxuries. ***In re McNeely***, 366 B.R. 542 (Bankr. N.D. W. Va. 2007)

Debtors proposed a plan that provided for the retention and payment of an encumbered four wheeler. Payments on the four wheeler would total $5,265 over the life of the plan, while general unsecured creditors would receive only $1000, resulting in a dividend of less than 3%. The court set forth four additional factors for good faith: (i) "'reasonably necessary' means adequate but not first class"; (ii) "Luxuries are excluded"; (iii) "A convenience is not the same as a necessity"; and (iv) "There is a sacrifice quotient in Chapter 13 cases." The court found that the retention and payment on the four wheeler violated good faith under § 1325(a)(3). ***In re McDonald***, Case No. 14-11740, 2015 WL 1524096 (Bankr. W.D. La. Mar. 27, 2015).

Fee Only cases:

Appears to be per se bad faith. ***In re Montry***, 393 B.R. 695 (Bankr. W.D. Mo. 2008)

District Court upheld bankruptcy court's ruling that fee only cases are not filed in good faith. Attorney also was denied fees***.*** ***In re Wayne E. Puffer***, 2011 WL 2689096 (D. Mass. 07/08/2011)

The Eleventh Circuit held that the bankruptcy court did not clearly err in determining that the debtor filed the petition and chapter 13 plan in bad faith. The bankruptcy court found lack of good faith because "the totality of the factual circumstances showed [the debtor] was best served by a Chapter 7 bankruptcy; only [the debtor's] attorney benefitted from proceeding under Chapter 13; and [the debtor] was likely to default in his Chapter 13 case and end up without a discharge." ***Brown v. Gore (In re Brown),*** 742 F.3d 1309 (11th Cir. 2014); *see also* ***Ingram v. Burchard***, 482 B.R. 313 (N.D. Cal. 2012) (finding that bankruptcy court did not clearly err in finding that a fee only plan in a "veiled Chapter 7" was not proposed in good faith).

The Fifth Circuit held that the bankruptcy court did not clearly err in finding the debtor's plan was filed in good faith. The debtor argued, and the bankruptcy court found persuasive, that (i) it would have taken her over a year to save up enough for the chapter 7 fee and (ii) filing chapter 7

would prevent her from declaring bankruptcy again for a longer period than a chapter 13, which was a concern given the debtor's legitimate fear of future medical debt. ***Sikes v. Crager (In re Crager),*** 691 F.3d 671 (5th Cir. 2012).

The First Circuit held that fee-only plans should be analyzed under a totality of the circumstances, noting that "[t]he dangers of such plans are manifest, and a debtor who submits such a plan carries a heavy burden of demonstrating special circumstances that justify its submission." ***Berliner v. Pappalardo (In re Puffer),*** 674 F.3d 78 (1st Cir. 2012); *see also* ***Berliner v. Pappalardo (In re Buck)***, 509 B.R. 737 (D. Mass. 2014) (holding that it was legal error to conclude that fee-only plan was per se lacking in good faith).

Burden of Proof:

The debtor bears the burden of establishing good faith. ***In re Francis***, 273 B.R. 87 (6th B.A.P. 2002)

Once good faith is challenged, the debtor has the burden to prove that the plan was filed in good faith. ***Boyce v. Barnhart***, 20 CBN 386 (Bankr. M.D. Pa. 2010)

"When a prima facie objection is raised, the debtors still have the burden of proof to establish their 'good faith'. This requires the debtors to produce some evidence in support of confirmation to address the 'good faith' issue. At a minimum, they should explain the circumstances" that lead them to seek relief. ***In re Lavilla, Daniel and Molly*** (20 CBN 641 (Bankr. E.D. 2010)

Disposable Monthly Income:

Even though the debtor rightfully excluded his Social Security benefits from the Disposable Monthly Test found in 1325(b), the Court found it was bad faith for the debtor to have a surplus in their budget, even though the surplus was attributable to the Social Security benefits. ***In re Westing***, 20 CBN 1000 (Bankr. D. Idaho 2010)

The Court required Social Security to be counted toward projected disposable income. Failure to do so is bad faith. ***In re Rodgers***, 20 CBN 1114 (Bankr. M.D. Fla. 2010)

Court found that the debtor's failure to dedicate Social Security benefits to the plan is not bad faith per se. ***In re Melander***, 2014 WL 988484 (Bankr. D. Minn. 3/13/14)

It is improper to consider the exclusion of Social Security benefits in a good faith analysis. ***In re Welsh*** (9th Cir. 2013)

"When a Chapter 13 debtor calculates his repayment plan payments exactly as the Bankruptcy Code and the Social Security Act allow him to, and thereby excludes SSI, that exclusion cannot constitute a lack of good faith." ***Anderson v. Cranmer (In re Cranmer),*** 697 F.3d 1314, 1319 (10th Cir. 2012); *see also* ***Drummond v. Welsh (In re Welsh)***, 711 F.3d 1120 (9th Cir. 2013)

("We cannot conclude, however, that a plan prepared completely in accordance with the very detailed calculations that Congress set forth is not proposed in good faith.").

"[R]etention of exempt social security benefits alone is legally insufficient to support a finding of bad faith under the Bankruptcy Code." ***Beaulieu v. Ragos (In re Ragos),*** 700 F.3d 220, 227 (5th Cir. 2012); *see also* ***Mort Ranta v. Gorman***, 721 F.3d 241, 253 n.15 (4th Cir. 2013) ("We note, however, that the exclusion of Social Security income from disposable income, as required by statute, by itself, does not constitute bad faith."); ***Fink v. Thompson (In re Thompson)***, 439 B.R. 140 (B.A.P. 8th Cir. 2010) ("[E]ven if the Debtors' retention of Social Security income could contribute to a finding of bad faith, standing alone it could not prevent the Debtors from establishing good faith under section 1325(a)(3).").

Duty to Raise Good Faith:

Court Has Duty to Review All Chapter 13 Plans. "§ 1325(a) instructs a bankruptcy court to confirm a plan only if the court finds, *inter alia*, that the plan complies with the 'applicable provisions' of the Code." ***United Student Aid Funds, Inc. v. Espinosa***, 559 U.S. 260, 277 (2010); *see also* ***In re Renteria***, 456 B.R. 444 (Bankr. E.D. Cal. 2011) (noting that a bankruptcy court has a "duty to make sure the Plan complies with the applicable provisions of the Bankruptcy Code"). In a footnote, the Supreme Court clarified that this obligation is required: "Section 1325(a) . . . *requires* bankruptcy courts to address and correct a defect in a debtor's proposed plan even if no creditor raises the issue." *Espinosa*, 559 U.S. at 277 n.14; *see also* ***In re Hopper***, 474 B.R. 872, 880 n.18 (Bankr. E.D. Ark. 2012) ("Bankruptcy courts have an independent duty to ensure that confirmation requirements, including the requirement that the plan be filed in good faith, are met, and can raise these issues *sua sponte*.").

Courts Should Carefully Scrutinize Plan to Ensure Good Faith. Debtor filed a "Chapter 20" case to strip off a wholly unsecured junior deed of trust lien from his primary residence. The district court noted that, while lien stripping is possible in a "Chapter 20," the creditors are still protected by the good faith requirement. The district court concluded that "bankruptcy courts should carefully scrutinize a Chapter 20 debtor's plan to ensure that it was proposed in good faith." ***Zeman v. Waterman (In re Waterman),*** 469 B.R. 334 (D. Colo. 2012).

Amount of Payments:

Debtors Need Not Contribute More than Required Under Projected Disposable Income Test. The debtors proposed a chapter 13 plan based on the projected disposable income using the National and Local Standards promulgated by the IRS. The trustee objected on good faith grounds because the debtors' actual expenses were less than the National and Local Standards used in the calculation of their projected disposable income. The bankruptcy court

held that, even though the actual expenses were less, the debtors did not need to contribute more than the calculated projected disposable income to propose their plan in good faith. ***In re O'Neill Miranda***, 449 B.R. 182 (Bankr. D.P.R. 2011).

Bad Faith Found Where Debtors Deducted Secured Payments for Collateral to Be Surrendered from Projected Disposable Income. Debtors proposed a chapter 13 plan which proposed a payment amount, which was derived by including in "amounts reasonably necessary to be expended" an amount for contractual payments for collateral which the debtors intended to surrender. The trustee objected, and the bankruptcy court found that this plan was proposed in bad faith. The district court affirmed the bankruptcy decision denying confirmation, noting that the payment calculation was technically correct but was not accurate. ***White v. Waage***, 440 B.R. 563 (M.D. Fla. 2010).

Plan Proposed in Good Faith Despite Fact that Debtors Began Retirement Contributions Three Months Prior to Filing. Three months prior to filing for bankruptcy, the debtors began making retirement plan contributions. The debtors deducted from disposable income the voluntary retirement contributions. Over the life of the plan, the debtors would make retirement contributions of about $32,500, but yet the unsecured creditors would only receive 10.8% on the unsecured debt of about $22,000. The trustee objected. The bankruptcy court refused to find bad faith, noting that it could not conclude that the intent of the retirement contributions was to decrease payment to unsecured creditors**.** ***In re Jensen***, 496 B.R. 615 (Bankr. D. Utah 2013).

Unfair Discrimination:

Unfair Discrimination Was Bad Faith. Debtors proposed a plan to pay nondischargeable state and federal tax debts before other unsecured creditors. The plan would pay 97% of the nondischargeable debt leaving nothing for the other unsecured creditors. Holding that the plan lacked good faith, the Eight Circuit found that the debtors were "prioritizing payment to creditors who will be paid in full *regardless* of the plan implemented in bankruptcy, at the expense of creditors with no other recourse." ***Copeland v. Fink (In re Copeland),*** 742 F.3d 811 (8th Cir. 2014).

Failure to Disclose:

Failure to Disclose Promptly Two Personal Injury Lawsuits Was Bad Faith. Debtor lacked good faith in filing petition, because debtor, who was an attorney, failed to disclose two personal injury law suits on her original schedules, first amended schedules, statement of financial affairs, and at the meeting of creditors. The fact that the debtor disclosed following a

trustee's motion to dismiss did not change the bad faith in filing the petition. ***Zizza v. Pappalardo (In re Zizza),*** 500 B.R. 288 (B.A.P. 1st Cir. 2013).

Failure to Disclose Multiple Assets and Money Transfers Was Bad Faith. Debtor filed petition and plan in bad faith based on failure to disclose (i) his one-half interest in an LLC that owned valuable real estate, (ii) a joint interest in a bank account, (iii) ownership of a .308 rifle, and (iv) transfers from his law firm's account into his wife's account. Debtor's plan proposed no distribution to unsecured creditors until the trustee discovered debtor's interest in LLC at which point the debtor amended the plan; however, the court determined it was "too little, too late." ***In re Gomery,*** 523 B.R. 773 (Bankr. W.D. Mich. 2015).

Plan Modification:

Modification Must Satisfy Good Faith Requirement. Court confirmed debtor's 60-month chapter 13 plan. During the life of the plan, the debtor retired and moved to modify the plan to reduce the monthly payments as well as the term of the plan to 36 months. The bankruptcy court held that the good faith requirement remained as to proposed modifications and held that the debtor did not present a good faith basis for reducing the length of the plan. ***In re Grutsch***, 453 B.R. 420 (Bankr. D. Kan. 2011).

Good Faith at Dismissal

I. Dismissal Issues

1. Does a Debtor have an absolute right to voluntarily dismiss a Chapter 13 case?

    i. 11 U.S.C. § 1307(b):

    > "On request of the debtor at any time, **if the case has not been converted** under section 706, 1112, or 1208 of this title, the **court shall dismiss** a case under this chapter. Any waiver of the right to dismiss under this subsection is unenforceable."

    ii. Supreme Court cases:

        1. *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365 (U.S. 2007).
        2. *Law v. Siegel*, 134 S. Ct. 1188 (U.S. 2014).

    iii. Cases holding there is an absolute right:

        1. *Barbieri v. RAJ Acquisition Corp. (In re Barbieri)*, 199 F.3d 616 (2d Cir. N.Y. 1999).
        2. *In re Williams*, 435 B.R. 552 (Bankr. N.D. Ill. 2010).
        3. *In re Mangual*, 2010 Bankr. LEXIS 4688 (Bankr. D.P.R. Dec. 20, 2010).
        4. *In re Fisher*, 2015 Bankr. LEXIS 875 (Bankr. W.D. Va. Mar. 19, 2015).

    iv. Cases holding there is no absolute right:

        1. *Rosson v. Fitzgerald (In re Rosson)*, 545 F.3d 764 (9th Cir. Wash. 2008).
        2. *Molitor v. Eidson (In re Molitor)*, 76 F.3d 218 (8th Cir. Minn. 1996).
        3. *Jacobsen v. Moser (In re Jacobsen)*, 609 F.3d 647 (5th Cir. Tex. 2010).

2. Trustee's duty to creditors to ensure that they are paid vs. debtor's right to dismiss.

    i. Query:

    Debtor failed to list an asset in schedules. Trustee learns of the sale of the asset for $500,000. Debtor moves to dismiss the case.

    1. Does the trustee go along with dismissal assuming the debtor will pay all his creditors outside of bankruptcy?

    2. Does the trustee move for an order seeking turnover of the sale proceeds?

    3. Does the trustee oppose dismissal on the basis of "bad faith"?

    4. Does the trustee move to convert to Chapter 7 on basis of "bad faith"?

    5. Can voluntary dismissal be denied on the grounds that conversion to Chapter 7 is in the best interest of creditors even when there is no bad faith?

    6. Does the trustee move to dismiss the case with prejudice and seek a bar on refiling or a bar on the future discharge of certain debts?

3. What are the factors that indicate "bad faith"?

Flygare v. Boulden, 709 F.2d 1344, 1347 (10th Cir. Utah 1983):
(1) the amount of the proposed payments and the amount of the debtor's surplus;
(2) the debtor's employment history, ability to earn and likelihood of future increases in income;
(3) the probable or expected duration of the plan;
(4) the accuracy of the plan's statement of the debts, expenses and percentage repayment of unsecured debt and whether any inaccuracies are an attempt to mislead the court;
(5) the extent of preferential treatment between classes of creditors;
(6) the extent to which secured claims are modified;
(7) the type of debt sought to be discharged and whether any such debt is non-dischargeable in Chapter 7;

(8) the existence of special circumstances such as inordinate medical expenses;
(9) the frequency with which the debtor has sought relief under the Bankruptcy Reform Act;
(10) the motivation and sincerity of the debtor in seeking Chapter 13 relief; and
(11) the burden which the plan's administration would place upon the trustee.

II. Duty to Disclose

1. Does a debtor have a duty to disclose an asset acquired post-confirmation?

    i. Rule 1007(h)

    "If, **as provided by § 541(a)(5)** of the Code, the debtor acquires or becomes entitled to acquire any interest in property, the **debtor shall** within 14 days after the information comes to the debtor's knowledge or within such further time the court may allow, file a supplemental schedule in the . . . chapter 13 individual debt adjustment case. If any of the property required to be reported under this subdivision is claimed by the debtor as exempt, the debtor shall claim the exemptions in the supplemental schedule. The duty to file a supplemental schedule in accordance with this subdivision **continues notwithstanding the closing of the case**, except that the schedule need not be filed in a . . . chapter 13 case with respect to property acquired after entry of the order . . . discharging the debtor in a . . . chapter 13 case."

    ii. Amy Catherine Dinn, *A Debtor's Duty to Update the Court*, 55 S. TEX. L. REV. 627 (2014).

Is There an Absolute Right to Dismissal 1307(b)?

Supreme Court

Marrama v. Citizens Bank of Massachusetts, 549 U.S. 365 (U.S. 2007). Holding that a debtor does not have an absolute right to convert a Chapter 7 case to a Chapter 13 case.

Law v. Siegel, 134 S. Ct. 1188 (U.S. 2014). The Court appears to limit the holding in *Marrama* by explaining that although 706(a) gives a debtor the right to convert, that right is "expressly conditioned" on a debtor's "ability to qualify as a 'debtor' under Chapter 13." In *Marrama*, the debtor would not have been eligible for a Chapter 13 case because of his bad faith conduct and therefore, the court did not have to allow a conversion. The Court says that "[a]t most, Marrama's dictum suggests that in some circumstances a bankruptcy court may be authorized to dispense with futile procedural niceties in order to reach more expeditiously an end result required by the Code."

2nd Circuit (Pre-*Marrama* precedent for an absolute right to dismiss)

Barbieri v. RAJ Acquisition Corp. (In re Barbieri), 199 F.3d 616 (2d Cir. N.Y. 1999). Decided prior to *Marrama* and holding that there is an absolute right to dismiss under 11 U.S.C. § 1307(b) because the court's power under § 105(a) does not allow the court to disregard the plain language of § 1307(b).

In re Armstrong, 408 B.R. 559 (Bankr. E.D.N.Y. 2009). Holding that *Barbieri* is no longer good law in the wake of the *Marrama* decision and that a debtor does not have an absolute right to dismiss under 11 U.S.C. § 1307(b).

Procel v. United States Tr. (In re Procel), 467 B.R. 297 (S.D.N.Y. 2012). Holding that *Barbieri* is still binding law in the 2nd Circuit despite the *Marrama* ruling.

5th Circuit (No absolute right)

Jacobsen v. Moser (In re Jacobsen), 609 F.3d 647 (5th Cir. Tex. 2010). Holding that there is no absolute right to dismiss when debtor has acted in bad faith and the court may use its power under 105(a) to grant a motion to convert a case to chapter 7 instead of granting the debtor's motion to dismiss. The court reasoned that there was no analytical distinction between the language of 1307(b) and 706(a), and therefore the rationale in *Marrama* must be applied to 1307(b).

8th Circuit (No absolute right)

Molitor v. Eidson (In re Molitor), 76 F.3d 218 (8th Cir. Minn. 1996). Holding that there is no absolute right to dismiss. The court relied on the "overall purpose and design of the statute as a whole" to conclude that allowing the debtor an absolute right to dismiss under 1307(b) would render 1307(c) "a dead letter and open up the bankruptcy courts to a myriad of potential abuses." This is a statutory construction argument rather than an 11 U.S.C. § 105(a) argument.

9th Circuit (No absolute right)

Rosson v. Fitzgerald (In re Rosson), 545 F.3d 764 (9th Cir. Wash. 2008). Holding that, in light of *Marrama*, "the debtor's right of voluntary dismissal under § 1307(b) is not absolute, but is qualified by the authority of a bankruptcy court to deny dismissal on grounds of bad-faith conduct or 'to prevent an abuse of process.' 11 U.S.C. § 105(a)."

Other Decisions

1st Circuit

In re Mangual, 2010 Bankr. LEXIS 4688 (Bankr. D.P.R. Dec. 20, 2010). Holding that there is an absolute right to dismiss even when a motion to convert is pending. However, dismissal can be conditioned and the debtors were barred from refiling any bankruptcy petition for one year.

3rd Circuit

Taylor v. Winnecour, 460 B.R. 673 (W.D. Pa. 2011). Upholding the lower court's ruling that there is no absolute right to dismiss. The "Court believes that 11 U.S.C. § 1307(b) permits the Court to consider factors such as a debtor's good faith or lack thereof and the consequences to creditors in deciding whether to grant or deny a debtor's Motion to Dismiss." (emphasis added)

In re Caola, 422 B.R. 13 (Bankr. D.N.J. 2010). Holding that there is no absolute right to dismiss post-*Marrama* if the court finds debtor acted in bad faith.

4th Circuit

In re Criscuolo, 2014 Bankr. LEXIS 2138 (Bankr. E.D. Va. May 12, 2014). Holding that there is no absolute right to dismiss and granting the trustee's motion to dismiss with prejudice.

In re Mattick, 496 B.R. 792 (Bankr. W.D.N.C. 2013). Holding that there is no absolute right to dismissal when a motion to convert is pending. Debtor's case was converted to Chapter 7 because he acted in bad faith.

In re Fisher, 2015 Bankr. LEXIS 875 (Bankr. W.D. Va. Mar. 19, 2015). Holding that after *Law v. Seigel*, it is clear that a debtor has an absolute right to dismiss a case that has not been previously converted and that a court cannot use its equitable powers to override the explicit provisions of the Code. However, the court can condition the dismissal by imposing a bar on refiling for a specified time or by barring the discharge of certain debts in a subsequent case.

6th Circuit

In re Thompson, 2015 Bankr. LEXIS 271 (Bankr. E.D. Ky. Jan. 28, 2015). Holding that there is an absolute right to dismiss. However, the court did not address whether there is an exception to this right for bad faith because there was no allegation of bad faith raised in the case.

In re Cyncynatus, 2013 Bankr. LEXIS 2998 (Bankr. N.D. Ohio July 24, 2013). Following the decisions in *Jacobsen* and *Rosson* and holding that there is no absolute right to dismiss when there are allegations of bad faith.

7th Circuit

In re Williams, 435 B.R. 552 (Bankr. N.D. Ill. 2010). Holding that debtor has an absolute right to dismiss. "Because the language of § 1307(b) accords debtors an unlimited right to dismissal of unconverted Chapter 13 cases, and because that right is not limited by judicial discretion or other provisions of the Bankruptcy Code, [debtor's] request to dismiss [a] Chapter 13 case must be granted. . . ."

In re Youngblood, 2013 Bankr. LEXIS 4260 (Bankr. C.D. Ill. Oct. 10, 2013). Holding that debtor does not have an absolute right to dismiss. "If good faith is a condition of eligibility to be a Chapter 13 debtor — and Marrama says that it is — then a debtor who has acted in bad faith, both before filing and with respect to the actual filing, is not eligible to be a Chapter 13 debtor. And, a debtor who is not eligible to be a Chapter 13 debtor is not entitled to the protections of Chapter 13 such as the absolute right to dismiss. The Debtor here forfeited her eligibility for Chapter 13 by her conduct in state court and by her lack of honesty in her filings here. Accordingly, she also forfeited her absolute right to dismiss this case."

In re Neary, 2014 Bankr. LEXIS 3533 (Bankr. N.D. Ind. July 17, 2014). Holding that the court has the authority to condition the dismissal of debtor's case because of bad faith. Dismissed with prejudice and 180 bar to refiling.

In re Harrold, 2012 Bankr. LEXIS 6202 (Bankr. N.D. Ind. Feb. 6, 2012). Holding that debtor has an absolute right to dismiss and there is no bad faith exception.

10th Circuit

Zeman v. Dulaney (in Re Dulaney), 285 B.R. 10 (D. Colo. 2002). Pre-*Marrama* case holding that debtor has an absolute right to dismiss. The court relies on the plain language of the statute, the legislative history, and the voluntary nature of Chapter 13 to support its position.

In re Rouse, 301 B.R. 86 (Bankr. D. Colo. 2003). In dicta, the court notes that a chapter 13 debtor has an absolute right to dismiss.

11th Circuit

In re Norsworthy, 2009 Bankr. LEXIS 1381 (Bankr. N.D. Ga. May 27, 2009). Adopting the reasoning in *Rosson* and holding that there is no absolute right to dismiss.

In re Letterese, 397 B.R. 507 (Bankr. S.D. Fla. 2008). Holding that there is no absolute right to dismiss "in the face of bad faith conduct."

In re Davis, 2007 Bankr. LEXIS 1751 (Bankr. M.D. Fla. May 16, 2007). Holding that there is an absolute right to dismiss even though the IRS challenged the motion to dismiss on the grounds that it was filed in bad faith. The Court acknowledged the *Marrama* decision but decided it was inapplicable to the issue of whether a debtor has an absolute right to dismiss.

Thursday July 2, 2015

3:00 – 4:00 **Individual and Small Business Chapter 11 Cases vs. Chapter 13 Business Cases.**
Moderator: Kathleen A. McCallister, Chapter 13 Standing Trustee for the District of Idaho (Meridian)
Honorable Thomas B. Bennett, Chief Judge of the United States Bankruptcy Court for the Northern District of Alabama (Birmingham)
John F. Cannizzaro, Partner, Cannizzaro, Bridges, Jillisky & Streng, LLC (Marysville, OH)
Amy Elizabeth Gullifer, Cannizzaro, Bridges, Jillisky & Streng, LLC (Marysville, OH)

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Individuals and Small Businesses: Chapter 11 v. Chapter 13

NACTT Annual Seminar: July 2, 2015

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DIFFERENCES BETWEEN CHAPTER 11 AND CHAPTER 13 BANKRUPTCIES: SECTION 1: AN OVERVIEW

ISSUE	CHAPTER 11	CHAPTER 13
Who is a Debtor?	Any person who may be a debtor in a Chapter 7, a railroad, and some state banks may be debtors. No Debt Restriction. 11 U.S.C. §109(d)	An individual with regular income that owes, on the date of filing, noncontingent, liquidated, unsecured debt of less than $383,175.00 and $1,149,525.00 in secured debt. A Chapter 13 debtor cannot be a corporation, partnership, LLC, or other business entity. 11 U.S.C. §§109(e), 104
What is the cost?	Filing Fee: $1,717.00 Quarterly Fees as set by UST (generally $325.00-$1,625.00 per quarter) Attorney's Fees: often range from $7,500.00-$20,000.00+ Fee Applications required	Filing Fee: $310.00 Trustee's Fees: Up to 10% of distributions. 11 U.S.C. § 1326 Attorney's Fees: "No-Look Fee" + post-confirmation fees, usually between $3,000.00-$7,500.00 Fee Applications required for hourly work above the no-look fee.
Role of the Trustee (and Bankruptcy Administrator in	• The U.S. Trustee ("UST") plays an	Generally, a standing trustee appointed by the U.S. Trustee

Alabama and North Carolina)[1]	active role in overseeing the bankruptcy • The UST conducts the Initial Debtor Interview • The UST conducts the §341 meeting of creditors • The UST reviews monthly operating reports and requests for fees from professionals employed by the estate	serves as the trustee in a chapter 13 case. The Chapter 13 Trustee exercises the powers enumerated in 11 U.S.C. 1302(b) & (c). The standing Chapter 13 Trustee reviews filings, computes payment requirements and represents the interests of the general unsecured creditors.[2] In the Bankruptcy Administrator districts (AL & NC), the judge(s) of the district appoint the standing chapter 13 trustee and this trustee exercises the powers set forth in section 1302(b) & (c).
Co-Debtor Stay	• There is no co-debtor stay	Co-Debtor stay under 11 U.S.C. 1307 for joint consumer debt
Debtor's Record-keeping responsibilities	• Open D-I-P accounts • close all bank accounts • Add United States Trustee as loss-payee • If the debtor is a corporation or other business entity, obtain a resolution to file bankruptcy • file monthly operating reports (See UST Chapter 11 handbook)	Encourage client to keep separate personal and business bank accounts Business Debtors are required to report post-petition income and expenses. If debtor is engaged in business, produce records reflecting the financial condition of debtor's business.
Plan Payments	Plan payments are not required until the effective date of the plan, following confirmation. no requirement	First plan payment is due 30 days after filing the petition, and every 30 days thereafter.

[1] Some material adapted from *Chapter 9 v. Chapter 11 v. Chapter 13*, American College of Bankruptcy Panel Discussing Emerging and Settled Chapter 9 Issues, presented by Marc Levinson, Esq., Hon. Thomas B. Bennett, Zack A. Clement, Esq., and Debra A. Dandeneau, Esq. March 15, 2014.

[2] Daniel M. Press & Brett Weiss. *Chapter 11 for Individual Debtors: A Collier Monograph*, 2012 Matthew Bender & Co., Inc. Section 2, [5].

	that payments be made on a monthly basis. Adequate protection payments must be made upon request of a creditor, unless the loan is over-secured, in which case payments depend on the amount of the equity cushion. 11 U.S.C. 361.	Provide pre-confirmation adequate protection payments to PMSI creditors. For secured claims whose value is distributed as periodic payments, the payments shall be equal monthly amounts and in an amount sufficient to provide adequate protection.
Right to Payment	Schedules control amount owed to creditor, unless a proof of claim is filed.	If a creditor does not file a proof of claim, it does not receive any distribution under the chapter 13 plan and may have its claim discharged at the conclusion of the case.[3]
Retention of Assets Under the Plan	Individual Debtors seeking confirmation through a "cramdown" under §1129(b) may be required to liquidate non-exempt assets or pay "new value" into the estate.	Debtors are generally entitled to retain all assets, although their value will affect the percentage paid to general, unsecured creditors.
Funding the Plan	Plan may be funded with income or liquidation of assets, or any combination thereof	Plan funded by monthly disposable payment.
Administering the Plan	Plan payments are made by the Debtor, or an administrator hired by the Debtor to make payments.	The Debtor makes payments, either directly or through a wage-withholding to the Chapter 13 trustee. In some instances a car payment, mortgage, or other long-term debt may be paid "outside the plan".
Length of Plan	No restriction on plan length	If the Debtor is paying less an 100% of her general, unsecured debt, the Plan must last at least 36 months if she is below-median, and 60 months if she is above-median. The Plan cannot exceed 60 months.

[3] Daniel M. Press & Brett Weiss. *Chapter 11 for Individual Debtors: A Collier Monograph*, 2012 Matthew Bender & Co., Inc. Section 2, [7].

Discharge	If the Debtor is a business entity, the debtor receives a discharge at confirmation of the plan. 11 U.S.C. 1141(d)(1)(A). If the Debtor is an individual, the discharge does not occur until all payments are completed under the plan, unless there is notice, hearing, and cause to discharge otherwise.	Debtor receives discharge after completion of all payments have been made, and after Debtor files certifications under 11 U.S.C. 1328.
Dismissal	The Debtor has the same dismissal rights as in a Chapter 7. There must be a notice and hearing, then may dismiss with court approval.	The Debtor has the right to dismiss his case at anytime. 11 U.S.C. 1307(b).

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DIFFERENCES BETWEEN CHAPTER 11 AND CHAPTER 13 BANKRUPTCIES: SECTION 2: DISCHARGE AND TREATMENT OF CERTAIN DEBTS

ISSUE	CHAPTER 11	CHAPTER 13
Breadth of Discharge	A discharge under this chapter does not discharge a debtor who is an individual from any debt excepted under Section 523 of this title. 11 U.S.C. 1141(a)(2)	All debts provided for by the plan are discharged except for those set forth in § 1328(a). Essentially all debts excluded from discharge under § 523 are discharged in Ch 13 other than: trust taxes, taxes where no return was filed or filed late and within 2 yrs of bankruptcy, unscheduled debts, fraud while acting as fiduciary, DSOs, student loans and claims for death or PI caused while operating a vehicle while intoxicated. Dischargeable debts in this chapter include: domestic relations property settlement claims and priority taxes provided for by the plan
TAXES <u>Dischargeability</u> • Taxes relating to unfiled returns • Taxes related to Fraud/Willful Evasion • Taxes arising from Returns Filed	 non-dischargeable non-dischargeable non-dischargeable	 non-dischargeable non-dischargeable non-dischargeable

Delinquently within 2 years of the petition date • Priority Income Tax for which a return was due within 2 years of the petition or assessed w/in 240 days of the petition (but see tolling related to Offer-in-compromise or bankruptcy) Plan Treatment • Pre-petition Priority Tax Debt	non-dischargeable Priority tax claims must receive "regular installment payments in cash" with post-confirmation interest, over a period of no longer than 5 years from the date the petition was filed, in a manner that is not less favorable than the most favored non-priority unsecured claim, unless the holder of a particular claim agrees to a different treatment of such claim. 11 U.S.C. 1129(a)(9)(C)[1]	dischargeable The plan shall provide for the full payment, in deferred cash payments, unless the holder of a particular claim agrees to a different treatment of such claim.
DOMESTIC SUPPORT OBLIGATIONS	A DSO must be paid in full in cash on the effective date of the plan unless the class has accepted the plan, in which case deferred payment may be made.[2]	A DSO must be paid as a priority debt through the Plan.11 U.S.C. 1322(a)(2). But, see §1322(a)(4) relating to treatment of a dso assigned to a governmental agency
SECURED DEBTS	Section 1111(b) provides that in a Chapter 11 case a nonrecourse secured creditor is treated as a recourse creditor unless the collateral is sold, either under 11 U.S.C. 363 or under the plan, or unless the creditor exercises	Secured claims governed by 11 USC 506: a claim is secured to the extent of the value of such creditor's interest in such property, and the creditor has an unsecured claim to the extent that the value is less than the claim.

[1] Williamson, John. The Attorney's Handbook on Small Business Reorganization Under Chapter 11. 6th Ed., 2006.

[2] Williamson, John. The Attorney's Handbook on Small Business Reorganization Under Chapter 11. 6th Ed., 2006.

SECURED DEBTS (cont.)	the Section 1111(b) election to have its claim treated as fully secured. To make a Section 1111(b) election, the creditor's interest in the collateral cannot be of inconsequential value. If a creditor exercises the Section 1111(b), the creditor waives the right to contest confirmation in return for payment in full of the allowed amount of its claim under the plan without interest. In the event the collateral is later liquidated the creditor has waived his right to the unliquidated portion.[3]	But see, 11 USC 1325(a), the hanging sentence that excepts purchase money car loans for consumer purposes, incurred within 910 days of the filing of the Chapter 13 petition, or within one-year if it was used to purchase another thing of value (such as household goods).
LEASES/EXECUTORY CONTRACTS	Nonresidential real property leases: deemed rejected unless assumed within 120 days from petition date or by confirmation of the plan, whichever is *earlier*. 11 U.S.C. 365(d)(4). Other than nonresidential real property lease, no deadline to assume. If rents are owed for post-petition, pre-rejection rents, they are administrative claims to be paid pursuant to the plan. 11 U.S.C. 365(d)(4)	11 U.S.C. 1322(b)(7) permits debtor to assume, assign or reject pursuant to 11 USC § 365. If plan is silent as to assumption or rejection, then personal property lease or executory contract is deemed rejected (§ 365(b)(3)). Defaults must be promptly cured. (§ 365(b)(1)(A). If plan is silent as to assumption or rejection, then debtor may modify confirmed plan to reject non-personal property lease or executory contract. 11 U.S.C. 365(d)(4) applies, but see *Ford Motor Credit Co. V. Parmenter (In re Parmenter)*, 527 F. 3d 606, 608, 610 (6th Cir. May 30, 2008)("where confirmed plan assumes car lease and provides for payments directly by debtor to lessor, lease deficiency & attorney

[3] Williamson, John. The Attorney's Handbook on Small Business Reorganization Under Chapter 11. 6th Ed., 2006.

		fees are not administrative expense…")

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Confirmation Standards	Description
Preliminary Steps	Prepare disclosure statement and serve all creditors with a copy of the proposed plan and the ballot. The Court must approve the disclosure statement, although if it is a small business case this step may be consolidated with the Plan confirmation.
Voting Requirements	In a Chapter 11 case, creditors are given the opportunity to vote on the proposed plan. The plan is deemed "accepted" by a class of creditors when the plan is accepted by creditors holding at least 2/3 in dollar amount and more than one-half in number of the allowed claims in the class that were voted in the election. 11 U.S.C. 1126(c). Acceptance requirements are calculated on the amount and number claims that were actually voted in the election. A failure to vote constitutes neither an acceptance nor rejection, but a plan receiving no votes is deemed rejected because it was not accepted.[1]
11 U.S.C. 1129(a)(1)	The Plan must comply with the applicable provisions of the Bankruptcy Code, including 11 U.S.C. 1123, which governs the contents of the Plan itself.
11 U.S.C. 1129(a)(2)	The Debtor must act in compliance with the applicable provisions of the Bankruptcy Code, including compliance with the disclosure and solicitation requirements.
11 U.S.C. 1129(a)(3)	Plan must be proposed in good faith ("Good faith" exists when there is a reasonable likelihood that the plan will achieve a result consistent with the objectives and purposes of the bankruptcy code. *In re Trenton Ridge, citing In re Madison Hotel Assocs.*, 749 F.2d 410, 425 (7th Cir. 1984).
11 U.S.C. 1129(a)(4)	Debtor must disclose terms of payment to be made to any professionals in connection with the plan and incident to the case, and they must be subject to the court's approval.
11 U.S.C. 1129(a)(5)	Debtor must disclose the identity and affiliations of certain individuals, such a directors, insiders, and affiliates.
11 U.S.C. 1129(a)(6)	Debtors overseen by governmental regulatory commissions

[1] Williamson, John. The Attorney's Handbook on Small Business Reorganization Under Chapter 11. 6th Ed., 2006, Section 4.08.

	must receive approval of any rate change to be applied post-confirmation.
11 U.S.C. 1129(a)(7)	The plan must meet the best-interests-of-creditors test, which means that non-consenting, impaired creditors, as of the effective date of the plan, must be paid as must as they would receive in a hypothetical Chapter 7 case.
11 U.S.C. 1129(A)(8)	Each class of claims or interests must have either accepted the plan or not be impaired under the plan.
11 U.S.C. 1129(a)(9)	Unless the creditor agrees to be treated differently, the plan must provide for payment in full in cash on the effective date of the plan of all administrative expenses and all priority claims except tax claims. Plan must provide for each priority unsecured tax claim of a governmental unit in regular installment payments in cash of a total value, as of the effective date of the plan, equal to the allowed amount of the claim over a period ending not later than 5 years after the date of the order for relief, and in a manner not less favorable than the most favored nonpriority unsecured claim provided for by the plan.[2]
11 U.S.C. 1129(a)(10)	If 1 or more classes of claims are impaired under the plan, at least one class of impaired claims (other than an insider class) must have accepted the plan.
11 U.S.C. 1129(a)(11)	Debtor must demonstrate that confirmation of the plan is not likely to be followed by liquidation, or the need for further reorganization. This is commonly referred to as the 'feasibility' test.
11 U.S.C. 1129(a)(12)	All filing fees and quarterly fees payable under 28 U.S.C. 1930, must have been paid or the plan must provide for the payment of all such fees on the effective date of the plan.
11 U.S.C. 1129(a)(13)	Plan must call for the continuation of all retiree benefits after the effective date of the plan.
11 U.S.C. 1129(a)(14)	All domestic support obligations, either pre-petition arrearage, or post-petition payments, must have been paid.
11 U.S.C. 1129(a)(15)	Projected Disposable Income Test: If the Debtor is an individual and the holder of an allowed unsecured claim objects to confirmation, it must be shown that the value, as of the effective date of the plan, of the property to be distributed under the plan is not less than the projected disposable income of the debtor (as defined in 1325(b)(2)) to be received during the five years from first payment due under the plan, or the length of time the plan payments shall be made, whichever is longer.
11 U.S.C. 1129(a)(16)	Property transfers must comply with state law requirements for property transfers by nonprofit corporations and trusts.

[2] Williamson, John. The Attorney's Handbook on Small Business Reorganization Under Chapter 11. 6th Ed., 2006, Section 4.09.

Confirmation by Cramdown 11 U.S.C. 1129(B)	A Chapter 11 Plan can be confirmed by cramdown if all requirements are met except for 11 U.S.C. 1129(a)(8), requiring acceptance of the plan by all impaired classes of claims and interests. To be confirmed by cramdown, the Plan must not "discriminate unfairly," and the Plan must be "fair and equitable" with regard to the nonaccepting impaired class at issue.
Unfair Discrimination	Factors to consider in determining whether discrimination is unfair include: (1) whether the discrimination is supported by a reasonable basis; (2) whether the debtor can confirm and consummate a plan without the discrimination; (3) whether the discrimination is proposed in good faith; and (4) how the class that is being discriminated against is treated. It has been held that a rebuttable presumption that a plan is unfairly discriminatory will arise when "there is: (1) a dissenting class; (2) another class of the same priority; and (3) a difference in the plan's treatment of the two classes that results in … an allocation under the plan of materially greater risk to the dissenting class in connection with the proposed distribution.[3]
"Fair and Equitable"	"Fair and Equitable" has two meanings, one for secured claim and another for unsecured claims: (1) Secured Claims (a) The Debtor can either retain or transfer assets with the liens intact and make deferred cash payments equal to present value of the lender's secured interest in the collateral (determined by 506(a) unless there is an 1111(b) election) (b) The Debtor can sell the collateral free and clear of liens so long as the lien attaches to the proceeds of the sale

[3] Daniel M. Press & Brett Weiss. *Chapter 11 for Individual Debtors: A Collier Monograph*, 2012 Matthew Bender & Co., Inc. Section 9, [7].

"Fair and Equitable" (cont.)	(2) Unsecured Claims Each creditor will receive or retain on account of its claim property, as of the effective date of the plan, equal to the allowed amount of its claim or nothing be paid or retained by any junior class of claims or interests. This is knowns as the Absolute Priority Rule. There is an exception to the absolute priority rule where the debtor can contribute new capital to the business under the plan, in exchange for retaining equity.

Hypothetical One

Joe Debtor appears at your office with the following facts: Mr. Debtor divorced his wife of 12 years approximately 6 months ago after he discovered she was having an affair with his best friend. When Debtor confronted his wife and her boyfriend, an altercation ensued. Using a sledge hammer he had conveniently brought with him, the Debtor caused significant damage to his friend's 2015 Dodge Ram 3500. There is a pending state court action for property damage, and the Answer is due in 7 days.

Shortly after Debtor confronted his wife, the marriage was terminated. The final decree incorporated the terms of the Separation Agreement. It contained the following terms:

1. Debtor received Vir2uall Gaming LLC, a single member company which has 2 million followers. The LLC owes debts of approximately $1,000,000.00, which the Debtor personally guaranteed. The debt is secured by a blanket lien on the company assets, worth $500,000.00. The LLC has an annual cash flow of $700,000.00. After expenses, the net is roughly $75,000.00 annually. Although the LLC was valued at $100,000.00 in the DR case, the Debtor now claims it has no independent value without his personal expertise.

2. Debtor retained a 401k rollover valued at $100,000.00.

3. Wife received the family home worth $500,000.00 subject to a $200,000.00 mortgage. Wife was ordered to refinance within one year, but she has failed to do so. She was also ordered to pay the mortgage of $2,100.00 per month.

4. Wife retained the 2010 BMW 5 series Debtor bought her three years ago when the LLC turned 1 million viewers. There is no lien, and it is valued at $30,000.00.

5. Debtor retained a 2010 Ford Taurus. There is no lien, and it is valued at $12,000.000.

6. Debtor was Ordered to pay the following:
   A. $50,000.00 personal line of credit to Chase Bank secured by his company stock;
   B. credit card debt in the amount of $150,000.00;
   C. a defaulted, co-signed student loan in the amount of $50,000.00.

7. Custody and medical bills (both existing bills and future expenses) for the children were equally divided. Current medical bills for the children total $5,000.00. He has not paid his portion of the medical bills. No child support was ordered because wife earns approximately $50,000.00 per year working for Mr. Debtor's ex-best friend's financial management firm.

8. Debtor was Ordered to pay his ex-wife $1,500.00 per month spousal support for 4 years. He is two months in arrears on his DSO obligation.

Mr. Debtor is not a good business man, but an excellent tech person. His wife handled the LLC's finance side. Since her attention was diverted over the last three years, she failed to prepare any financials for the company. Consequently, no tax returns have been filed for the last two years. He also discovered that although the 2008 tax return was filed timely, the tax liability for 2008, the first year of the company's existence, was never paid. The tax debt is now $8,000.00, including $1,300.00 in penalties.

In addition to owning and operating Vir2uall Gaming LLC, Mr. Debtor shares with you that he has a hobby of collecting and restoring vintage automobiles. He owns about five automobiles in various states of disrepair. The most valuable vehicle is a 1969 Dodge Charger that the Debtor plans to restore for use as his personal vehicle. In its current condition, the Charger is worth $15,000.00, but the Debtor expects its value to triple when he finishes the restoration. Debtor purchased this vehicle two years ago, and he currently owes $21,000.00 on the loan secured by the title.

Debtor needs help and wants to know his best options for protection under the Bankruptcy Code.

Hypothetical Two

Potential clients come to see you about their financial situation. Husband and Wife own and operate a large daycare business. The business is operated out of a large building that the corporation is purchasing specifically for the business. It is a commercial building which has a large fenced in play area with kids yard and the inside has been modified to contain "classrooms" for the different age groups for the children as well as a nursery and a kitchen for preparing meals. The daycare operation cares for approximately forty children and they have owners have four employees that care for the children in addition to the owners. The business is incorporated. The Debtors have owned this business for about eight years but moved into their current location about 5 years earlier. The business did well and the owners purchased a nice home, an expensive travel trailer and a couple of nice vehicles. They owe money on all of their vehicles and there is little equity in their house due to the market.

The business property is worth about $325,000 and has a lien of $262,000. The clients are behind approximately $28,000 on the payments on the building and the bank has foreclosed. There is a sale set for the following week. You also discover that the clients are past due on their property taxes for the building as well and owe for 2013 and 2014. Year 2015 is not due yet. The loan is in the name of the business and the debtors have guaranteed the loan.

The business has various items of business equipment such as computers, printers and software to operate the business and has other equipment such as refrigerators, stoves, a washer and dryer and several microwave ovens plus the usual assortment of children's dishes for eating meals. The value of all of these items is probably around $2500 although the depreciation schedule on the corporate tax returns lists a value of $6000 in 2014. The clients tell you they would be lucky to get $1500 for all the items.

The business also owns two vans for transporting the children one of which is worth about $4500 and the other is only worth $1200. The business is leasing a nicer vehicle the owner drives when she has "to go grocery shopping for the food for the children and to pick up supplies like toilet paper and cleaning products.

The business also owes the IRS about $24,000 which the IRS says is a priority claim for both income and withholding taxes.

The clients have another $70,000 in credit card debt much of which they indicate is for the business but you note that the credit cards all appear to be in the clients names personally. Clients contend that the business has no value because the amount of the credit card debt exceeds the value of the business assets but you suspect they will have a hard time proving the credit card debt is owed by the corporation.

The clients' main objective is to save the building so that they can continue to operate the business. Although they indicate that it does not make much income they are adamant that they want to save the business.

While the Debtors have incorporated their business you suspect that they have not been very good about observing corporate formalities. After reviewing the corporate bank statements and balance sheets you also suspect that reason that the business is behind on its payments has to do with the clients handling of the business. Many of the charges on the corporate account appear to be personal in nature (clearly the ski lift tickets and numerous charges at Bloomingdales were not likely a business expense) and excessive.

What is your suggestion for helping these clients?

Hypothetical Three

Potential clients come to see you about their financial situation. Husband and Wife own 100% of a corporation. The business manufactures electronic components for use in luxury boats. The clients invested a significant amount of money purchasing equipment to manufacture the parts. Unfortunately shortly after the clients started the business the economy took a downward spiral and the demand for these components has dropped to about 15% what the market previously demanded.

The corporation follows corporate formalities and keeps separate bank accounts. The business account has about $4000 in it and the business owns a small trailer they use to transport their products. The trailer is worth about $2500. The business has an SBA loan for $30,000 which is secured by the assets of the business which are worth about $40,000. The SBA loan is also secured by the clients VW Bug worth about $7,000 which has no other liens against it. The clients have personally guaranteed the SBA loan. Wife also works full time as a nurse and helps her husband in the business. They earn about $2500 a month from the business and wife's take home pay is about $3000 per month. The clients are working hard trying to make their business successful. A couple of years ago when the wife went back to work they hired a couple of ladies to try to help the business grow but one of the employees was handling payroll and ended up stealing some money and not paying the withholding taxes. As a result of the theft the clients had to use their personal credit cards to keep the business afloat. Now the business owes the IRS and the state about $19,000 in withholding taxes and penalties. The clients appear sincere and want to save the business.

The clients own a house and are a few months behind in the house payments. There is no equity in the house. The have some outstanding medical debts, about $60,000 in student loans and some credit card bills of approximately $30,000. Although they indicate that the credit card bills belong to the business you do not see that the business name appears on any of the statements except for one which has a balance of $12,000. The husbands name also appears on that account. Additionally they guaranteed the SBA loan for husband's business.

The creditors have started to sue the clients and one has just served wife's employer with a garnishment. The clients were barely able to make their mortgage payments and feed their children before and are now faces with reduced income from the garnishment. They are distraught but know that given the chance they will be able to make their business grow and someday hope to pay everyone back what they owe them. Right now they are barely staying afloat and even with all the belt tightening they have done they can barely scrape up $500 a month to pay towards their debts.

You want to help these new clients. What do you suggest for them and what considerations do you have? What about the co-signed SBA loan and the tax liabilities of the business?

Hypothetical Four

Potential client comes to see you about his financial situation. Thomas John previously owned a business that specialized in home remodeling which he called TJ's Drywall and Home Remodeling, Inc. The business was incorporated in 1997. The business tax returns never showed much of a profit, however you suspect that business expenses are inflated on the tax returns based on the fact that the client is living in a nice subdivision and renting a house that costs about $2200 per month. He also appears to be eating and purchasing clothing despite that his tax returns show about $4000 a year in income.

Client operated this business for 17 years. TJ did not strictly adhere to corporate formalities and essentially had one bank account that he used to pay all expenses such as his rent, his truck, all of his food and utilities and also to purchase his building supplies and pay his help. TJ typically has one employee but brings in additional workers when he lands bigger jobs. Over the years TJ has established relationships with various suppliers an often the invoices are just billed to "TJ". The name on his checking account is "TJ's Drywall."

TJ has fallen on some harder times with the crash of the real estate market. He had a couple of jobs hanging drywall for new home builders but the builders stopped in the middle of construction and TJ was never paid. TJ was never good about paying his withholding taxes or filing his quarterly reports. Over the years he has accrued a couple of large balances on his accounts with some of the local home repair and lumber stores. Recently some of his suppliers have declined to allow him any more credit on building supplies and the IRS has taken funds out of his bank account. He subsequently closed that checking account.

TJ talks to his accountant who advises him to quit operating the corporation and to start a new business so with his accountant's help he dissolves his corporation and files an assumed name with the Secretary of State. TJ's new business is now called "Thomas John's Drywall and Home Remodeling." TJ continues to employ the same worker, obtain jobs from the same contractors and use the same equipment owned by TJ's Drywall and Home Remodeling, Inc. The business has the usual assortment of ladders, compressors, nail guns, hand tools, TJ's 2003 truck which the business has been depreciating but is titled in TJ's name personally and a cargo trailer to haul the equipment in. The truck is worth about $11,000 and the trailer is worth about $2500. He opens a new checking account which has about $1200 in it account. He tells you that all of his prior work has been paid for and that he has no account receivables.

TJ comes to see you as the IRS continues to pursue the past due taxes and the suppliers are getting ready to sue him. TJ understands from his accountant that the purpose of his corporation was to insulate him from personal liability and believes that by dissolving his prior corporation he is now debt free however the IRS and his creditors are still after him and his new business.

How do we help TJ?

Thursday July 2, 2015

4:05 – 5:05 **Evidence:** How to Effectively Examine and Cross-Examine a Witness.
Moderator: Deborah B. Langehennig, Chapter 13 Standing Trustee for the Western District of Texas (Austin)
Honorable Barbara J. Houser, Chief Judge of the United States Bankruptcy Court for the Northern District of Texas (Dallas)
Johnie J. Patterson, II, Walker & Patterson, PC (Houston, TX)

INDEX

Why Bother With The Rules Of Evidence

- You can win a case you should not have won by knowing the rules of evidence.
- You can lose a case you should have won by not knowing the rules of evidence
- You can make your trial go smoothly, to the joy of the court.
- Direct relation to your confidence in the courtroom

Why Bother With The Rules Of Evidence

- **FED. R. BANKR. P. 9017**
  - **"THE FEDERAL RULES OF EVIDENCE AND RULES 43, 44 AND 44.1 F. R. CIV. P. APPLY IN CASES UNDER THE CODE."**
  - RULE 43 – TAKING TESTIMONY:
    - 43(A) - IN OPEN COURT. AT TRIAL, THE WITNESSES' TESTIMONY MUST BE TAKEN IN OPEN COURT UNLESS A FEDERAL STATUTE, THE FEDERAL RULES OF EVIDENCE, THESE RULES, OR OTHER RULES ADOPTED BY THE SUPREME COURT PROVIDE OTHERWISE. FOR GOOD CAUSE IN COMPELLING CIRCUMSTANCES AND WITH APPROPRIATE SAFEGUARDS, THE COURT MAY PERMIT TESTIMONY IN OPEN COURT BY CONTEMPORANEOUS TRANSMISSION FROM A DIFFERENT LOCATION.

Why Bother With The Rules Of Evidence

- **Burden of proof**
- **Standard of proof**
- **Evidentiary issues**
  - **Authenticity**
  - **Admissibility**
- **Trial presentation**

DEMONSTRATIVE EXHIBITS

- EVIDENCE IS EITHER DEMONSTRATIVE OR SUBSTANTIVE.
- DEMONSTRATIVE EVIDENCE GENERALLY ILLUSTRATES SOME VERBAL OR DOCUMENTARY EVIDENCE.
- MUST BE RELEVANT (401), MATERIAL (401) AND COMPETENT/ACCURATE (901 & 902).

DEMONSTRATIVE EXHIBITS

- NOT ADMITTED FOR THE TRUTH ASSERTED.
  - CHARTS AND SUMMARIES ARE VALID ONLY TO THE EXTENT THAT THEY ACCURATELY REFLECT THE UNDERLYING SUPPORTING EVIDENCE.
  - NOT SUBSTANTIVE EVIDENCE.
  - A TRIAL COURT HAS THE DISCRETION TO PERMIT PARTIES TO SHOW THE FACT FINDER CHARTS AND OTHER VISUAL AIDS THAT SUMMARIZE OR ORGANIZE TESTIMONY OR DOCUMENTS THAT HAVE ALREADY BEEN ADMITTED INTO EVIDENCE. *PIERCE V. RAMSEY WINCH CO.*, 753 F.2D 416, 431 (5TH CIR. 1985).

DEMONSTRATIVE EXHIBITS

- Demonstrative Exhibits are not a crutch
- The Power Point is a presentation tool…not magic.

DEMONSTRATIVE EXHIBITS

- What Is Effective?
  - (1) Knowing your audience.
  - (2) Having a conversation, not a lecture.
  - (3) Telling a story.
    - If the demonstrative exhibit takes away from (1),(2), or (3), do not use it.

DEMONSTRATIVE EXHIBITS

- What Is A Demonstrative Exhibit?
  - Photographs,
  - Videos,
  - Charts / Graphs,
  - Summaries.

Must be authenticated or identified pursuant to the Rules of Evidence

DEMONSTRATIVE EXHIBITS

- Photographs/Videos
  - Generally authenticated by the testimony of a person with knowledge of the matter depicted.
  - Testimony must show that the photograph or video fairly and accurately depicts the matter in question.

DEMONSTRATIVE EXHIBITS

- Diagrams, Charts, and Graphs
  - Used to help clarify the testimony of the witness (not substitute).
  - Predicate of accuracy is necessary, even if only admitted for demonstrative purposes.

DEMONSTRATIVE EXHIBITS

- "Would it assist you in your testimony if you had this exhibit available for your use?
  - Map, Google Earth or Chart
  - Photograph
  - Before and After Pictures
  - Blow-ups Of Portions of Documents/Pictures

JUDICIAL NOTICE

- RULE GOVERNS NOTICE OF ADJUDICATIVE FACTS, NOT LEGISLATIVE FACTS.

  – FACT:

  – AN ASSERTION OF FACT IS A DESCRIPTIVE STATEMENT THAT CAN BE FALSIFIED. SUZANNA SHERRY, FOUNDATIONAL FACTS AND DOCTRINAL CHANGE, 2011 U. ILL. L. REV. 145, 150.

JUDICIAL NOTICE

- ADJUDICATIVE FACT
  - FACTS THAT RELATE SPECIFICALLY TO THE ACTIVITIES OR CHARACTERISTICS OF THE LITIGANTS, AND ARE FACTS THAT WOULD TYPICALLY GO TO THE FACT FINDER. BRENDA C. SEE, *WRITTEN IN STONE? THE RECORD ON APPEAL AND THE DECISION MAKING PROCESS*, 40 GONZ. L. REV. 157, 191 (2004)
    - DID THE DEBTOR MAKE THE JANUARY PAYMENT?
    - DID THE CREDITOR DEMAND PAYMENT OF THE PREPETITION CLAIM?
    - WAS THE DEBT ONE FOR ALIMONY, MAINTENANCE OR SUPPORT?

JUDICIAL NOTICE

- LEGISLATIVE FACT
  - GENERALIZED STATEMENTS ABOUT THE WORLD THAT HELP THE COURT DECIDE QUESTIONS OF LAW AND POLICY. SEE, CULP DAVIS, ADMINISTRATIVE LAW TEXT § 7.03 (3D ED. 1972).
  - ANY GENERALIZED FACT ABOUT THE WORLD – NOT SPECIFIC TO THE PARTIES – THAT A JUDGE USES TO DECIDE A CASE.
    - COMMONSENSE CONCLUSION THAT FLEEING FROM A POLICE OFFICER IS A VIOLENT FELONY. SEE, *SYKES V. U.S.*, 131 S. CT. 2267 (2011).
    - GENERALLY ARE SUBJECT TO EXPERT TESTIMONY.
    - ARE NO RULES REGULATING THE USE OF LEGISLATIVE FACTS.

JUDICIAL NOTICE

- FACT MAY BE NOTICED THAT IS NOT SUBJECT TO REASONABLE DISPUTE BECAUSE:
  - GENERALLY KNOWN;
  - CAN BE ACCURATELY AND READILY DETERMINED FROM SOURCES WHOSE ACCURACY CANNOT REASONABLY BE QUESTIONED.
- JUDICIAL NOTICE CAN BE TAKEN AT ANY STAGE OF THE PROCEEDING.
- PARTY IS ENTITLED TO BE HEARD ON THE PROPRIETY AND ON THE NATURE OF THE FACT TO BE NOTICED.

JUDICIAL NOTICE

- PROPER JUDICIAL NOTICE OF ADJUDICATIVE FACTS:
  - NOTICE THAT SPRING INCLUDES THE MONTHS OF MARCH, APRIL AND MAY. *IN RE GOETZ*, 43 B.R. 849, 850 (BANKR. W.D. WIS. 1984).
  - NOTICE THAT FORECLOSURE SALES OCCURRED BETWEEN 10:00AM AND 4:00PM ON THE FIRST TUESDAY OF THE MONTH. *IN RE MARTIN*, 97 B.R. 1013, 1020 (BANKR. N.D. GA. 1989).
  - NOTICE OF THE DOCKET AND THE CONTENT OF THE BANKRUPTCY SCHEDULES AND OTHER DOCUMENTS FILED IN THE CASE FOR THE PURPOSE OF DETERMINING THE TIMING AND STATUS OF EVENTS IN THE CASE. *IN RE BUTTS*, 350 B.R. 12 (BANKR. E.D. PA. 2006), AFF'D 2007 WL 1722805 (E.D. PA. 2007).

JUDICIAL NOTICE

- JUDICIAL NOTICE OF BANKRUPTCY COURT'S OWN RECORDS
  - COURT MAY TAKE NOTICE OF RELATED PROCEEDINGS AND RECORDS IN CASES BEFORE THAT COURT. *STATE OF FLA. BD. OF TRUSTEES OF INTERNAL IMP. TRUST FUND V. CHARLEY TOPPINO & SONS, INC.*, 514 F.2D 700, 704 (5TH CIR. 1975).
  - DOES NOT MEAN THE COURT HAS TAKEN NOTICE OF THE TRUTH OF FACTS ASSERTED IN EVERY DOCUMENT IN THE COURT FILE. *IN RE SCARPINITO*, 196 B.R. 257 (BANKR. E.D. N.Y. 1996)
  - **FACTS/ALLEGATIONS CONTAINED IN PLEADINGS ARE HEARSAY ALLEGATIONS AND SHOULD NOT BE ADMITTED.**

WITNESSES

- Rule 611
  - COURT SHOULD MAINTAIN CONTROL SO AS TO:
    - MAKE PROCEDURES EFFECTIVE FOR DETERMINING THE TRUTH;
    - AVOID WASTING TIME;
    - PROTECT WITNESSES FROM HARASSMENT OR UNDUE EMBARRASSMENT.

WITNESSES

- EXCLUDING WITNESSES – RULE 615 (THE "RULE")
  - AT A PARTY'S REQUEST, THE COURT **MUST** ORDER WITNESSES EXCLUDED.
  - CAN'T BE EXCLUDED:
    - INDIVIDUAL THAT IS A PARTY;
    - DESIGNATED CORPORATE REPRESENTATIVE;
    - PERSON ESSENTIAL TO PRESENTATION OF A PARTY'S CASE;
    - PERSON AUTHORIZED BY STATUTE TO BE PRESENT.

WITNESSES

- EXCLUDING WITNESSES – RULE 615 (THE "RULE")
  - The first strategic decision you will need to make.
  - Are there witnesses other than the parties?
    - If not, no one to exclude
  - Dueling experts, or testimony that is contradictory?
    - Depending on the order of testimony, you may not want to exclude your witness.

WITNESSES

- **WITNESSES 601 – 615**
  - COMPETENCY – RULE 601
    - EVERY PERSON COMPETENT TO TESTIFY.
    - IF STATE LAW DETERMINES CLAIM OR DEFENSE, STATE LAW DETERMINES COMPETENCY
  - PERSONAL KNOWLEDGE REQUIRED – RULE 602
    - WITNESS MAY TESTIFY ONLY IF EVIDENCE IS INTRODUCED SUPPORTING A FINDING OF PERSONAL KNOWLEDGE OF THE MATTER TESTIFIED TO.
    - EVIDENCE TO PROVE PERSONAL KNOWLEDGE MAY COME FROM THE WITNESS'S OWN TESTIMONY.
  - RULE DOES NOT APPLY TO EXPERTS (RULE 703).

WITNESSES

- Cross-Examination:
  - Should not should not go beyond the subject matter of direct;
  - May inquire into witness's credibility;
  - Discretion to allow beyond as if on direct.

WITNESSES

- CROSS-EXAMINATION:
  - Used to control witness and testimony
  - Should only use leading questions
  - Should not give witness an opportunity to explain – no open ended questions

WITNESSES

- LEADING QUESTIONS:
  - NOT TO BE USED ON DIRECT EXCEPT TO DEVELOP WITNESS TESTIMONY IF NECESSARY;
  - SHOULD ALLOW:
    - ON CROSS;
    - WHEN A PARTY CALLS A HOSTILE WITNESS;
    - WHEN A PARTY CALLS AN ADVERSE PARTY;
    - WHEN A PARTY CALLS A WITNESS IDENTIFIED WITH AN ADVERSE PARTY.

WITNESSES

- Direct, or non-leading question
  - Who
  - What
  - When
  - Where
  - Why
  - Describe
  - Explain

WITNESSES

- Witness *Voir Dire*
  - Testimony lacks personal knowledge – Lack of Foundation.
  - Examples:
    - Competency under 601
    - Qualification as an expert 702
    - Personal knowledge 602
    - Authentication 901
    - Unavailability in connection with hearsay exception 804
  - Cross is limited solely to the question of sufficiency of the foundation.

WITNESSES

- Witness *Voir Dire*
  - An objection for lack of foundation may entitle you to an immediate cross-examination of the witness.
  - Think about strategy – taking control.
  - Utilize it to block the introduction of evidence, which would be lost if cross was withheld until AFTER direct

WITNESSES

- Witness Prep
  - A lawyer has a duty to prepare a witness to testify
  - May include discussion concerning the application of law to the events in issue
  - Must "respect the important ethical distinction between discussing testimony and seeking improperly to influence it."
  - *Geders v. U.S.*, 425 U.S. 80, 90 n.3 (1976)

WITNESSES

- Primary Objectives In Preparing A Witness
  - Introduce the legal process
  - Help the witness tell the truth
  - Make sure all relevant facts are disclosed
  - Eliminate irrelevant facts
  - Refresh, but not direct, the witness's memory
  - Provide self-confidence
  - Defend herself during cross-examination

WITNESSES

- In preparing a witness to testify, a lawyer may:
  - Invite the witness to provide truthful, favorable testimony;
  - Discuss the role of the witness;
  - Discuss effective courtroom demeanor;
  - Discuss witness's recollection;
  - Discuss witness's probable testimony;
  - Reveal other testimony or evidence that will be presented, and ask witness to reconsider her recollection in that light;

WITNESSES

- In preparing a witness to testify, a lawyer may:
  - Discuss the applicability of law to the events at issue;
  - Review the factual context into which the witness's observations will fit;
  - Review documents that may be introduced;
  - Discuss the probable lines of cross-examination that the witness should be prepared to meet.
- RESTATEMENT (3RD) OF THE LAW GOVERNING LAWYERS § 116, reporters note to cmt. B (2000) (collecting cases)

WITNESSES

- Practical Advice For The Busy Consumer Lawyer
  - Tell them in advance they will need to testify
  - Tell them to arrive early
  - Talk to them by phone ahead of time
  - Talk to your client before the hearing or during a recess
  - Ask the Court for time

WITNESSES

- Practical Advice For The Busy Consumer Lawyer
  - In general terms, tell the witness WHY the testimony is needed – what is the issue?
  - Do Not tell the witness what the “right answer” is
  - Tell the witness “where”
    - Where you will sit
    - Where they will sit
    - Where they stand to take the oath
    - Where they will sit to testify
    - Where opposing counsel will sit

WITNESSES

- Practical Advice For The Busy Consumer Lawyer
  - Tell the witness the kinds of questions they will be asked – by you and by others
  - Explain the necessity of waiting to answer until questions are finished – The Two Second Rule
  - Importance of answering the question asked
  - Tell the witness proceeding is recorded – Avoid “Uhumm” and “uh uh”, and shaking or nodding of head

WITNESSES

- Practical Advice For The Busy Consumer Lawyer
  - It is ok to say “I don’t know” or “I don’t remember”
  - Show the client the documents
  - Prepare for objections
    - Not directed at witness
    - Stop talking when an objection is raised
    - Explain what “sustained” and “overruled” mean

WITNESSES

- Practical Advice For The Busy Consumer Lawyer
  - Explain the limited focus of hearing
  - Expect cross-examination
    - Stay under control
    - Do not get angry
    - Do not argue
    - Explain re-direct

HEARSAY BASICS

- HEARSAY IS NOT ADMISSIBLE UNLESS PROVIDED FOR BY FEDERAL STATUTE, RULES OF EVIDENCE, OTHER RULES PRESCRIBED BY THE SUPREME COURT – RULE 802
- Hearsay is a statement that:
  - The declarant does not make while testifying at the current trial or hearing; and
  - A party offers in evidence to prove the truth of the matter asserted in the statement.
  - Rule 801

HEARSAY BASICS

- "STATEMENT" INCLUDES ORAL ASSERTION, WRITTEN ASSERTION, AND NONVERBAL CONDUCT, IF INTENDED AS AN ASSERTION – RULE 801(A)

- "DECLARANT" – PERSON WHO MADE THE STATEMENT – RULE 801(B)

HEARSAY BASICS

- STATEMENTS THAT ARE **NOT** HEARSAY – RULE 801(D)
  - THE DECLARANT TESTIFIES AND IS SUBJECT TO CROSS EXAMINATION ABOUT A PRIOR STATEMENT, AND THE STATEMENT
    - IS CONSISTENT WITH THE DECLARANT'S PRIOR STATEMENT AND IS OFFERED TO REBUT A CLAIM OF RECENT FABRICATION, OR TO REHABILITATE WHEN ATTACKED ON OTHER GROUNDS
    - IS INCONSISTENT WITH THE DECLARANTS TESTIMONY AND WAS GIVEN UNDER OATH AT A TRIAL/HEARING OR IN A DEPOSITION.
    - IS INCONSISTENT WITH THE DECLARANT'S TESTIMONY AND IS OFFERED TO REBUT AN EXPRESS OR IMPLIED CHARGE THAT THE DECLARANT RECENTLY FABRICATED IT OR ACTED FROM A RECENT IMPROPER INFLUENCE OR MOTIVE IN SO TESTIFYING; OR
    - IDENTIFIES A PERSON AS SOMEONE THE DECLARANT PERCEIVED EARLIER.

HEARSAY BASICS

- STATEMENTS THAT ARE **NOT** HEARSAY – RULE 801(D)
  - AN OPPOSING PARTY'S STATEMENT THAT IS OFFERED AGAINST THE OPPOSING PARTY, AND
    - WAS MADE BY THE PARTY IN AN INDIVIDUAL OR REPRESENTATIVE CAPACITY;
    - IS A STATEMENT THAT WAS ADOPTED OR BELIEVED TO BE TRUE;
    - WAS MADE BY THE PARTY'S AGENT OR EMPLOYEE ON A MATTER WITHIN THE SCOPE OF THAT RELATIONSHIP, DURING THE RELATIONSHIP; OR
    - WAS MADE BY THE PARTY'S CO-CONSPIRATOR.

HEARSAY BASICS

- EXCEPTIONS TO HEARSAY (REGARDLESS OF WHETHER THE DECLARANT IS AVAILABLE AS A WITNESS) – RULE 803
  - THEN-EXISTING MENTAL, EMOTIONAL OR PHYSICAL CONDITION
    - EX, MOTIVE, INTENT OR PLAN
  - BUSINESS RECORDS
  - ABSENCE OF A RECORD OF A REGULARLY CONDUCTED ACTIVITY: EVIDENCE THAT A MATTER IS NOT INCLUDED IN THE RECORD DESCRIBED ABOVE, IF :
    - THE EVIDENCE IS ADMITTED TO PROVE THAT THE MATTER DID NOT OCCUR OR EXIST;
    - A RECORD WAS REGULARLY KEPT FOR A MATTER OF THAT KIND; AND
    - NEITHER THE POSSIBLE SOURCE OF THE INFORMATION NOR OTHER CIRCUMSTANCES INDICATE A LACK OF TRUSTWORTHINESS. (BURDEN IS ON THE OPPONENT)

HEARSAY BASICS

- EXCEPTIONS TO HEARSAY WHEN DECLARANT UNAVAILABLE – RULE 804
  - "UNAVAILABLE" MEANS
    - COURT RULES THAT A PRIVILEGE APPLIES
    - REFUSAL TO TESTIFY DESPITE A COURT ORDER
    - CANNOT BE PRESENT TO TESTIFY DUE TO DEATH OR THEN EXISTING INFIRMITY, PHYSICAL ILLNESS, OR MENTAL ILLNESS
    - ABSENT FROM TRIAL AND THE PROPONENT HAS NOT BEEN ABLE, BY PROCESS OR OTHER REASONABLE MEANS, TO PROCURE
      - DECLARANT'S ATTENDANCE FOR FORMER TESTIMONY OR RESIDUAL HEARSAY EVIDENCE; OR
      - DECLARANT'S ATTENDANCE OR TESTIMONY FOR (1) STATEMENT UNDER BELIEF OF IMMINENT DEATH, (2) STATEMENT AGAINST INTEREST, OR (3) STATEMENT OF PERSONAL OR FAMILY HISTORY.
    - RULES OF UNAVAILABILITY DO NOT APPLY IF THE STATEMENT'S PROPONENT PROCURED OR WRONGFULLY CAUSED THE UNAVAILABILITY .

HEARSAY BASICS

- EXCEPTIONS TO HEARSAY WHEN DECLARANT UNAVAILABLE – RULE 804
  - FORMER TESTIMONY. RULE 804(B)(1) TESTIMONY THAT
    - WAS GIVEN AS A WITNESS AT A TRIAL, HEARING, OR LAWFUL DEPOSITION (CURRENT OR DIFFERENT PROCEEDING); AND
    - NOW OFFERED AGAINST A PARTY WHO HAD AN OPPORTUNITY TO DEVELOP IT BY DIRECT, CROSS, OR REDIRECT EXAMINATION
  - STATEMENT UNDER THE BELIEF OF IMMINENT DEATH
  - STATEMENT AGAINST INTEREST 804(B)(3)
    - A STATEMENT THAT A REASONABLE PERSON IN DECLARANT'S POSITION WOULD HAVE MADE ONLY IF THE PERSON BELIEVED TO BE TRUE BECAUSE IT WAS CONTRARY TO DECLARANT'S PECUNIARY INTEREST, OR HAD A GREAT TENDENCY TO INVALIDATE THE DECLARANT'S CLAIM AGAINST SOMEONE ELSE
  - STATEMENT OF PERSONAL OR FAMILY HISTORY
  - STATEMENT OFFERED AGAINST A PARTY THAT WRONGFULLY CAUSED THE DECLARANT'S UNAVAILABILITY

BUSINESS RECORDS

- Business Records
- Hearsay Exception – 803(6)

BUSINESS RECORDS

- Rule 803(6) followed Uniform Act by providing for admission of the record if the custodian or other qualified witness testifies to its identity and the mode of its preparation.
- The rationale underlying the business records exception to the rule against hearsay is that the inherent reliability of business records is "supplied by systematic checking, by regularity and continuity which produce habits of precision, by actual experience of business in relying upon them, or by a duty to make an accurate record as part of a continuing job or occupation." Fed. R. Evid. 803(6), Notes of Advisory Committee on Proposed Rules.

BUSINESS RECORDS

- The record of an act, event, condition, opinion, or diagnosis is not excluded by hearsay if:
  - 1 Record is contemporaneous ("made at or near the time")
  - 2 Record created by someone with knowledge, or from information transmitted by someone with knowledge
  - 3 It is a record maintained
  - 4 The making of the record was a regular practice of the business
  - 5 Nothing about the source or the circumstances indicates a lack of trustworthiness.

BUSINESS RECORDS

- The record of an act, event, condition, opinion, or diagnosis is not excluded by hearsay if:
  - the record was kept in the course of a ***regularly conducted activity of a business,*** organization, occupation, or calling, whether or not for profit;
    - "Regularly conducted business activity"
      - » All types of commercial operations
      - » Every variety of business, as long as the routine of such body is characterized by the type of formality that guarantees the requisite degree of reliability.
      - » Records of illegal enterprises admissible if other elements satisfied
      - » Rule extends to sole proprietors and the records of individuals operating as independent contractors
      - » Records prepared and maintained by an individual concerning purely personal matters are not included in the exception

BUSINESS RECORDS

- The record of an act, event, condition, opinion, or diagnosis is not excluded by hearsay if:
  - **the record was kept in the course of a regularly conducted activity of a business**, organization, occupation, or calling, whether or not for profit;
    - Must be a record that is regularly maintained in the business
    - the record must be prepared and maintained as part of the regular practice of the business
      - » This requirement is supportive of trustworthiness, and its practical impact is to exclude records prepared solely in anticipation of potential or pending litigation.
      - » Must be made pursuant to established company procedures for the systematic or routine and timely making and preserving of company records, and relied upon by the business in the performance of its function. See Advisory Committee Note.

BUSINESS RECORDS

- Record must be made by a person with knowledge
  - All persons who participate in the initial furnishing of information must possess personal knowledge of the matters related
  - All persons furnishing and recording the information must be under a duty to do so.

BUSINESS RECORDS

- The record of an act, event, condition, opinion, or diagnosis is not excluded by hearsay if:
  - making the record was a regular practice of that activity
  - Absence of routineness may result in a lack of motivation to be accurate
  - Excludes all records prepared for litigation
  - See *Palmer v. Hoffman*, 318 U.S. 109 (1943)

BUSINESS RECORDS

- The record of an act, event, condition, opinion, or diagnosis is not excluded by hearsay if:
  - all these conditions are shown by the testimony of the custodian or another qualified witness, or by a certification that complies with Rule 902(11) or (12) or with a statute permitting certification
  - No custodian (or other qualified witness), no authentication

BUSINESS RECORDS

- Self Authenticating Business Records – 902(11)
  - Original or copies of documents which satisfy 803(6);
    - As shown by a certification of the custodian or another qualified person;
  - Proponent must give an adverse party ***reasonable written notice*** of the intent to offer the record, AND
  - Must make the records and the certification available for inspection.
  - A qualified witness is one who can explain the record keeping system of the organization and vouch that the requirements of Rule 803(6) are met. *United States v. Brown*, 553 F.3d 768, 792 (5th Cir.2008)

BUSINESS RECORDS

- Missing Records
  - *E.g.*, chapter 7 debtor has destroyed accounting records
    - *U.S. v. Wells*, 262 F.3d 455 (5th Cir. 2001) (Drug ledgers routinely destroyed every week; oral testimony of "bookkeeper" disallowed as hearsay)
    - Destroying records on a regular basis may preclude a finding of keeping them in the course of a regularly conducted business activity
    - See 1004 – Lost or destroyed originals

BUSINESS RECORDS

- Records not created by business sometimes included in business records exception
  - *United States v. Duncan*, 919 F.2d 981, 986-87 (5th Cir. 1990) (concluding there was "no requirement that the [business] records be created by the business having custody of them"; insurance company custodians could provide foundation to admit records compiled by those companies from the business records of hospitals)

BUSINESS RECORDS

Business Records Mnemonic

- **W**hat – *What* is this document
- **P**et – Are you familiar with the *practices* of the business as to the creation and preservation of the document
- **O**wners – Is this created in the *ordinary course* of the business
- **C**all – Was this made *contemporaneously*
- **P**ets – Was this created by a *person with knowledge?*

Thursday July 2, 2015

4:05 – 5:05 **Claims Madness:** Trips and Traps of Filing Claims, Objecting To Claims, Not Objecting to Claims, and Unfiled Claims.
Moderator: Isabel C. Balboa, Chapter 13 Standing Trustee for the District of New Jersey, Camden Vicinage (Cherry Hill)
Honorable Cynthia A. Norton, United States Bankruptcy Judge for the Western District of Missouri (Kansas City)

INDEX

Cynthia A. Norton
U.S. Bankruptcy Judge
W.D. of Missouri, at Kansas City
April 24, 2015

CLAIMS MADNESS

Part One: Introduction and Background

The claims allowance process has always been ripe for bad behavior. Beyond **Rule 9011** and the criminal penalties for filing a false claim, what are the ethical considerations in:

- ► Filing claims?
- ► Failing to file claims?
- ► Signing claims?
- ► Objecting to claims?

Does signing a claim make you a witness? And what ethical ramifications are there when a debtor or trustee files claims on behalf of a creditor under **Rule 3004** – are there conflicting duties to the debtor, to the estate and to the creditor on whose behalf the claim is filed? Have any of the ethical considerations changed in light of recent amendments to **Rule 3001** in December 2011 and 2012, respectively, that in subsection **(c)(2)** imposed on claims-filers additional requirements in individual debtor cases and included a mechanism for sanctions, and that in subsection **(c)(3)** removed the requirement of documentation for holders of open-end or revolving credit debt? Should it change if you are in a judicial district that allows claims objections to be granted by default without a hearing?

This section will address recent claims decisions and the potential ethical issues these decisions raise. A note of caution: in light of the two recent amendments to **Rule 3001**, cases preceding the amendments may or may not retain persuasive effect.

Part Two: Dissection of Rule 3001

So, let's start with the precise language in **Rule 3001**, and to fully understand the issue, we start with one of the last subsections of **Rule 3001**, **subsection (f)**. **Rule 3001(f**), which gives **Rule 3001** its "teeth," provides:

> A proof of claim *executed and filed i*n accordance with these rules shall constitute *prima facie evidence* of the validity and amount of the claim.

(emphasis added).

Turning back, then, to the rest of **Rule 3001:**

► ***General Rule***: **Rule 3001** is the general rule governing the filing of proofs of claim.

► ***Substantial Compliance Required***: **Rule 3001(a)** requires that a proof of claim conform substantially to the Official Form.

► ***Execution by Creditor/Authorized Agent*****: Rule 3001(b**) requires that when the creditor is filing the claim, the claims shall be executed by the creditor or its authorized agent.

Rule 3001(c), governing the *documentation requirement*s, contains the recent amendments, and has several subparts.

► **Rule 3001(c)** originally required a copy of the writing *when a claim is based on a writing* or an interest in property or, if the writing has been lost or destroyed, a statement of the circumstances of the loss or destruction. The documentation requirement still applies, **EXCEPT** for open-end and revolving credit claims in individual debtor cases, discussed below.

QUERY: ***What is the remedy for a creditor's failure to provide documentation or who only provides insufficient documentation?*** Prior to the amendments (and to some extent after the amendments), courts were generally divided into two camps, the "exclusive view" and the "non-exclusive view." The majority exclusive view is that **§ 502(b)** sets forth the exclusive grounds for disallowance of a claim, and failure to file documentation is not among them. Therefore, an objection to a claim based solely on the claimant's failure to attach documents required by **Rule 3001** is without merit. *E.g.*, *In re Brunson*, 486 B.R. 759, 769-70 (Bankr. N.D. Tex. 2013) (Houser, J.). Under the minority view, the failure to attach sufficient documentation to a claim can result in disallowance if, after an objection, a creditor does not prove its claim by a preponderance of the evidence. *E.g*., *In re Lytell*, 2012 WL 253111 (E.D. La. Jan. 26, 2012); *In re Gulley*, 400 B.R. 529 (Bankr. N. D. Tex. 2009); *In re Armstrong*, 320 B.R. 97 (Bankr. N.D. Tex. 2005).

► Added Effective December 1, 2011: **Rule 3001(c)(2)(A) – (D)** imposes additional requirements in individual debtor cases and includes a mechanism for sanctions. As noted by Judge Houser in *Brunson*, 486 B.R. 759, 769-70 the judicial disagreement between the exclusive and non-exclusive camps should be resolved by the December 1, 2011 amendments adding subsections **(c)(2)(A) – (D),** since a creditor's failure to follow the Rule does not result in automatic disallowance. Rather,

►**Rule 3001(c)(2)(A):** ***Itemization Required*****:** requires the creditor file an itemized statement of any interest, fees, expenses, or other charges incurred before the petition was filed.

►**Rule 3001(c)(2)(B):** ***Cure Amount Required:*** requires a secured creditor to include a statement of the amount necessary to cure any default as of the date of the petition.

►**Rule 3001(c)(2)(C):** ***Home Mortgage Escrow Required*****:** requires the creditor whose interest is in the debtor's principal residence to include an attachment prescribed in the Official Forms and, if there is an escrow account, an escrow account statement in a form consistent with applicable nonbankruptcy law.

►**Rule 3001(c)(2)(D):** ***Remedy*****:** provides that if the claimholder fails to provide any information required by subdivision (c), the court may, after notice and a hearing, take either or both of the following actions:

(i) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or

(ii) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure.

► Added Effective December 1, 2012**: Rule 3001(c)(3)(A): Documentation Exception for credit-card like creditors and their collection agents/claims buyers:**

When a claim is based on an open-end or revolving consumer credit agreement – except one for which a security interest is claim in the debtor's real property – the creditor shall include a statement with all of the following information that applies to the account:

(i) the **name** of the entity from whom the **creditor purchased** the account;

(ii) the **name** of the entity to whom the debt **was owed** at the time of an account holder's last transaction on the account;

(iii) the **date** of an account holder's **last transaction**;

(iv) the **date** of the **last payment** on the account; and

(v) the **date** on which the account **was charged** to profit and loss.

Rule 3001(c)(3)(B): Ability of Debtor/Trustee to Request the Writing: On written request by a party in interest, the holder of a claim based on an open-end or revolving consumer credit agreement shall, within 30 days after the request is sent, provide the

requesting party a copy of the writing specified in paragraph (1) of this subdivision [the writing on which the claim is based].

Part Three: Legal & Ethical Issues Raised

The amendments raise several legal and ethical issues. Recognizing that **Rule 9011** still applies to claims, in addition to ethical obligations under **MRPC 3.1** (meritorious claims and defenses) and **MRPC 3.2** (expediting litigation) the following questions remain:

► Is the debate between exclusive view/non-exclusive view resolved?

► Is it ever ethical to object to claims based on lack of documentation? Does it make a difference if your district allows claims objections to be sustained by default?

► Is there still a basis to ask for disallowance? Is that ethical?

► What do you do with secured creditors who refuse to file claims?

► Do the itemization requirements in particular make it risky for a trustee to file a claim on a creditor's behalf?

► Is there still some way to deal with abusive claims filing/claims objections practices?

► What are "best practices" for debtors, creditors, and trustees in filing and objecting to claims? What type of evidence will it take for a debtor to defeat the claim of a claims buyer? When should the Amendments be applied retroactively? Under what circumstances should you be entitled to attorney fees?

Part Four: Case Law Summary:

When a secured creditor doesn't file a claim in Chapter 13 or the claim is late:

In re Dumain, 492 B.R. 140 (Bankr. S.D.N.Y. 2013) (Morris, C.J.). Chapter 13 debtor objected to late- filed claim of secured creditor; discussing the three approaches to creditor bar dates; (1) that the omission of secured creditors from **Rule 3002(a)** (necessity of filing a claim) means that secured creditors have no bar date, e.g., *In re Strong*, 203 B.R. 105, 111-12 (Bankr. N.D. Ill. 1996); (2) the secured creditor must comply with a bar date, but not necessarily the bar date provided in **Rule 3002(c)** (i.e., completion of plan payments, or the filing of a trustee's final report, or some other date); and (3) secured creditors musts comply with the bar date. The court adopts the third approach in light of the plain language in **§ 502(b)(9)**; neither the plan nor the schedules created an informal proof of claim.

Commented [DC1]: This case has been disagreed with by In re Pajian, 508 B.R. 708 (Bankr. N.D. Ill. 2014) – I didn't know if you'd want to add this or leave as is

Compare In re Pajian, 508 B.R. 708 (Bankr. N.D. Ill. 2014) (Cassling, J.) (noting that the policy considerations underlying the *Dumain* court's approach – that it is unfair to permit a secured creditor to file a proof of claim after a plan has been confirmed – are not present in the 7th Circuit; since the 7th Circuit holds that a confirmed plan is a binding contract between the debtor and the creditors, so long as the proof of claim is filed before confirmation, no unfairness occurs; overruling the debtor's objection to the secured portion of the claim but sustaining the objection as to the unsecured portion).

In re Barker, 2014 WL 1273765 (B.A.P. 9th Cir. Mar. 28, 2014) (not designated for publication). Bankruptcy court did not err in disallowing late-filed claims in chapter 13; no informal proof of claim; no judicial admission doctrine.

PRACTICE TIP: Creditors' lawyers may be able to create an informal proof of claim for their clients by including language sufficient to prove the four elements in their entry of appearance. To constitute an informal proof of claim under *Dumain* a document must have been (1) timely filed with the bankruptcy court and part of the judicial record; (2) state the existence and the nature of the debt; (3) state the amount of the claim against the estate; and (4) evidence the creditor's intent to hold the debtor liable with the debt.

PRACTICE TIP: Debtors' lawyers may be able to file a late claim on the secured creditor's behalf under **Rule 3004** and **Rule 9006(b)(1)** on the grounds of excusable neglect (Credit to Judge William Houston Brown).

QUERY: Is there authority to compel a secured creditor to file a claim?

When the secured creditor's claim has been expunged:

In re Jimenez, 492 B.R. 373 (Bankr. S.D.N.Y. 2013) (Morris, C.J.) Secured creditor can't compel the Chapter 13 debtor to surrender or abandon the property, once the creditor obtained stay relief and the debtor had expunged the claim.

When the creditor refuses to attach documentation:

Lack-of-Documentation Claims Objections No Longer Allowed*: In re Brunson*, 486 B.R. 759 (Bankr. N.D. Tex. 2013) (Houser, J.) Amended **Rule 3001** would be applied retroactively to chapter 13 debtors' case filed before the effective date of the amendment; debtors' blanket claims objections to scheduled claims based solely on lack of documentation could not be sustained.

Accord; And, Debtors Can't Avoid the Result by Recharacterizing the Objection as a Standing Argument. *In re Gorman*, 495 B.R. 823 (Bankr. E.D. Tenn. 2013) (Rucker, J.) The alleged lack of supporting documentation was not a valid basis for objecting to a proof of claim filed by assignee of credit card account, even if debtor's recharacterized the objection as an objection to standing.

The creditor, through a servicer, filed a claim for $365 on Feb. 23, 2011. The basis for the debt was a Mastercharge account ending in 6639. The claim included a statement that provided an account number, the amount of the debt, and the date the debt was charged off. The place for last transaction date was blank. The chapter 13 debtors objected to the claim on the grounds that the documentation as to ownership of the claim was not attached, and that a power of attorney was not attached to establish an appropriate agency relationship for the servicer to file the claim. Debtors had scheduled the claim as disputed. The court finds there is support for most of the debtors' argument, but it is the minority view, *citing In re Richter*, 478 B.R. 30 (Bankr. D. Colo. 2012); the court was bound to follow the majority view of the 6th Circuit, *B-Line, LLC v. Wingerter*, 594 F.3d 931, 941 (6th Cir. 2010).

The debtors argued that the claim lacks validity because it violated **Rule 3001**, because the servicer failed to provide evidence of its authority, and no statement of the loss of that evidence was attached. But failure to attach a power of attorney is not a violation of **Rule 3001(b); Rule 9010 s**tates that evidence of a power of attorney is not required for the execution and filing of a claim; claim was thus in substantial conformity. Plus, the Official Form 10 was changed in 2012 to delete the direction that an authorized agent must attach a power of attorney if one existed. However, claim did not comply with the version of **Rule 3001(c)(1**) in effect at the time the claim was filed since no documentation attached; not fair to apply new **Rule 3001(c)(3)** retroactively, even though the objection was filed after the effect of the subsection **(c)(3).**

Standing: An allegation of lack of documentation is not a valid objection even if the debtors re-characterize it as an objection to standing. A valid objection to standing must raise a factual dispute about who is the holder of the claim. The debtors must allege that, to the best of their knowledge, information, and belief, either (a) they owe someone else or (b) they do not owe the obligation at all. In addition, the court does not find support for holding otherwise based on debtor's desire to impose a heavier burden on creditors in order to lighten the debtors' burden to review the proofs of claims which have been filed, especially when the burden is imposed by the Bankruptcy Code and Rules.

And, Debtors Can't Avoid This Result By Scheduling Debts as Disputed: *In re Rehman*, 479 B.R. 238 (Bankr. D. Mass. 2012) (Hoffman, J.). Pre-amendment to **Rule 3001(c)(3)**, alleged deficiencies in supporting documentation attached to proofs of claim for credit card debt filed by creditors that had attached account summaries and the like did not constitute ground for disallowance of proofs of claim; debtor was estopped, when she listed unsecured debts in precise amounts and with the same account numbers as the credit card debts but listed as "disputed," when she did not contest she owed the debts.

Alleged Abuse of Claims Process Can't Be Raised as Claim Objection; Need an Adversary. *In re Stow*, 2013 WL 3199825 (Bankr. E.D. Tenn. June 24, 2013) (Rucker, J.).

Debtor objected to claims to which no documentation was attached, and argued that creditor's intentional decision not to comply with **Rule 3001(c)** or oppose the objections was an abuse of the bankruptcy system. The court found that the remedy is generally loss of the evidentiary presumption contained in **Rule 3001(f),** unless the creditor fails to respond or does not oppose disallowance. Debtor did not file a **Rule 11** motion. If the debtor seeks further relief, such as an injunction or a claim for damages for abuse of process, an adversary proceeding must be filed. **Rule 7001(1), (7).**

But If You Are Going to File an Adversary, Don't Delay: Adversary Complaint Alleging Abuse of Claims Process Not Untimely Per Se, But Debtors Didn't Show Cause to Relitigate or Impose Sanctions, Particularly Given Their Delay. *In re Ruth*, 473 B.R. 152 (Bankr. S.D. Tex. 2012) (Bohm, J.) Months after the court entered an order allowing all claims based on the Chapter 13 Trustee's notice, the debtors filed a complaint against unsecured creditor (LVNV Funding) seeking disallowance (reconsideration) of the claim, actual and punitive damages for vexatious litigation and sanctions against the creditor based on the conduct of allegedly willfully and intentionally filing thousands of proofs of claim without sufficient supporting documentation. The court rejected the creditor's argument that the complaint was untimely; **§ 502(j),** governing reconsideration of claims, imposes no time constraints. However, **§ 502(j)** should not be used as a means to rehash already litigated issues; if already litigated, claims reconsideration should be limited to a one year limitation under **Rule 60(b)** standards as incorporated by **Rule 9024**. Here, the allowance of the claim was not litigated, so court could exercise its "virtually plenary" discretion and the equities of the case to determine whether the claim should be reconsidered.

The court agreed that the documents attached to the claim were insufficient to conclusively establish that the creditor was the present holder of the debt, but debtors put on no evidence rebutting the presumption of validity of the claim. In addition, the proffered reason of debtor's counsel for waiting to object – that he didn't think it was economically prudent to object but then changed his mind – was not a sufficient reason. "For the Chapter 13 system to operate efficiently and effectively, the Chapter 13 trustee, and all creditors who have filed claims, need to know relatively soon what the universe of allowed claims will be so that the trustee can make the proper distribution to creditors once the plan is confirmed." The court agrees that filing a claim with amount for "unsecured chargeoff" and last 4 digits of account number is insufficient and in bad faith, but declines to award sanctions under inherent power given the debtors' delay in objecting, and debtors have no standing to object to claims filed in cases other than their own. Debtors' claim for vexatious litigation similarly fails.

"Creditors should not be permitted to deliberately file woefully deficient proofs of claim in the hope that the debtor will not object to their violations of **Rule 3001** … [but] it is still

incumbent on all debtors (including the Plaintiffs here) to timely file objections to proofs of claim pursuant to the Local Rules and notices sent by the trustee…"

And, Adversaries Likely Don't Work Anyway: *In re Poteet*, 2011 WL 3626696 (Bankr. E.D. Tenn. Aug. 17, 2011) (Cook, J.) Chapter 13 debtors filed an adversary complaint against eCast, alleging that the five proofs of claim it filed were not supported by documentation and, based on this allegation, seeking damages for alleged violations of the automatic stay, **Rule 3001(c)** and the **FDCPA**. The bankruptcy court granted the defendant's motion to dismiss for failure to state a claim. "If the proof of claim is inaccurate or incomplete, the debtor's remedy is to object to the claim…" In addition, **Rule 3001** does not provide a remedy for failure to comply, and there is no basis for creating a private right of action under the rule; violation of the rule does not result in sanctions. *B-Line, LLC v. Wingerter (In re Wingerter)*, 594 F.3d 931, 941 (6th Cir. 2010). Also, the filing of a proof of claim in a bankruptcy case is not a violation of the **FDCPA**.

Accord*; In re Turner*, 2011 WL 4352158 (Bankr. E.D. Tenn. Sept. 16, 2011) (Rucker, J.) In granting creditor's motion to dismiss a *Poteet*-type complaint for failure to state a claim, the court notes that even inaccurate claims filed do not violate the stay; even for failure to provide insufficient documentation, the result is not a cause of action against the creditor, but, rather, the loss of the creditor's prima facie validity for its proof of claim; debtor's claim fails to state fraud with particularity under **Rule 9(b)**; debtor's request for sanctions denied for failure to comply with the **Rule 11** 21-day safe harbor requirement.

> ►***Compare: Times Have Changed****: In re Garvida*, 347 B.R. 697 (B.A.P. 9th Cir. 2006) (sustaining objection to arrearage amounts in proof of claim where creditor failed after numerous requests to produce itemization).

Compare: When the Chapter 13 Trustee Files the Claims: *In re Richter*, 478 B.R. 30 (Bankr. D. Colo. 2012) (Romero, J.). Chapter 13 debtors in 100% plan objected to claims filed by two credit card creditors who had failed to attach documentation and evidence of any assignment, and on the grounds of standing to file claims. Debtors had scheduled one creditor, and not the other. One creditor later amended its claim and attached documentation. The creditors did not respond to the objection, but the Chapter 13 Trustee responded, arguing that the objections to claims based on lack of documentation should not be upheld, under *In re Reynolds*, 470 B.R. 138 (Bankr. D. Colo. 2012), and that the remedy for a **Rule 3001(c)(2)(D**) violation was not disallowance. The debtors responded that the Chapter 13 Trustee lacked standing to respond on the creditors' behalf. The Trustee proposed to show cause the creditors to compel them to intervene, but rather than file such a motion, the Trustee filed a supplemental motion, arguing that **Rule 3001** doesn't require proof of an assignment, and that an evidentiary hearing should be set to allow the creditors a last opportunity to defend. The debtors moved to strike the response.

The court held that the Trustee has standing, particularly in a 100% payment plan case; that the first creditor was allowed to amend after the bar date and the amended claim be deemed timely since the substantive content was the same; debtors' objection to the amended claim was therefore moot. With respect to the assigned creditor who had attached no documentation, the court noted the three approaches for whether documentation of an assignment needs to be attached to the claim; assignment not required in reliance on **Rule 3001(e)(1);** assignment required; and the middle-approach (requiring evidence of ownership). The court believes some documentation evidencing assignment is required. This creditor could not rely on the presumption of validity.

The court expressed its concern at several points in the opinion regarding the Trustee's actions in responding when the original creditors had not, but held that an objection to standing is a substantive objection that debtors could proceed with, and that since one of the claims was not entitled to the presumption of validity, the trustee had put himself in the awkward position of having to defend the creditor's proof of claim and that the trustee bore the burden of establishing that the creditor held an enforceable claim. The motion to strike the trustee's response was denied.

Compare: When the Debtors Offer Testimony*: In re Pursley*, 451 B.R. 213 (Bankr. M.D. Ga. 2011) (Laney, C.J.) (objections to eCAST claims; debtors overcame presumption of validity by offering testimony that they didn't know anything about eCAST, and had not owed eCAST any money; in addition, eCAST's attorneys refused to provide information).

When the creditors' documentation is insufficient:

Substantial Compliance OK; Discussing Standard of Testimony/Evidence Required, & Limited Disagreement with Pursley*: In re Crutchfield*, 492 B.R. 60 (Bankr. M.D. Fla. 2013) (Walker, J.). Applying amended **Rule 3001(c)(3)** with respect to open-end credit agreements to Chapter 13 case filed before the effective date, and overruling the debtor's objection to 7 unsecured claims on the grounds of insufficient documentation; although none of the proofs of claim provide 100% of the information required under **Rule 3001(c)(3)**, the missing information does not affect the ability of the debtor to match the claim to a known and acknowledged debt; in each case, the account summary provided additional information not expressly required by the Rule that can be useful in identifying a corresponding debt; finding substantial compliance.

The court disagrees with *Pursley* in two respects; the court is unpersuaded that a debtor's testimony that he never made any agreement with the entity who filed the claim; he never received any notice of assignment of the claim; never received any correspondence from the assignee; never heard of the assignee; and has no knowledge he owes money to assignee would be sufficient to rebut the evidentiary presumption; second, *Pursley* focused on whether the creditor could prove its assignment under state law by establishing that it was

the proper party in interest to enforce the claim; enforceability of a claim under **§ 502(b)(1)** refers to the nature of the claim, not the sufficiency of the proof.

Accord; Debtors Will Need to Present Evidence*: In re Goeller*, 2013 WL 3064594 (Bankr. E.D. Va. June 19, 2013) (Mayer, J.) Objections to claims on grounds of insufficient documentation had to be set for evidentiary hearing, and in one case, re-served; discussing the requirements of the various subsections of **Rule 3001** and the remedies:

"The underlying principal governing these objections is that the bankruptcy claims process should be simple and straight-forward so that creditors can be promptly paid. This objective is furthered if creditors are able to file claims without undue expense or burden. At the same time, there must be standards so that trustees, debtors and other creditors can reasonably determine whether filed claims are proper. **Rule 3001** endeavors to balance these competing principles. Mere non-compliance with the informational requirements of **Rule 3001** such as attachment of documentation or providing specific information should not be, in and of itself, grounds to disallow the claim. If the proof of claim can reasonably be analyzed, it should not be summarily disallowed because it does not fully comply with the informational requirements of **Rule 3001**, but the creditor may be sanctioned for the non-compliance. Substantive objections on the merits of a claim, such as an incorrect calculation of the claim, that the claim is not owed or that payments have not been credited, are favored over objections to technical or procedural defects. In this case, there is a mix of both types. It is necessary to determine who the creditors are and the amounts of their claims. Objections intended to resolve these issues are entirely proper. Objections intended to eliminate claims so that a chapter 13 plan will "work" do not further the objectives of the bankruptcy claims process. Courts have some discretion with respect to default judgments. In this instance, the matters must be set for a hearing and the debtors must present evidence to support their objections."

Accord; Debtors Failed to Present Evidence: *In re Umstead*, 490 B.R. 186 (Bankr. E.D. Pa. April 3, 2013) (Frank, C.J.). Chapter 13 debtor's objection to proofs of claims allegedly owing on debtor's credit card account, disputing whether the claimants were the owners of the accounts, overruled. Claims were substantially in compliance; failure of proof of claim to specify the "last payment" and the "last transaction" did not deprive claim of prima facie evidentiary status, particularly given debtor's failure to introduce *any* evidence disputing the validity or the amount of the claim.

Accord; No Evidence, But What About State Law? State Law Requirements May Not Be Relevant: *Matter of Berardi*, 2013 WL 6096227 (Bankr. D.N.J. Nov. 20, 2013) (Wizmur, J.) The Chapter 13 debtors seek here to expunge a proof of claim filed on behalf of an alleged assignee of credit card debt owed by one of the debtors. The debtors contend that the claim is unenforceable under state law because there is no evidence of a clear

assignment attached to the proof of claim and no proof that notice was given to the debtors of the purported assignment. Because the proof of claim meets all filing requirements and is entitled to a presumption of validity, and because the debtors have failed to produce any evidence to rebut the presumption, the debtors' motion to expunge is denied.

"Although the last payment date is obviously in error, I can readily determine that enough information has been provided to substantially comply with the rule and afford enough information to allow the debtors to identify the debt. (cite omitted). In this case, the names of the card issuer, Applied Bank and Applied Card Systems, are similar enough to put the debtor on notice, and the amount scheduled by the debtors, $1,508, and the amount in the proof of claim, $1,508.13, are practically identical. The debtors' further challenge to the validity of the assignment under state law, based on their contention that New Jersey law requires notice to be given to a debtor of any assignment before a valid assignment of that interest can exist, must also fail on the same ground. Even if the debtors are correct that notice of the assignment to the debtors is required, a proposition I disagreed with in *Lafferty*, *[*2012 WL 6645729, Bkrtcy.D.N.J., December 19, 2012], the debtors have produced no facts to establish that the debtors failed to receive such notice. In the absence of any evidence to negate the prima facie validity of the filed claim, the objection must fail."

Accord; State Law Did Not Render Claim Unenforceable. *In re Nussman*, 501 B.R. 297 (Bankr. E.D.N.C. 2013) (Humrickhouse, J.). Rejecting debtor's argument that the creditor was a claims buyer under applicable North Carolina law, and thus was required to attach additional documentation; the state law requirements were pleading requirements for state law collection suits; filing a proof of claim does not constitute a collection effort and failure to comply with the state law did not render the claim unenforceable.

Accord; And Possible Bad Faith of Chapter 13 Debtors. *In re Hill*, 2014 WL 80157 (Bankr. E.D. Ky. Feb. 28, 2014) (Wise, J.). Debtors' blanket objections to credit card claims filed by third party collectors or servicers were overruled; the claims substantially complied with **Rule 3001(c)(3);** the claims were not scheduled as disputed. "Finally, if the Debtor had a sincere question regarding the documentation underlying the claims, she could have made the written request to the creditor as provided in sub-part (B) of **Rule 3001(c)(3)**. Instead of complying with the procedural rules, the Debtor has pursued litigation." Chapter 13 Trustee's objection that plan was not proposed in good faith was not addressed, since debtors had to amend plan anyway. "The amendment matters. The requirements of amended **Rule 3001(c)(3)(A)** *replaced* the requirement of attaching the original contract *unless* the documents are requested from the claimant pursuant to **Rule 3001(c)(3)(B)**."

"The claims process is intended to be a simple, manageable process—not one full of pitfalls that prevent legitimate claims from being paid. The harder courts make it for legitimate creditors to get paid, the farther they get from the goals of bankruptcy and the pursuit of justice." (cites omitted). The Debtor's objections appear to be attempts to prevent legitimate claims from being paid, and to create costs and time consuming difficulties for creditors in having to prove their claims in ways not required by the Bankruptcy Rules. The Debtor has made no allegation that the debts are owed to someone else, or that the debts are not owed at all. In short, the claimants' documentation is sufficient and the Debtor's standing arguments are without merit."

And don't forget, Rule 11 is still alive and well:

***Rule 11 Against Creditor's Attorney**: In re Obasi*, 2011 WL 6336153 (Bankr. S.D.N.Y. Dec. 19, 2011) (Lane, J.) (creditor's attorney's practice of filing proofs of claim without review of the signing attorney constituted a clear violation of **Rule 9011**; however, court denies the U.S. Trustee's request for civil contempt and sanctions for failure of service under the safe harbor rules; rejecting an argument of the creditor's attorney that the duty of reasonable inquiry was satisfied by the law firm's procedures; that argument ignores the personal nature of an attorney's obligations under **Rule 9011**. The attorney in question did not review the document and had no intention of doing so prior to filing. Instead, he authorized – in advance – an associate under his supervision to sign his name to whatever document that associate produced. While he set out a checklist for the associate to follow, he had no way of ensuring that his associate would comply with that checklist or that the resulting written product would otherwise comply with **Rule 9011**. "A signer may not drop papers into the hopper and insist that the court or opposing counsel undertake bothersome factual and legal investigation … at a minimum, the reasonable inquiry standard requires at least some affirmative investigation on the part of the signer."

***Rule 11 Against Debtor's Attorneys in Objecting**: In re McFarland*, 462 B.R. 857 (Bankr. S.D. Fla. 2011) (Olson, J.) (order to show cause entered why sanctions should not be imposed on attorneys who filed objections to proofs of claim based on lack of supporting documentation, when debtors had scheduled claims, as undisputed, in amounts that equaled or exceeded amounts set forth in the proofs of claim. Debtor's counsel violate ethical rules by objecting to a claim for lack of documentation when the debt is scheduled in substantially the same or greater amount, by disputing liability or amount with no substantial basis, or seeking to strike a claim in its entirety when any portion of the debt is undisputedly due and owing; imposing sanctions, including suspensions from practice).

***But Can I Still Object If I Schedule As Disputed?** In re Armstrong*, 487 B.R. 764 (E.D. Tex. 2012) (Clark, D.J., affirming Rhoades, B.J.) Debtor's counsel violated **Rule 9011** when he filed purely procedural objections, based on lack of supporting documentation, to each and every claim filed by credit card issuer; affirming bankruptcy court's imposition

of $500 monetary sanction, finding that the debtor's attorney "participated in, or facilitated a scheme to improperly manipulate the bankruptcy process." Attorney filed Chapter 13 for affluent debtor, representing that all creditors would be paid; plan confirmed on that basis; debtor's counsel contended he was simply fulfilling his duties to this client. "That tired excuse for abuse of opposing parties and the advancement of baseless claims has been thoroughly discredited." 487 B.R. at 773. Such conduct violated **Rule 3.01** (meritorious claims) and **3.02** (minimizing the burdens and delays of litigation). "It is not uncommon to see dozens of attorneys in a bankruptcy courtroom, presenting arguments and objections on a long list of cases, with rulings issued at a pace that makes a cattle auction appear leisurely. A bankruptcy court does not have the time district courts devote to a motion, to examine each petition, proof of claim and objection; the bankruptcy judge must rely on counsel to act in good faith. The potential for mischief to be caused by an attorney who is willing to skirt ethical obligations and procedural rules is enormous. There is no question that strong deterrence must be a consideration when a bankruptcy judge considers sanctions."

See also In re Velez, 465 B.R. 912 (Bankr. S.D. Fla. 2012) (Olson, J.) (debtor's attorney violated **Rule 9011** by objecting to claims that debtors had scheduled for a substantially similar amount; attorney suspended from practice for 31 days. "The gig is up … on debtors taking advantage of the cost of responding to claims objections and obtaining orders striking claims which the debtor has acknowledged owing in whole or substantial part…" (cite omitted). Also, scheduling claims as disputed doesn't shift the burden back to the creditor).

But, Fact That Claim Ultimately Denied Does Not Mean Claim Was Frivolous: *In re Torres*, 2013 WL 1248640 (C.D. Cal. Mar. 27, 2013) (creditor filed claim against the chapter 11 debtor; the bankruptcy court lifted the stay to allow the claim and debtor's counterclaim to be liquidated in state court; the debtor prevailed, so creditor's claim was denied, and debtor requested sanctions against the creditor under the bankruptcy court's inherent power to sanction; the bankruptcy court refused to grant any sanction, and the debtor appealed. On appeal, the district court held that the bankruptcy court did not abuse its discretion in refusing to grant sanctions in favor of debtor and against a creditor whose claim was ultimately denied; simply because a claim is ultimately deemed meritless or without evidentiary support does not necessarily indicate that such a claim was brought in bad faith; a finding of bad faith is necessary to impose sanctions under the court's inherent power to sanction).

How does all this effect fee-shifting?

Even Though Claim Not Compliant, Not Scheduled, and Debtors' Requested Information and Creditor Refused to Respond, & Debtors Weren't Requesting Disallowance, Debtor's Attorney Fees Disallowed. *In re Dunlap*, 2013 WL 5497047

(Bankr. D. Colo. Oct. 3, 2013) (Tallman, C.J.). Chapter 13 debtors objected to a collector's claim of $508.95 for insufficient compliance with **Rule 3001(c)(3)**; debtors had not scheduled the creditor, and the objection was properly served and creditor did not respond. Court found that the claim did not comply with Rule 3001(c)(3). However, above-median debtors were in a five-year confirmed plan paying a $69.96 dividend, or less than $1/10^{th}$ of one percent to the more than $80,000.00 of unsecured claims.

"The instant claim Objection is but one of seven objections that the Debtors have filed in this case. The Court searches in vain for a glimmer of economic rationality underpinning the Debtors' objections. The total value of claims that the Debtors have objected to is less than $3,000.00. Successful resolution of all objections in the Debtors' favor would result in less than $3.00 to be divided up among the remaining claimants. The disallowance of Claim # 12, the subject of this particular Objection, would increase the dividend to be divided among the remaining unsecured creditors by less than $ .50. This Objection is all the more remarkable for the Debtors' failure to advance any substantive objection to the Creditor's claim. Debtors wholly ignore the applicable Bankruptcy Code section, **11 U.S.C. § 502(b),** as authority to disallow the claim. Instead, the Debtors rely exclusively on a procedural rule, **[Rule] 3001** as authority for disallowance. The Court has previously held that revisions to **Rule 3001**, effective December 1, 2011, have limited a bankruptcy court's latitude in granting relief based on a creditor's failure to comply with the documentation requirements in **Rule 3001(c)** and that **Rule 3001(c)(2)(D)** does not permit the Court to disallow a proof of claim based solely on a creditor's failure to comply with **Rule 3001(c)**. (cite omitted). Given that the Debtors' Objection fails to raise any substantive objection to the allowance of the Creditor's claim, the Objection must be denied."

With respect to the debtors' request to prohibit the creditor from presenting the omitted information as evidence in the future and request for attorney fees under **Rule 3001(c)(2)(D)(ii),** the court agrees that the attorney fees were "caused" by the creditor's failure to document the claim; however, the reasonableness element was lacking. "The Court's review of the Debtors' plan and the claims filed in this case reveals a total benefit to the remaining creditors in the estate, resulting from disallowance of Claim # 12, to be less than $ .50. Where the greatest potential benefit of the attorney's labors is less than $ .50, the Court finds that any attorney fees incurred in such an enterprise are unreasonable as a matter of law."

But See; What is Good for the Goose Is Good for the Gander; Creditor's Attorney Fees Denied. *In re Wirth*, 503 B.R. 800, 803-04 (Bankr. W.D. Wis. 2013) (Martin, J.). Creditor could not claim attorney fees incurred in defending the Chapter 13 debtor's objection to its proof of claim, where the attorney fees were caused by the creditor's own lack of diligence in not sufficiently itemizing its attorney fees in the proof of claim to begin with. "The court has the responsibility for avoiding waste of estate assets and preventing overreaching by attorneys in their attempts to be paid attorney's fees from the estate." (cite omitted).

Rule 3002.1 Fee Shifting: *In re Harris*, 492 B.R. 225 (Bankr. S.D. Tex. 2013) (Isgur, J.)

Rule 3002.1 Fee Shifting*: In re Lopez*, 2012 WL 6760175 (Bankr. S.D. Tex. Dec. 31, 2012) (Paul, J.) (no sanctions awarded under **Rule 3002.1** when the secured creditor's claim predated the effective date of the Rule, and complied with the Official Form in effect at the time the claim was filed).

But what to do we do with abusive practices?

When the Creditor Files a Claim That Was Discharged in a Previous Case. *In re Guenot,* 2014 WL 67320 (Bankr. D.N.J. Jan. 2, 2014) (Ferguson, J.) Creditor filed a claim in a Chapter 13 case based on debt that had been discharged in the debtor's previous Chapter 7. The proof of claim was later withdrawn, and the creditor received no payment under the plan. Debtor's attorney filed an adversary complaint against the creditor and its attorneys, alleging that filing the proof of claim violated the discharge injunction of **§ 524,** the **FDCPA**, and various state consumer protection laws. The bankruptcy court found subject matter jurisdiction based on "related to" jurisdiction, given that, in the Chapter 13, any recovery would inure to the benefit of creditors and thus had an impact on the administration of the estate. However, state and federal consumer protection laws are pre-empted by the bankruptcy code in the claims objection context where the laws conflict; the requirement that a debtor have actual damages under the Bankruptcy Code and Rules conflicts with consumer laws that only require ascertainable damages. Here, the damages are self-created, since the only damages are attorney fees for prosecuting the adversary. The debtor failed to produce any evidence to support the allegation that she was upset, such as a certification from a medical professional. "Being 'upset' does not warrant compensation under **§ 362(k).** The Debtor's emotional distress, to the extent it existed, also suffers from the same self-created problem as the attorney's fees. Unlike a demand letter or a phone call directly to a debtor from a creditor or collection agency, a debtor has no reason to be aware of the filing of a proof of claim. If Ms. Guenot was aware that [the creditor] had filed a proof of claim it could only be because her attorney told her about it in order to file this complaint. Had her attorney chosen to call [the creditor's] counsel and ask them to withdraw the claim, then perhaps the Debtor's emotional distress could have been avoided." Summary judgment granted in favor of the creditor.

Additional Punishment to Offending Creditor Not Necessary*: *In re Gilliland, 474 B.R. 482 (Bankr. N.D. Miss. 2012) (Houston, J.) Chapter 13 debtor filed adversary complaint against creditor Capital One and its collection agency which filed a claim that had been discharged in his prior Chapter 7, seeking damages for violating the discharge injunction, filing a false proof of claim, violation of **Rule 3001**, and violation of the **FDCPA**, and requesting that the bankruptcy court certify a class action and seeking injunctive relief. The creditor withdrew the claim, and argued that there were discrepancies in the debtor's name and address from the Chapter 7 that caused it not to recognize that this was a

discharged debt. The court denied class certification, noting that the debtor's circumstances were different from other putative class members, in that the debt related to a business in another town with a different address. The court also noted that Capital One had already agreed to certain claims processing procedures in a Massachusetts adversary case, and that to add additional measures here would be "piling on."

Filing Time Barred Claim Not an FDCPA Violation: *In re Claudio*, 463 B.R. 190 (Bankr. D. Mass. 2012) (Boroff, J.) (filing of a proof of claim on account of a debt that is barred by the statute of limitations in a Chapter 13 case did not constitute a violation of the **FDCPA**; adversary complaint dismissed. Also, sanctions denied for debtor's failure to comply with the safe harbor provisions of **Rule 9011**).

Intentional Filing of Unsecured Claim Which Is In Fact Fully Secured May Violate Rule 11: *In re Burnette*, No. 11-71622, at 2 (Bankr. W.D. Va. Nov. 18, 2011) (in disallowing the claim as an obstacle to the debtor's ability to confirm a bankruptcy plan under which his creditors could be paid in full, the bankruptcy judge noted that "the intentional filing of an unsecured claim by the creditor which in fact has a fully secured claim and is being so treated in the Plan may violate the provisions of [**Rule] 9011(b)(1), (2),** and **(4)** and subject the creditor to possible sanctions"). *See also White v. FIA Card Services*, 494 B.R. 227 (W.D. Va. 2012) (error for bankruptcy court to refuse to void judgment lien of creditor when the creditor filed an unsecured claim in debtor's chapter 13 case).

Commented [DC2]: I looked high and low, but could not locate this case

Practice of Filing Claims as Secured When They are Not: Fees Awarded Under Inherent Power: *In re Campbell*, 2013 WL 2443377 (Bankr. E.D.N.C. June 5, 2013) (Humrickhouse, J.) The City filed a claim for water services against the Chapter 13 debtor as a secured claim. In fact, since debtor was a renter, the claim was unsecured. The debtor's lawyer emailed the City's counsel, noting that he had previously filed many objections to what he described as frivolous city claims for small amounts, and stating he would seek **Rule 11** sanctions if the claim was not amended. The City did not amend the claim, and debtor's counsel filed an objection to the claim and a motion for sanctions under **Rule 9011**. The court denied sanctions under **Rule 11** for the procedural defect of not giving the City 21 days' notice of the unfiled motion; formal adherence to **Rule 11** procedures is required and an informal email did not suffice. The Advisory Committee notes state that "[i]n most cases, counsel should be expected to give informal notice to the other party, whether in person or by a telephone call or letter, of a potential violation before proceeding to prepare and serve a **Rule 11** motion." Thus, while Counsel's email was exactly the right first step, it does not satisfy the official notice requirements of **Rule 9011**." However, the Court would impose attorney fees under **§ 105(a**); the court was persuaded that the City's erroneous classification of claims was not the result of isolated or clerical error; and, rather, impeded the fair and efficient functioning of the court. The court awarded a total of

$3,449.10 in fees and expenses to debtor's counsel for bringing the issue to the court's attention.

Moye v. Cage, 2011 WL 3444221 (S.D. Tex. Aug. 8, 2011) (not designated for publication) (dismissing appeal by creditor who had filed secured claim based on unperfected security interest and whom bankruptcy court had sanctioned in the amount of $23,255 in favor of the Chapter 7 trustee who had had to object to the claim; appeal was interlocutory)

Other Claims/Claims Filing/Claims Objection Issues

Discharge by Claim Objection? *In re Hann*, 711 F.3d 235 (1st Cir. 2013)

Objection When Creditor Files Claim After Issuing a 1099-C filed: *In re Reed*, 492 B.R. 261 (Bankr. E.D. Tenn. 2013) (Stair, J.) (minority view)

Chapter 7 Trustee Shouldn't File Claims On Creditors' Behalf: *In re Vancleef*, 479 B.R. 809 (Bankr. N.D. Ind. 2012) (Klingeberger, J.). In a 2007 chapter 7 case, later reopened to administer a personal injury claim, the court found it was not appropriate for the Chapter 7 Trustee to file claims on behalf of the Schedule F creditors who did not file claims in response to the bar date; noting the two approaches by court in interpreting **§ 501(c)** – the "hose the debtor" approach and the "put out the fire" approach; the court concluded that the purpose of **§ 501(c)** was to protect the debtor or to facilitate reorganizations; the Chapter 7 Trustee could not comply with the requirements of **Rule 3001** and would have had a duty to object to her own claims, since the Chapter 7 trustee also has a duty to a debtor to impartially and fairly administer his case and for the benefit of those who actively participate in it. Noting, without so holding, that a Chapter 13 trustee might have a duty to file a claim on a mortgage creditor's behalf under **§ 1302(b)(4)** so that a debtor's case "can be effectively implemented." Posit a situation in which a Chapter 7 trustee had knowledge that a creditor had a valid cause of action for an exception to discharge; could that trustee, commensurate with her duties to creditors and to the debtor under **§ 704** actively engage with the creditor to make certain that the complaint was timely filed? This court says no – that would be improper and a derogation of the trustee's duties.

Can we solve the mortgage crisis through the claims objection process?

Wells Fargo Bank v. Oparaji (In the Matter of Oparaji), 698 F.3d 231 (5th Cir. 2012) (mortgage creditor not judicially estopped from claiming, in debtor's second chapter 13 filing, postpetition mortgage arrears and costs not claimed in debtor's previous chapter 13 filing. The debtor has the ability and responsibility to keep track of his outstanding debt; there is no statute or judicial precedent imposing a legal responsibility on the secured creditor to seek the full amount to which it is entitled in each amended secured claim; reversing bankruptcy court decision affirmed by the district court imposing sanctions).

In re Ramos, 493 B.R. 355 (Bankr. D.P.R. 2013) (Flores, J.) (creditor did not hold a valid secured claim against chapter 13 debtors' real estate under Puerto Rico law because the mortgage deed was invalidly recorded after the filing of the petition. The subsequently filed unsecured claim was untimely filed, so was denied. Creditor did not, however, violate the stay for filing an alleged secured claim and sanctions are not warranted for filing an allegedly false claim, given the uncertainty in the new Puerto Rico law).

In re Kreitzer, 489 B.R. 698 (Bankr. S.D. Ohio 2013) (Humphrey, J.) (allegations that holder of the secured claim filed a false claim and should be sanctioned were barred by res judicata and collateral estoppel; state court in the foreclosure action had determined that the creditor held the note and mortgage; subsequent assignment of a properly recorded mortgage did not render it perfected and subject to avoidance).

In re Moehring, 485 B.R. 571 (Bankr. S.D. Ohio 2013) (Humphrey, J.) (chapter 13 debtor's objection to transferred mortgage claim on the grounds it was "false"; that the claim was fraudulently assigned; and that the accrued interest was improperly calculated were overruled. Debtor did not have standing to object to the notice of transfer; only the transferor has standing. Although original claim was filed by a creditor who didn't own the claim, such that the later filing by the transferee of an amended claim did not related back and thus was not timely, the creditor proved it was the holder and that its interest calculations were correct. Since the confirmed plan provided for payment of the creditor, the Chapter 13 Trustee could pay the creditor (recognizing the split of authority).

In re Rinaldi, 2013 WL 655514 (Bankr. E.D. Wis. Feb. 22, 2013) (Kelley, J.) (denying debtors' complaint and objection to claim of mortgage lender; allegations of civil RICO, abuse of process, etc., without merit).

In re Verity, 2012 WL 3561669 (Bankr. D.N.J. Aug. 16, 2012) (Steckroth, J.) (debtors filed a Chapter 13 to stay an ongoing foreclosure action against their home. After the lenders and a servicer filed secured claims, the Chapter 13 debtors filed adversary, objecting to the claims, and seeking sanctions for filing an improper claim, damages under the **FDCPA**, and breach of contract. Debtors asserted that "they did not owe any money to the creditor or have any relationship with the creditor." The court granted summary judgment in favor of the lender; debtors were barred by *Rooker-Feldman* or the court should abstain under *Young v. Harris*; plus, debtors failed to establish any evidence to support at **FDCPA** violation).

In re Akers, 2012 WL 3133924 (Bankr. D.C. Aug. 1, 2012) (Teel, J.) (after Chapter 13 plan was completed, debtor filed an adversary complaint against her mortgage lender, for alleged misrepresentation of escrow and other loan balances, misapplication of payments, improper penalties and filing of a fraudulent proof of claim that misstated her arrears. The court did not have subject matter jurisdiction over the first 3 counts. With respect to the

proof of claim, there is no statute or rule or case law that provides an independent cause of action for damages for an alleged fraudulent proof of claim; although **Rule 9011** applies, debtor had not complied with the safe-harbor provision. To the extent the debtor believes the lender was paid excessive amounts, it is irrelevant, since debtor modified the plan to pay the lender directly).

In re Peed, 2012 WL 1999485 (Bankr. S.D. Ala. June 4, 2012) (Mahoney, J.) (court granted the defendants' motion to dismiss adversary complaint filed by Chapter 13 debtors against their mortgage company and its lawyers; no basis to sue lawyers for tort of wantonness under Alabama law for filing motions or proofs of claim in a bankruptcy case; appropriate remedy is **Rule 9011** sanctions, **§ 105(a),** or contempt. In addition, no violation of the **FDCPA)**.

In re Peterson, 2012 WL 4175008 (Bankr. N.D. Miss. Sept. 19, 2012) (Houston, J.) (chapter 13 debtor's complaint against mobile home financer for alleged misapplication of interest as violation of the stay and seeking actual and punitive damages and injunctive relief denied. The interest that accrued was allowed by contract and was incurred when the plan payments did not begin for several months. Debtors otherwise could not prove that creditor had improperly omitted earned but uncollected prepetition interest in the proof of claim and attempted to recoup it as the payments were applied).

Saturday July 4th

1:30- 2:30 **Ethical Issues Regarding Limited-Scope Representation and Withdrawal from Representation in Bankruptcy Cases.**
Moderator: Martha G. Bronitsky, Chapter 13 Standing Trustee for the Northern District of California (Hayward)
Mark C. Leffler, Boleman Law Firm (Richmond, VA)
Michael J. McCormick, Bankruptcy Senior Partner, McCalla Raymer (Roswell, GA)

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Saturday July 4th

1:30- 2:30 ***Crawford vs LVNV Funding*: How Can It Be Wrong When It Feels So Right?**
Moderator: Laurie Weatherford, Chapter 13 Standing Trustee for the Middle District of Florida (Winter Park)
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The Statute of Limitations: A Definition[1]

A statute of limitations is a legislatively proscribed period of time within which a lawsuit must be brought on a claim. In most cases, the running of the statute of limitations is an affirmative defense to suit that must be raised by a defendant.[2] The limitations period for a specific type of action under state law, *e.g.*, a personal injury claim, may vary from state to state.[3]

It is often unclear which statute of limitations applies to a particular claim. For example, contractual choice of law terms may discord with local conflict of laws, statutes or precedent. There may be a dispute over which cause of action, and its applicable statute of limitations, applies to a claim. (Are revolving credit accounts written contracts, accounts stated, or, in the absence of a signed credit agreement, an unwritten account?) The statute of limitations in many states differs as to actions on similar claims. Additionally, the beginning of the limitations period for an open or revolving consumer account is, generally, the date of the last transaction on the account. However, that date is also subject to interpretation. (Is it the date of the last payment, the date of the creditor's last non-suit collection attempt, or the date of any creditor transaction on the account, such as final delinquency or interest charges?) Finally, determining if the statute of limitations applies also involves facts that are uniquely within the defendant's knowledge, such as where the debtor lived during the life of the account and after delinquency. All of these factors make determining which statute of limitations applies and whether it has run more complicated and the answer can mean the difference between a suit surviving a motion to dismiss or not.

> **As is generally true elsewhere, in Alabama the statute of limitations is an affirmative defense, not an element of the plaintiff's claim.** *E.g., Special Assets, L.L.C. v. Chase Home Finance, L.L.C., 991 So. 2d 668, 675 (Ala. 2007).*

The Effect of the Running of the Statute of Limitations

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[1] Portions of this paper are excerpted with permission from Alane A. Becket & William A. McNeal, *A Claimant's Dilemma: The Statute of Limitations and Proofs of Claim*, Am. Bankr. Inst. J., April 2015.

[2] Fed. R. Civ. P. 8(c)(1).

[3] For example, in Virginia, the statute of limitations for personal injury claims is two years, Va. Code Ann. § 8.01-243A (2014); however, in Tennessee, it is one year, Tenn. Code Ann. § 28-3-104(a)(1) (2014).

It is nearly uniformly held that the running of the statute of limitations does not extinguish the debt, but rather, only the remedy if raised properly and proven.[4] "The expiration of a statute of limitation does not extinguish the substantive right itself, just the right to enforce a remedy. . . . A statute of repose or duration, on the other hand, provides a date upon which the substantive right itself no longer exists."[5]

The Statute of Limitations and the FDCPA

Enacted in 1978, the FDCPA arose as a result of "abundant evidence of the use of abusive, deceptive, and unfair debt collection practices by many debt collectors."[6]

The FDCPA proscribes specific acts, for example, communicating with third parties about a debt or contacting debtors early in the morning or late at night. It also more generally prohibits debt collectors from engaging in harassing or abusive behavior, employing unfair practices in the collection of debts, and making false representations to collect debts. However, nothing in the FDCPA prohibits the lawful collection of debts for which the statute of limitations for a suit has run.[7]

Likewise, filing suit on an out of statute debt is not a violation of the precise terms of the FDCPA. However, "Federal circuit and district courts have uniformly held that a debt collector's threatening to sue on a time-barred debt and/or filing a time-barred suit in state court to recover that debt violates §§ 1692e and 1692f."[8] Section 1692e of Title 15 prohibits the false representation of -- the character, amount, or legal status of any debt.[9] Section 1692f prohibits using unfair or unconscionable means to collect or attempt to collect any debt.[10] Filing suit when

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[4] *Gatewood v. CP Med. LLC*, Adv. No. 5:14-ap-7068, No. 5:13-bk-73363, at 2-3 n.2 (Bankr. W.D. Ark. Feb. 6, 2015) (order granting summary judgment to defendant and dismissing complaint) (citation omitted); *but see* Miss. Code Ann. § 15-1-3(1) (2014) ("The completion of the period of limitation prescribed to bar any action, shall defeat and extinguish the right as well as the remedy."); *Heritage Mut. Ins. Co. v. Picha*, 397 N.W.2d 156 (Wis. Ct. App. 1986) ("Wisconsin may be unique in holding that the running of a statute of limitations not only extinguishes the remedy to enforce a right but also destroys the right itself.").

[5] *Gatewood v. CP Med. LLC*, Adv. No. 5:14-ap-7068, No. 5:13-bk-73363, at 2-3 n.2.

[6] 15 U.S.C. § 1692(a) (2014).

[7] *Johns v. Northland Group, Inc.*, No. 14-2947, 2015 U.S. Dist. LEXIS 93, at *10 (E.D. Pa. Jan. 5, 2015) (holding that, "[p]ursuant to the FDCPA, a debt collector may seek voluntary repayment of the time-barred debt, so long as the debt collector does not initiate or threaten legal action in connection with the collection efforts").

[8] *Crawford v. LVNV Funding, LLC*, 758 F.3d 1254, 1259 (11th Cir. 2014).

[9] 15 U.S.C. § 1692e (2014).

[10] 15 U.S.C. § 1692f (2014).

the plaintiff knows the statute of limitations provides the defendant with a complete defense has been held to violate both provisions.

The Statute of Limitations and Bankruptcy Claims

A "claim" in bankruptcy is not the same as a claim eligible for suit. The Bankruptcy Code defines "claim" broadly as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured . . . ".[11] The definition is intentionally expansive so that any party who may make a claim against the debtor is notified of the bankruptcy,[12] after which any disputes over the claim can be adjudicated.

Indeed the fact that a claim may be subject to disallowance due to the running of an applicable statute of limitations, "does not defeat the *existence* of the claim in bankruptcy." *Roach vs. Edge* (*In re Edge*), 60 B.R. 690, 699 (Bankr. M.D. Tenn. 1986). "Quite the contrary: the existence of the claim must be determined independent of limitations questions else the process of *allowance* under § 502 becomes redundant if not circular." *Id.* By ruling that a proof of claim for an out of statute debt is a violation of the FDCPA, the Eleventh Circuit in *Crawford v. LVNV Funding LLC*[13], has effectively prohibited certain claimants from filing legitimate bankruptcy claims, eschewing the claim determination process for adjudicating the allowance of claims.

> **In Alabama, a creditor's right to payment is not eliminated by a limitations bar. …("[A] statute of limitations generally is procedural and extinguishes the remedy rather than the right ….") …Thus, the defendant has a right to payment of its time-barred debt and a consequent entitlement to file a proof of claim as to the time-barred debt.**
> *Johnson v. Midland Funding, 2015 U.S. Dist. LEXIS 36581* (Bankr. S.D. Ala. 2015)

> **While the FDCPA and the Bankruptcy Code can be read together, the FDCPA and the Code, while overlapping, serve different purposes and the FDCPA is not controlling after debtor files a voluntary petition.**
> *Gatewood v. CP Med. LLC*, (Bankr. W.D. Ark. Feb. 6, 2015)

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[11] 11 U.S.C. § 101(5).
[12] *Johnson v. Home State Bank*, 501 U.S. 78, 83 (1991) ("We have previously explained that Congress intended by this language to adopt the broadest available definition of 'claim.'").
[13] 758 F.3d 1254 (11th Cir. 2014).

While the filing of a proof of claim in a bankruptcy is subject to both the Bankruptcy Code and the FDCPA, and is an action to collect a debt, within the ambit of the FDCPA, it is, when compliant with the rules of bankruptcy, not deceptive, false, or misleading.
Robinson v. eCAST Settlement Corp.,(N.D. Ill. Feb. 3, 2015)

Denying a motion to dismiss and holding that filing a proof of claim in a bankruptcy for an out of statute debt is an attempt to collect a debt in violation of the FDCPA because it creates the misleading impression in the least sophisticated consumer that the debt is legally enforceable.
Patrick v. PYOD, LLC, (S.D. Ind. Aug. 20, 2014)

Dismissing suit finding that filing a proof of claim in a bankruptcy for an out of statute debt is not an improper collection activity proscribed by the FDCPA and makes no false representations, threats of illegal action, and is not a deceptive means of collection, or an unfair or unconscionable collection method.
LaGrone v. LVNV Funding LLC (Bankr. N.D. Ill. Jan. 21, 2015)

Bankruptcy's allowance of the filing of a proof of claim for an out of statute debt is not a requirement, thus, posing no conflict with the FDCPA; and that a creditor may comply with both the Bankruptcy Code and the FDCPA, by not filing a claim on an out of statute debt
Brimmage v. Quantum3 Group LLC (Bankr. N.D. Ill. Jan. 9, 2015)

Crawford vs LVNV Funding: How Can It Be Wrong When It Feels So Right?

Moderator: Laurie Weatherford, Chapter 13 Standing Trustee for the Middle District of Florida

Honorable Michael B. Kaplan
United States Bankruptcy Judge for the District of New Jersey

Alane Becket, Becket & Lee LLP

NACTT Annual Seminar
Salt Lake City, UT
July 4, 2015

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Agenda

- The nature of the Statute of Limitations
- The FDCPA and the Statute of Limitations
- Filing suit on out of statute debts
- *In re Crawford*
- *Post-Crawford*

Statute of Limitations: A Defense

- When a lawsuit is filed, SOL may be a defense
- It is typically the defendant's burden to assert and prove the SOL has run
- SOL as a defense is waived if not raised and judgment may be entered against the defendant
- *State law* is not generally violated when suit is filed on an out of statute debt
- The applicable SOL is not clearly defined

Statute of Limitations: A Defense

As is generally true elsewhere, in Alabama the statute of limitations is an affirmative defense, not an element of the plaintiff's claim. *E.g., Special Assets, L.L.C. v. Chase Home Finance, L.L.C., 991 So. 2d 668, 675 (Ala. 2007).*

Which State's SOL Applies?

- Contract choice of law
- Debtor's residence
- State of Creditor's primary place of business
- Borrowing statutes

When Does the SOL Begin to Run?

- Date of last payment
- Date when payment is due
- Date of last transaction – what is the last t/a
- Charge-off date
- Date of creditor's last collection attempt
- Date the debtor last acknowledged the debt

Effect of the SOL – A Legal Determination

The application of a statute of limitations is a legal determination, which we review for correctness. However, "[t]o the extent that the statute of limitations analysis involves 'subsidiary factual determination[s],' we review those factual determinations using 'a clearly erroneous standard.'" *Ottens v. McNeil*, 239 P.3d 308 (internal citations omitted).

See, also, Fla. Bar v. Spann, 682 So. 2d 1070, 1073 (Fla. 1996) (finding the unauthorized practice of law by nonlawyer employees who wrote letters to a client that contained legal advice, *viz.*, statute of limitations applicable to a client's claims, that only a lawyer can give).

Statutory Policy

- **The Bankruptcy Code:** To provide an honest but unfortunate debtor the opportunity to obtain a fresh start and to ensure debtors repay their creditors the maximum they can afford.
- **The FDCPA:** To stop the use of abusive, deceptive, and unfair debt collection practices by many debt collectors.

The FDCPA

§ 803. Definitions [15 USC 1692a]

(5) The term "debt" means any obligation or alleged obligation of a consumer to pay money arising out of a transaction in which the money, property, insurance or services which are the subject of the transaction **are primarily for personal, family, or household purposes**, whether or not such obligation has been reduced to judgment.

(6) The term "debt collector" means any person … who regularly collects or attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another. …**The term does not include** -

(A) **any officer or employee of a creditor** while, in the name of the creditor, collecting debts for such creditor; …

The FDCPA

§ 807. False or misleading representations [15 USC 1692e]

A debt collector may not use any false, deceptive, or misleading representation or means in connection with the collection of any debt. [T]he following conduct is a violation of this section:

(2) The false representation of -

(A) **the character, amount, or legal status of any debt;** …

Filing Suit on OOS Debts and the FDCPA

- Filing suit on an out of statute debt is not specifically prohibited under the precise terms of the FDCPA
- The FDCPA prohibits:
  - The false representation of -- the character, amount, or legal status of any debt. [15 USC 1692e]
  - A debt collector may not use unfair or unconscionable means to collect or attempt to collect any debt. [15 USC 1692f]
- Filing suit on an out of statute debt has been held to violate both provisions

Filing Suit on OOS Debts and the FDCPA

Phillips v. Asset Acceptance, LLC, 736 F.3d 1076, 1083 (7th Cir. 2013) (finding an FDCPA violation for suing on a debt on which applicable statute of limitations had run):

- Because few unsophisticated consumers would be aware that a statute of limitations could be used to defend against lawsuits based on stale debts, such consumers would unwittingly acquiesce to such lawsuits.

Grant-Hall v. Cavalry Portfolio Servs., LLC, 856 F. Supp. 2d 929, 944 (N.D. Ill. 2012)

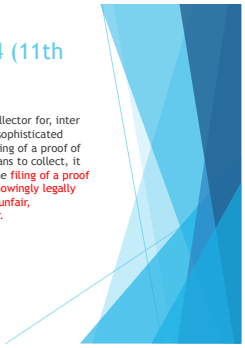
- The filing of a legally defective debt collection suit can violate § 1692e where the filing falsely implies that the debt collector has legal recourse to collect the debt.

Kimber v. Fed. Fin. Corp., 668 F. Supp. 1480, 1487 (M.D. Ala. 1987)

- The court agrees with Kimber that a debt collector's filing of a lawsuit on a debt that appears to be time-barred, without the debt collector [sic] having first determined after a reasonable inquiry that that limitations period has been or should be tolled, is an unfair and unconscionable means of collecting the debt.

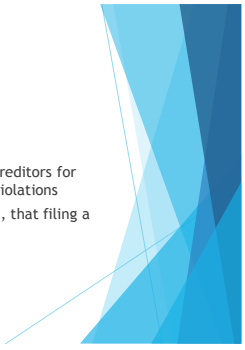
Crawford v. LVNV, 758 F.3d 1254 (11th Cir. 2014)

- The FDCPA affords a private right of action against a debt collector for, inter alia, unfair and deceptive practices, as tested by the least sophisticated consumer standard. Because, according to the court, the filing of a proof of claim is a debt collection activity, or at least an indirect means to collect, it falls within the ambit of the FDCPA. The court found that the filing of a proof of claim against an estate in bankruptcy for a debt that is knowingly legally unenforceable pursuant to apposite statute of limitations is unfair, unconscionable, deceiving, or misleading to such a consumer.
  - rehearing denied
  - stay of the mandate denied
  - petition for certiorari denied



Background

- Debtors filed Chapter 13
- Creditors filed POCs for out of statute debts
- Debtors filed adversary proceedings against creditors for filing stale claims arguing, inter alia, FDCPA violations
- Creditors moved to dismiss arguing, inter alia, that filing a POC is not an FDCPA violation



Background

- Debtors' AP dismissed by Bankruptcy Court
- Debtors appealed
- District Court affirmed dismissal of Debtors' AP
- Debtors appealed
- 11th Circuit vacated the District Court's dismissal of the Debtor's AP and remanded FDCPA case
  - (But, determined the FDCPA was violated)

Debtors' Principal Arguments

- Acknowledges that debtor's successful outcome would change the result of virtually every other judicial opinion on the subject
- Argues that despite the uniform nature of the bankruptcy laws, a "debt collector's" rights in bankruptcy are limited by the FDCPA:

  "… Sims (sic) position on the law will have no effect on Creditors because they will never be subject to the FDCPA. … The FDCPA is the yoke which debt collectors bear for the privilege of being debt collectors. There is no reason to provide debt collectors with a playground full of vulnerable consumers in the Bankruptcy forum for debt collectors to bully with impunity from FDCPA liability."

Creditors' Principal Arguments

- The FDCPA is not "pre-empted" by the Bankruptcy Code, but:
  - Overwhelming weight of authority: POCs are not subject to the FDCPA
  - A POC for an out of statute debt is not false or fraudulent
  - A POC is not "tantamount" to a civil action/complaint
  - The FDCPA historically applied to acts taken outside of the bankruptcy to collect a debt involved in a bankruptcy

The *Crawford* District Court

Setting the weight of authority aside, Appellants have not alleged any conduct that amounts to an FDCPA violation. Appellants were never threatened, never tricked, never lied to or deceived; they were never even spoken to. Appellees never asked Appellants for a dime; instead, they merely filed claims in the bankruptcy court. As a matter of law, that conduct does not amount to an effort to collect a debt. Even if it did, it is not the sort of abusive practice the FDCPA was enacted to prohibit.

The *Crawford* 11th Circuit Opinion

A deluge has swept through U.S. bankruptcy courts of late. Consumer debt buyers--armed with hundreds of delinquent accounts purchased from creditors--are filing proofs of claim on debts deemed unenforceable under state statutes of limitations. This appeal considers whether a proof of claim to collect a stale debt in Chapter 13 bankruptcy violates the Fair Debt Collection Practices Act…

The *Crawford* 11th Circuit Opinion

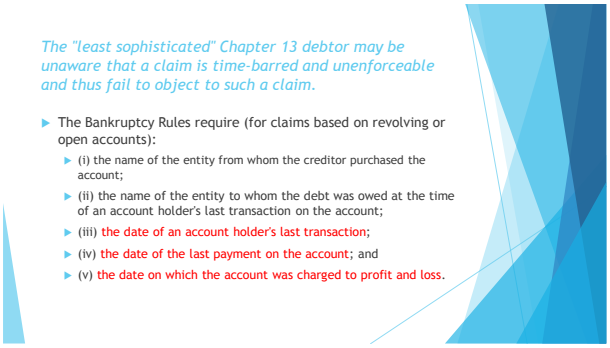
- A Chapter 13 debtor's memory of a stale debt may have faded and personal records documenting the debt may have vanished, making it difficult for a consumer debtor to defend against the time-barred claim.
- Similar to the filing of a stale lawsuit, a debt collector's filing of a time-barred proof of claim creates the misleading impression to the debtor that the debt collector can legally enforce the debt.
- The "least sophisticated" Chapter 13 debtor may be unaware that a claim is time-barred and unenforceable, and thus fail to object to such a claim.

The "least sophisticated" Chapter 13 debtor may be unaware that a claim is time-barred and unenforceable and thus fail to object to such a claim.

- The Proof of Claim Form requires (all claims):
  - Documentation supporting the claim
  - Statement of the basis for the claim
  - Last 4 digits of account number
  - Name by which the debtor may know the creditor
  - Itemization of interest charges

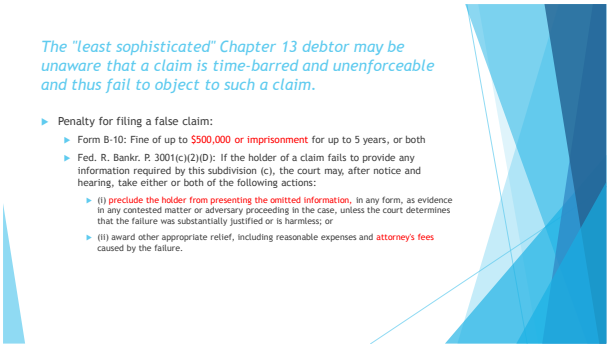
The "least sophisticated" Chapter 13 debtor may be unaware that a claim is time-barred and unenforceable and thus fail to object to such a claim.

- The Bankruptcy Rules require (for claims based on revolving or open accounts):
  - (i) the name of the entity from whom the creditor purchased the account;
  - (ii) the name of the entity to whom the debt was owed at the time of an account holder's last transaction on the account;
  - (iii) the date of an account holder's last transaction;
  - (iv) the date of the last payment on the account; and
  - (v) the date on which the account was charged to profit and loss.



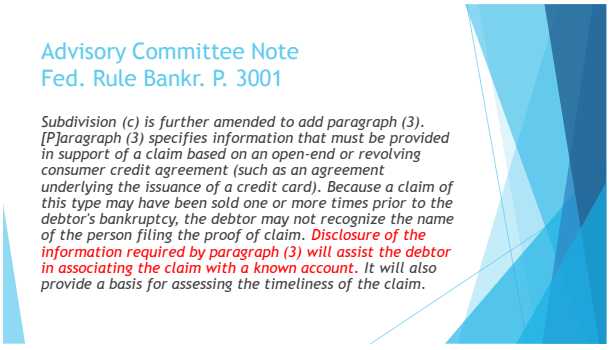
The "least sophisticated" Chapter 13 debtor may be unaware that a claim is time-barred and unenforceable and thus fail to object to such a claim.

- Penalty for filing a false claim:
  - Form B-10: Fine of up to $500,000 or imprisonment for up to 5 years, or both
  - Fed. R. Bankr. P. 3001(c)(2)(D): If the holder of a claim fails to provide any information required by this subdivision (c), the court may, after notice and hearing, take either or both of the following actions:
    - (i) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or
    - (ii) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure.



Advisory Committee Note Fed. Rule Bankr. P. 3001

Subdivision (c) is further amended to add paragraph (3). [P]aragraph (3) specifies information that must be provided in support of a claim based on an open-end or revolving consumer credit agreement (such as an agreement underlying the issuance of a credit card). Because a claim of this type may have been sold one or more times prior to the debtor's bankruptcy, the debtor may not recognize the name of the person filing the proof of claim. Disclosure of the information required by paragraph (3) will assist the debtor in associating the claim with a known account. It will also provide a basis for assessing the timeliness of the claim.



11 U.S.C. 502: Is an OOS Claim "Unenforceable"?

Johnson v. Midland Funding: (S. D. Ala. 2015)

…when the Bankruptcy Code uses the word 'claim' – which the Code itself defines as a 'right to payment … it is usually referring to a right to payment recognized under state law. … Thus, if a creditor has a right to payment … recognized by applicable state law despite the lapse of the limitations period, he has a claim for such time-barred debt and is entitled to file a proof of claim as to such time-barred debt.

11 U.S.C. 502: Is an OOS Claim "Unenforceable"?

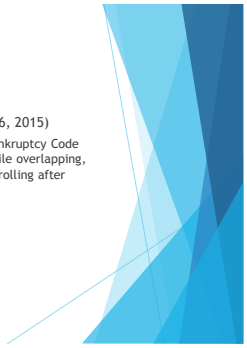
In Alabama, a creditor's right to payment is not eliminated by a limitations bar. …("[A] statute of limitations generally is procedural and extinguishes the remedy rather than the right ….") …Thus, the defendant has a right to payment of its time-barred debt and a consequent entitlement to file a proof of claim as to the time-barred debt.

11 U.S.C. 502: Is an OOS Claim "Unenforceable"?

Because the statute of limitations is an affirmative defense that is lost if not properly asserted, there is a sense in which a time-barred claim is legally enforceable when the proof of claim is filed, subject to becoming unenforceable only later, if and when the defense is raised. Under this view, filing a proof of claim on a time-barred claim would be proper under the Code even accepting the plaintiff's position that the claim must be enforceable when the proof of claim is filed.

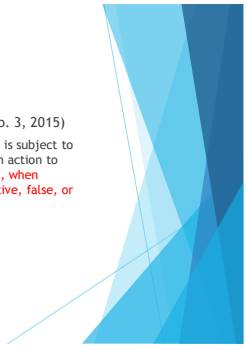
After *Crawford*:

- *Gatewood v. CP Med. LLC*,(Bankr. W.D. Ark. Feb. 6, 2015)
  - Dismissing complaint: while the FDCPA and the Bankruptcy Code can be read together, the FDCPA and the Code, while overlapping, serve different purposes and the FDCPA is not controlling after debtor files a voluntary petition.



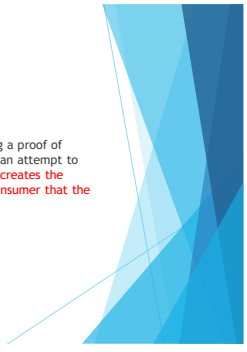
After *Crawford*:

- *Robinson v. eCAST Settlement Corp.*,(N.D. Ill. Feb. 3, 2015)
  - While the filing of a proof of claim in a bankruptcy is subject to both the Bankruptcy Code and the FDCPA, and is an action to collect a debt, within the ambit of the FDCPA, it is, when compliant with the rules of bankruptcy, not deceptive, false, or misleading



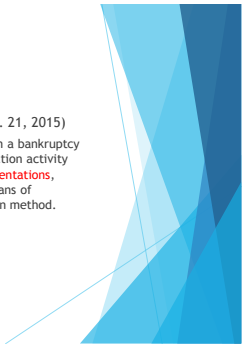
After *Crawford*:

- *Patrick v. PYOD, LLC*, (S.D. Ind. Aug. 20, 2014)
  - Denying a motion to dismiss and holding that filing a proof of claim in a bankruptcy for an out of statute debt is an attempt to collect a debt in violation of the FDCPA because it creates the misleading impression in the least sophisticated consumer that the debt is legally enforceable.



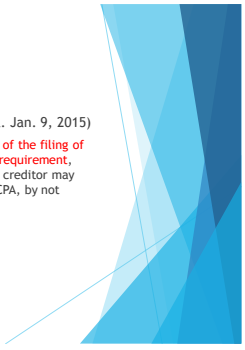
After *Crawford*:

- *LaGrone v. LVNV Funding LLC* (Bankr. N.D. Ill. Jan. 21, 2015)
  - Dismissing suit finding that filing a proof of claim in a bankruptcy for an out of statute debt is not an improper collection activity proscribed by the FDCPA and makes no false representations, threats of illegal action, and is not a deceptive means of collection, or an unfair or unconscionable collection method.



After *Crawford*:

- *Brimmage v. Quantum3 Group LLC* (Bankr. N.D. Ill. Jan. 9, 2015)
  - Denying motion to dismiss: bankruptcy's allowance of the filing of a proof of claim for an out of statute debt is not a requirement, thus, posing no conflict with the FDCPA; and that a creditor may comply with both the Bankruptcy Code and the FDCPA, by not filing a claim on an out of statute debt

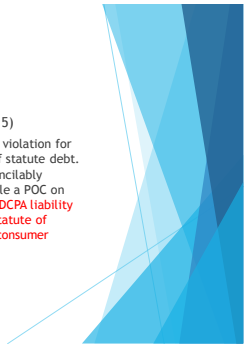


After *Crawford*:

- *Donaldson v. LVNV Funding, LLC* (S.D. Ind. Apr. 7, 2015)
  - Motion to dismiss granted: A bankruptcy debtor is not an unsophisticated consumer, such as a plaintiff in an FDCPA action, but is represented by an attorney, and his estate is protected by a trustee, calling for the "competent lawyer" standard to apply to the POC

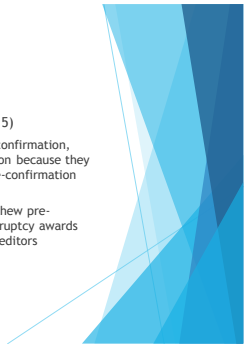
After *Crawford*:

- *Reed v. LVNV Funding, LLC*, (N.D. Ill. Mar. 27, 2015)
  - Denying a motion to dismiss a complaint for FDCPA violation for filing a proof of claim in a bankruptcy for an out of statute debt. The FDCPA and the Bankruptcy Code are not irreconcilably conflicting because a claimant is not required to file a POC on time-barred debt, and the filer is not immune to FDCPA liability merely because the debt remains valid despite a statute of limitations defense, applying the unsophisticated consumer standard



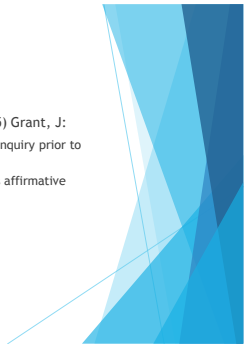
After *Crawford*:

- *Covert v. LVNV Funding, LLC*, (4th Cir. Mar. 3, 2015)
  - Debtors/Plaintiffs were barred from raising, post-confirmation, claims that they should have raised pre-confirmation because they knew or should have known of them during the pre-confirmation bankruptcy proceedings
  - To hold otherwise would incentivize Debtors to eschew pre-confirmation damages claims in favor of post-bankruptcy awards that they would not be required to distribute to creditors



Sanctions for filing OOS POC?

- *In re Sekema*, 523 B.R. 651 (Bankr. N.D. Ind. 2015) Grant, J:
  - Claimants did not conduct a reasonable pre-filing inquiry prior to filing proofs of claims for out of statute debts.
  - Reasonable inquiry extends to determining obvious affirmative defenses



Saturday July 4th

3:00 - 4:00 Post-Confirmation Plan Modification: The Applicable Commitment Period and the Disposable Income Test Do Apply . . . Don't They?
Moderator: Tammy Terry, Chapter 13 Standing Trustee for the Eastern District of Michigan (Detroit)
Johnie J. Patterson, II, Walker & Patterson, PC (Houston, TX)
Alice Whitten, Vice President – Senior Counsel, Wells Fargo (Minneapolis, MN)

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POST-CONFIRMATION MODIFICATION

1) MUST A POST-CONFIRMATION MODIFICATION ADHERE TO THE APPLICABLE COMMITMENT PERIOD OF §1325(B)?

a) **No** - By the plain language of §1329, the provisions of §1325(b) are not applicable to post-confirmation modifications. The language of the statute limits its applicability to the confirmation itself, and confirmation is separate and distinct from modification. *In re Lorenzo*, 2013 Bankr. LEXIS 1944 (Bankr. S.D. Fla. 2013). Thus, the equitable powers of the bankruptcy court cannot be utilized.

i) See, e.g., *In re Powers*, 507 B.R. 262 (Bankr. C.D. Ill. 2014);

(1) Stating that "[d]ebtors are only required to commit all of their projected disposable income to plan payments for distribution to unsecured creditors if the trustee or an unsecured creditor has objected to confirmation of the plan and if the debtor has not otherwise provided to pay all unsecured claims in full." 507 B.R. 262, 268 (Bankr. C.D. Ill. 2014) (citing 11 U.S.C. § 1325(b)(1).

(2) "The plain meaning of § 1325(b) is that it provides an additional condition for confirmation of a plan which has otherwise met the requirements of § 1325(a). . . . Nothing in § 1325(b) suggests that it applies outside of the confirmation process." *Id.* at 269 (citing *In re Davis,* 439 B.R. 863, 867 (N.D. Ill. 2010)).

(3) The plain meaning of § 1329(b)(1) is that the enumerated provisions apply to chapter 13 modifications, and other un-enumerated provisions do not. To read 1329(b)(1) as incorporating provisions which were specifically *not* listed would render the provision extraneous. If all provisions of chapter 13 apply to plan modifications, there would have been no reason for § 1329(b)(1) to have been specifically drafted. *See Davis,* 439 B.R. at 868.

(4) Because 1325(b) is limited to the confirmation process, proposed plan modifications are NOT analyzed under a disposable income test.

ii) *In re Grutsch* , 453 B.R. 420 (Bankr. D. Kan. 2011)

(1) Note: this holding was challenged in *In re Cormier*, 478 B.R. 88 (D. Mass 2012), which simply holds the opposite. (Since these are issues over which courts are split, most of these opinions are opposed by at least one other – but that does not mean that they are not still good law.)

(2) The opinion states: "[T]he fact § 1329(c) specifically references the applicable commitment period weighs heavily against attempts to read the provisions of § 1325(b) into § 1329(b)." Further, "[w]ith the enactment of BAPCPA, Congress clearly recognized that § 1329 should be amended to incorporate the concept of the applicable commitment period. However, Congress chose only to address the applicable commitment period in § 1329(c). The fact that Congress specifically amended one subsection of § 1329 to incorporate the applicable commitment period, but elected not to make similar changes to another subsection of § 1329, strongly implies that the absence of any mention to § 1325(b) or the applicable commitment period in § 1329(b) is not accidental or caused by Congressional oversight." 453 B.R. at 426.

iii) *In Re Davis*, 439 B.R. 863 (N.D. Ill. 2010) (also challenged by *In re Cormier*)

(1) Section 1329(b)(1) expressly lists four subsections of chapter 13 that apply to a modification under § 1329, § 1322(a), § 1322(b), § 1323(c), and the requirements of section 1325(a). By specifying only these four provisions, 1329(b) implicitly excludes other provisions.

(a) By specifically including certain statutory provisions in the requirements under § 1329, the court concludes that any provision not included in the list was *intentionally omitted*.

(b) The majority of decisions addressing this issue follow this line of reasoning.

iv) Some courts allow debtors to shorten their plans to less than the applicable commitment period.

- See, eg, *In re Tibbs*, 478 B.R. 458 (Bankr. S.D. Fla. 2012) (holding that the debtors could modify their confirmed plan to allow for payment of the remaining amount owed under the plan before the termination of the applicable commitment period without paying all allowed unsecured claims in full).
- *In re Barnes*, 506 B.R. 777 (Bankr. E.D. Wis. 2014) (holding that the debtor need not comply with the "projected disposable income" requirement of § 1325(b) at modification, but the debtor must show why he cannot make the reduced payments through the original plan length as part of a showing of "good faith" under § 1325(a)(3)).
- *See also* for similar lines of reasoning:
  - *In re Sunahara*, 326 B.R. 768, 781 (9th Cir. BAP 2005);
  - *In re McCully*, 398 B.R. 590, 593 (Bankr.N.D.Ohio 2008);
  - *In re Young*, 370 B.R. 799, 802 (Bankr.E.D.Wis.2007);
  - *In re Ewers*, 366 B.R. 139, 142–43 (Bankr.D.Nev.2007).
  - *In re McAllister*, 510 B.R. 409 (Bankr. N.D. Ga. 2014);
  - *In re Swain*, 509 B.R. 22 (Bankr. E.D. Va. 2014); and
  - *In re Barnes*, ___ B.R. ___, 2014 WL 1016062 (Bankr. E.D. Wis. 2014).

b) **Yes** – Applicable Commitment Period is a temporal requirement, and while §1329 does not specifically enumerate §1325(b), it does incorporate §1325(a) which provides that a plan shall be confirmed, *except as provided in subsection (b).*

i) Courts in this camp base their holdings on three primary arguments:

(1) That § 1325(a) itself incorporates § 1325(b), thus making the latter provision applicable to modifications;

(2) That § 1325(a)(1) requires that a plan "compl[y] with the provisions of this chapter;" and

(3) That the reference to the applicable commitment period in § 1329(c) indicates Congressional intent to incorporate the provisions requiring compliance with the applicable commitment period into a plan modification. *In re Grutsch*, 453 B.R. 420, 425 (Bankr. D. Kan. 2011).

ii) See, e.g., *In re King*, 439 B.R. 129 (Bankr. S.D. Ill 2010);

(1) Holding challenged by *In re Swain*, 509 B.R. 22 (E.D. Va. 2014).

(2) An interpretation of section 1329 to include section 1325(b) is consistent with the idea that the commitment period is intended to determine the plan length.

(3) Imposing a fixed, minimum duration for chapter 13 plan confirmation and modification is consistent with pre-BAPCPA practice. Pre-BAPCPA, a debtor was rarely permitted to conclude a plan in less than 36 months. 11 U.S.C. § 1325(b)(1)(B) (2004). The court interprets § 1325(b) to mean that Congress substituted an "applicable commitment period" for the previously mandatory three-year repayment term. Section 1325(b)(4)(B) imposes a minimum plan duration, unless full repayment is made to unsecured creditors in a shorter time. The court

notes that "BAPCPA obviously precipitated many changes in Chapter 13 practice," but does not conclude that the elimination of a minimum plan length in cases where a debtor is not proposing to pay 100% to their unsecured creditors is one of those changes. 439 B.R. at 135 (Bankr. S.D. Ill. 2010).

(4) An interpretation of 1329 that includes 1325(a) is the only construction that gives meaning to 521(f), which allows the court and other parties to monitor the debtor's financial situation to determine the necessity of plan modification.

(5) Court believes that it has the authority to consider changes in the debtor's income at the time a proposed modified plan is filed per *In re Lanning*, 560 U.S. 505 (2012).

iii) *In re Heyward*, 386 B.R. 919 (Bankr. S.D. Ga. 2008)

(1) Holding challenged by I*n re Barnes*, 506 B.R. 777 (E.D. Wis. 2014)

(2) A below-median-income debtor moved post-confirmation to seek a reverse mortgage so he could make his payments early. The court allowed the reverse mortgage transaction but did not allow him to pay early unless the funds obtained from the reverse mortgage transaction were sufficient to pay off unsecured creditors in full.

2) **POST-CONFIRMATION WINDFALLS** – unanticipated change standard / discretionary standard

a) *In re Ormiston*, 501 B.R. 303 (Bankr. E.D. N.C. 2013) (Post Confirmation inheritance is property of the estate and Trustee's Motion To Modify granted)

i) Basis of the holding is the unanticipated change in the debtor's financial circumstances after confirmation.

b) *In re McAllister*, 510 B.R. 409 (Bankr. N.D. Ga. 2014) (Life insurance proceeds not property of the estate, Trustee's Motion To Modify denied.)

i) Holding challenged by *In re Gilbert*, 526 B.R. 414 (N.D. Ga. 2015).

c) *Carroll v. Logan (In re Carroll)*, 735 F.3d 147 (4th Cir. 2013)(Inheritance received more than 180 post-petition was property of the estate and Debtors could not deprive their creditors a part of their windfall) (Contrasted to and challenged by *In re McAllister*)

i) Basis of the holding is the interaction of Sections 541 and 1306. Section 541 includes in property of the estate: "Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date— by bequest, devise, or ***inheritance*** [.]" 735 F.3d at 150.

ii) Section 1306 expands the definition of property of the estate by saying that it includes property specified in Section 541, and (1) all property ***of the kind specified in such section*** that the debtor acquires after the commencement of the case but ***before the case is closed, dismissed, or converted*** to a case under chapter 7, 11, or 12 of [the Code], whichever occurs first." *Id.*

iii) This is because the TYPE of property is a distinct concept from the time at which the debtor acquired his interest in the property. *See In re Tinney,* 07-42020-JJR13, 2012 WL 2742457 at *2 (Bankr.N.D.Ala. July 9, 2012).

iv) Most courts agree that 1306 modifies the time period in chapter 13 cases. *In re Vannordstrand*, 356 B.R. 788, 2007 WL 283076, at *2 (B.A.P. 10th Cir.2007).

d) What types of unanticipated changes will permit modification under the unanticipated change standard?

i) Must be substantial and must be a change that substantially affects the debtor's ability to make future payments. Must also be something that was not taken into account at the time of confirmation.

(1) Refinancing of a mortgage is not sufficient for modification – *In re* Murphy, 474 F.3d 143 (4th Cir. 2013).

(2) Tax refund is also insufficient – *In re Flennory*, 280 BR 896 (S.D. Ala. 2001).

ii) Other courts conclude that no change in circumstance is necessary for post-confirmation modification of a plan. These courts conclude that because § 1329 explicitly permits modification of a confirmed plan, it operates as a statutory exception to the principle of claim preclusion. *In re Lopez*, No. 09-81662-PWB, 2011 WL 4017514, at *3 (Bankr. N.D. Ga. July 19, 2011).

3) MAY A DEBTOR PAY-OFF HIS CONFIRMED CHAPTER 13 EARLY, MODIFICATION OR NO MODIFICATION?

a) **Yes** - *In re Smith*, 449 B.R. 817 (Bankr. M.D. Fla. 2011) (*Motion To Approve Early Payoff* granted)

i) Holding challenged by *In re Rhymaun*, 2011 WL 9378787 (S.D. Fl. 2011), which did *not* allow an above-income debtor to modify plan early.

ii) Due to the debtor's decrease in income, unsecured creditors may have feared that debtor's waiting too long to pay would result in debtor's default, seeking a downward modification of her payments, or abandoning her plan by filing chapter 7.

b) **Yes** - *In re Ezzell*, 438 B.R. 108 (Bankr. S.D. Tex 2010)(Receipt of funds sufficient to pay off base of confirmed plan precluded Trustee's Motion to Modify)

i) Completion of payment occurs when a debtor makes payments to the trustee, not when a trustee makes payments to creditors.

ii) See also *In re Ruth*, 505 B.R. 804 (Bankr. S.D. Tex. 2014)

4) MODIFICATION TO SURRENDER COLLATERAL – CAN CONFIRMED PLANS BE MODIFIED TO ALLOW DEBTORS TO SURRENDER THEIR COLLATERAL AND RECLASSIFY ANY DEFICIENCY AS AN UNSECURED CLAIM?

i) **Yes** – *In re Tucker*, 500 B.R. 457 (Bankr. N.D. Miss. 2013)

(1) However, in this particular case, debtor acted in bad faith through undue delay in seeking to surrender collateral and doing so after the collateral was damaged by fire. This is a violation of the good faith requirement in 1325(a)(3).

ii) **No** – *In re Nolan*, 232 F.3d 538 (6th Cir. 2000)

(1) Holding has been challenged – *Bank One, NA v. Leuellen*, 322 B.R. 648 (S.D. Ind. 2005).

(a) "This court has considered *Nolan* carefully, and respectfully disagrees with its interpretation of section 1329(a) as forbidding in all cases modifications like the one in this case. This modification allows Chapter 13 debtors who experience a dramatic change in their income, and who act in good faith and with the bankruptcy court's approval, to surrender collateral to the secured creditor, to treat any deficiency as an unsecured debt, in order to avoid liquidation under Chapter 7 and to continue making payments to creditors." 322 B.R. at 656.

Saturday July 4th

3:00 - 4:00 The Consumer Financial Protection Bureau: Why You Need to Know About the CFPB and How it Affects Your Practice.
Moderator: Russell A. Brown, Chapter 13 Standing Trustee for the District of Arizona (Phoenix)
Joann Needleman, Clark Hill, P.C. (Philadelphia, PA)

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The Consumer Financial Protection Bureau:

What You Need to Know About the CFPB and How it Affects Your Practice.

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Russell Brown

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Disclaimer

This information is not intended to be legal advice and may not be used as legal advice. Legal advice must be tailored to the specific circumstances of each case. Every effort has been made to assure this information is up-to-date. It is not intended to be a full and exhaustive explanation of the law in any area. It should not be used to replace the advice of your own legal counsel.

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REGULATORY HISTORY & BACKGROUND

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Federal Trade Commission (FTC)

- Primary agency in charge of consumer protection for financial services
- Limited authority - no rulemaking for FDCPA or Mortgage Servicing

Consumer Financial Protection Bureau (CFPB)

- Dodd-Frank Wall Street Reform and Consumer Protection Act
- Authorizes the Consumer Financial Protection Bureau

Authority of the Bureau

- ✓ Mission - make rules more effective, consistently and fairly enforcing rules, and empower consumers to take more control over their financial lives
- ✓ Supervise, examine and enforce covered persons - banks and non-banks
- ✓ Issue regulations under the enumerated consumer protection laws including UDAAP, FCRA, FDCPA, RESPA & TILA

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Structure of the CFPB

- Consumer response team (complaint portal)
- Consumer Education and Engagement
- Supervision Enforcement and Fair Lending
- Research, Markets & Regulation

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How the CFPB discharges its authority

- Power to investigate
  - i. Civil Investigation Demand (Supervise)
  - ii. Examination (either on-site or by deposition)
  - ii. Enforcement (bring law suit and enter into consent orders)
- Through bulletins, white papers or research - policy making without formal rule making
- Examination Manuals

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RULES REGARDING MORTGAGES AND SERVICING

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Initial Mortgage Rule – January 2013 eff. January 2014

- Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act (Regulation Z)
  - ✓ Minimum requirements for ability to pay
  - ✓ Presumptions for qualified mortgage (QM) - strengthens requirement for sub-prime loans and rebuttable presumption that sub-prime is not a QM
  - ✓ Requirements for QM – what is needed

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2013 – Mortgage Servicing Rules eff. February 2013 Reg X (RESPA)

- Error resolution and information requests (§§ 1024.35 and 1024.36) – procedures to respond to information request and complaints of error
- Force-placed insurance (§ 1024.37) – prohibited unless a reasonable basis that no hazard insurance exists, 45 days advanced notice and 30 days after 1st notice and 15 days before insurance in place
- General servicing policies, procedures, and requirements (§ 1024.38)
- Early intervention with delinquent consumers (§ 1024.39) – good faith efforts to establish **live contact** with borrowers by 36th day of delinquency to inform of loss mitigation options
- Continuity of contact with delinquent consumers (§ 1024.40) – maintain reasonable policies and procedures to enable delinquent borrowers access to server personnel to assist with loss mitigation options

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Significant Changes to Loss Mitigation Options for Consumer

- Loss mitigation (§ 1024.41) – Specific procedures to evaluate loss mitigation options – (loan modification). When a servicer receives a timely loss mitigation application, the servicer must
  - Acknowledge receipt and inform the borrower whether the application is complete or incomplete
  - Evaluate complete loss mitigation applications within 30 days for all loss mitigation options available to the applicant
  - Notify the borrower of the results of the evaluation as well as evaluate timely appeals
  - Refrain from beginning or completing the foreclosure process when a borrower is being evaluated for loss mitigation options.
  - Reasonable diligence in obtaining documents and information
  - Dual tracking prohibited – unless account is more than 120 days delinquent, violation of due on sale clause or servicer is joining foreclosure as a subordinate

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2013 – Mortgage Servicing Rules eff. February 2013 Reg Z (TILA)

- Interest rate adjustment notices for ARMs (§ 1026.20) – notices between 210 and 240 days before 1st payment after rate first adjust, and 60 to 120 days notice before payment at new level is due when rate adjustment causes payment to change (sample forms)
- Prompt crediting of mortgage payments and responses to requests for payoff amounts (§ 1026.36(c)) – crediting as of the day of receipt and payoffs within 7 days after receipt of written request
- Periodic statements for mortgage loans (§ 1026.41) – how, when and what manner statements must be sent, exemptions if get a coupon book or small servicer (sample forms)

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Amendments - October 2013 Bankruptcy & FDCPA Addressed

- Clarifies compliance requirements in relation to bankruptcy law and the FDPCA – servicers needed guidance on how to communicate with consumers in light of bankruptcy and delinquency (live contact)
- Servicers expressed concern about how to fulfill servicing requirements without violating the law
- Bankruptcy trustees expressed concerned about consumers being confused by communication during bankruptcy

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Bankruptcy Exemptions – Loss Mitigation

- 1024.39(d)(1) Borrowers in Bankruptcy - servicers exempt from loss mitigations when debtor in bankruptcy , but adds:
  - **Comment 39(d)(1)-2** which states that with respect to any portion of the mortgage debt that is not discharged, a servicer must resume compliance with § 1024.39 after the first delinquency that follows the earliest of any of three potential outcomes in the borrower's bankruptcy case: (i) the case is dismissed, (ii) the case is closed, or (iii) the borrower receives a discharge under 11 U.S.C. §§ 727, 1141, 1228, or 1328
  - **Comment 39(d)(1)-3** clarifies that the exemption applies when any of the borrowers who are joint obligors with primary liability on the mortgage loan is a debtor in bankruptcy.

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Bankruptcy Exemptions – Periodic Statement Requirement

- 1026.41(e)(5) - exempting a servicer from the periodic statement requirements in § 1026.41 for a mortgage loan while the consumer is a debtor in bankruptcy
  - **Comment 41(e)(5)-1** clarifies that the exemption begins once a petition has been filed commencing a case under Title 11 of the United States Code in which the consumer is a debtor.
  - **Comment 41(e)(5)-2** clarifies that with respect to any portion of the mortgage debt that is not discharged, a servicer must resume sending periodic statements in compliance with § 1026.41 within a reasonably prompt time after the next payment due date that follows the earliest of any of three potential outcomes in the consumer's bankruptcy case: (i) the case is dismissed, (ii) the case is closed, or (iii) the consumer receives a discharge under 11 U.S.C. §§ 727, 1141, 1228, or 1328. However, this requirement to resume sending periodic statements does not require a servicer to communicate with a consumer in a manner that would be inconsistent with applicable bankruptcy law or a court order in a bankruptcy case.

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FDCPA Implications

- **1024.39(d)(2)** Fair Debt Collection Practices Act - Bureau concludes that the FDCPA "cease communication" provision does not override servicers' obligations to have various communications with borrowers, ***live contact rule for loss mitigation options***, that are specifically mandated by the Dodd-Frank Act or to respond to certain ***borrower-initiated communications*** in accordance with the 2013 Mortgage Servicing Final Rules.
- **1024.39(d)(2)** exempts a servicer that is a debt collector under the FDCPA with respect to a borrower from the other requirements of § 1024.39 after the borrower has exercised this "cease communication" right.
  - Bureau encourages servicers to pursue loss mitigation options to the extent that the FDCPA permits - ***not sure how you can do that if you get a C&D***

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But wait…. more Amendments in November 2014

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- Successors in Interest - The proposed amendments will define "borrower" or "consumer" to include successors in interest and would permit a successor in interest to retain "the same rights as the original owner, with no change in substance," including rights related to early intervention, continuity of contact, and loss mitigation assistance
- Definition of Delinquency - Defined in some sections but not all. Newly proposed delinquency definition is "a period of time during which a borrower and the borrower's mortgage loan obligation are delinquent. A borrower and borrower's mortgage loan are delinquent beginning on the date a periodic payment sufficient to cover principal, interest, and, if applicable, escrow became due and unpaid, until such time as the outstanding payment is made."
- Information Request - Amend how servicers respond to request for information concerning loans in trust for which Frannie & Freddie are the trustee, by not requiring servicer to provide the name of the trust if not specifically requested by borrower
- Forced Placed Insurance - Notice requirements relaxed to instances when servicer wishes to force place insurance when insufficient coverage exists and permits mortgage account number on all notices

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- Early Intervention/Live Contact - more clarification on "good faith attempts" and permits a combination of attempts to contact for other purposes (loss mitigation options)

  Borrowers in Bankruptcy - Must comply with live contact requirement for a non-debtor with someone in a Chapter 7 or 11, exempt from live contact with a debtor in a Chapter 12 or 13

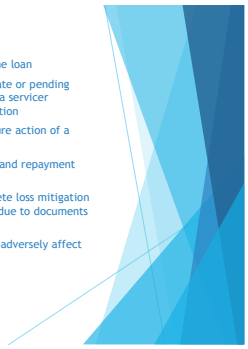
  ✓ Have to comply with early written intervention notice requirements for all debtors in bankruptcy unless
    - no loss mitigation requirements available,
    - plan provides for surrender of property or avoidance of lien, or no provision for payment of pre-bankruptcy arrears or maintenance due under the loan
    - statement of intent to surrender property; or
    - order to avoid lien or lift stay entered

  FDCPA - Exempt for C&D remains

  ✓ Exemption from written early intervention notice (notice) applies only if no loss mitigation options available, if they are available required to send a modified notice set forth in the rules
    - To rely on exemption, C&D must be received and servicer is a debt collector
    - Safe harbor notice that would not otherwise violate the FDCPA
    - If Borrower in bankruptcy and exercised C&D rights, servicer must provide notice only if borrower is represented by someone authorized to communicate with servicer

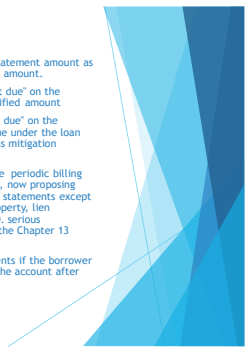
Loss Mitigation

- Procedures would be required during the life of the loan
- Foreclosures would have to be dismissed if sale date or pending foreclosure would interfere or otherwise prohibit a servicer sufficient time to evaluate loss mitigation application
- Permit servicer of a junior lien to join in foreclosure action of a senior lien , even if junior lien is not delinquent
- Permits servicers to offer short term forbearance and repayment plans
- Enhance borrowers' rights in relations to a complete loss mitigation plan and prevents a servicer from denying a plan due to documents not in the borrowers control
- Codify policy that transfer of servicing should not adversely affect borrower who is pursuing loss mitigation.



Periodic Statements

- Accelerated loan - servicers have to include the reinstatement amount as the "amount due" as opposed to the entire accelerated amount.
- Under a permanent loss mitigation option, the "amount due" on the periodic billing statement shall be the permanent modified amount
- Under a temporary loss mitigation option, the "amount due" on the periodic billing statement can be either the amount due under the loan documents or the amount due under the temporary loss mitigation program.
- Although bankruptcy accounts were exempted from the periodic billing statement requirements in October 2013 amendments, now proposing that bankrupt accounts begin receiving periodic billing statements except under specific exceptions, such as surrender of the property, lien avoidance, lift stay, or borrower specific asserts a C&D. serious consideration given to sending periodic statements to the Chapter 13 trustee.
- Permit servicers to forego sending charged-off statements if the borrower will not be charged any additional fees or interest on the account after charge-off.

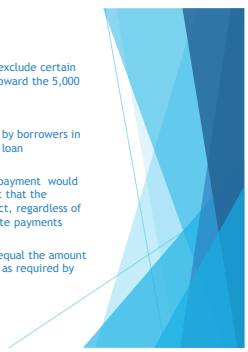


Small Servicers

- greater flexibility - proposed amendments would exclude certain seller-financed transactions from being counted toward the 5,000 maximum loan limit to qualify as a small servicer

Payment Processing

- clarify how servicers should treat payments made by borrowers in temporary loss mitigation programs or permanent loan modifications
- Under temporary loss mitigation option, periodic payment would still be the principal, interest, and escrow amount that the borrower is required to pay under the loan contract, regardless of whether the borrower is required to make alternate payments under the loss mitigation agreement.
- Under a modified loan a periodic payment would equal the amount sufficient to cover principal, interest, and escrow as required by the modified agreement.



2015 Priorities for the CFPB

- Debt Collection Rules – including rules on time-barred debt, which may impact proofs of claim
- Credit Reporting – possibility of requiring discharged debt to be deleted from credit report
- Medical debt - credit reporting of medical debt
- Student Loan – supporting policies which will permit dischargeability of student loan debt.
- Auto Financing – ability to pay rules
- Small Dollar Lending - ability to pay and preclusions on periodic loans

QUESTIONS ?

Saturday July 4th

3:00 - 4:00 Where in the Code Does It Say? An Examination of Bankruptcy Terms We All Use and Their Sources.

Beverly M. Burden, Chapter 13 Standing Trustee for the Eastern District of Kentucky (Lexington)

Ashley D. Bruce, Berger Singerman LLP (Fort Lauderdale, FL)

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l. **Debtors can request a “hardship discharge”?**

m. **Debtors can discharge divorce-related property settlement claims (unless they get a “hardship discharge”)?**

n. **Debtors can discharge § 523(a)(6) debts for “willful and malicious injury by the debtor to another entity or to the property of another entity” (unless they get a “hardship discharge”)?**

o. **Who gets money on hand when case converts after confirmation?**

p. **Court may enter a "drop-dead" order?**

Where In The Code Does It Say:	Statute(s)
Mortgage "arrearages" can be cured through the plan while regular mortgage payments resume?	**11 U.S.C. § §§ 1322(c)(1) and 1322(b)(5)**

One significant power that chapter 13 grants to debtors is the right to cure defaults on long-term debts pursuant to § 1322(b)(5). Section 1322(b)(5) is the Bankruptcy Code section that allows a debtor to cure defaults on a mortgage debt and maintain regular payments on the mortgage.[1] That provision – limited to debts "on which the last payment is due after the date on which the final payment under the plan is due" – states that a chapter 13 plan may "provide for the curing of any default within a reasonable time," but only if the plan also provides for "maintenance of payments while the case is pending." Section 1322(c) allows debtors to cure defaults on their principal residence until the "hammer falls" at a foreclosure sale.[2]

Chapter 13 plans utilizing this provision are called "cure and maintain plans." Cure and maintain plans are quite common and beneficial for debtors allowing them the ability to take up to 5 years to pay an often substantial pre-petition mortgage arrearage while otherwise not impairing the lender's contractual rights. If this "cure and maintain" approach is chosen by chapter 13 debtor, then the plan must provide for maintenance of payments while debtor's case is pending, which requires the same principal and interest payments as provided in the note, within the time frame specified in the note. If chapter 13 debtor is successful in curing her default, the

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[1] Section 1322(b) provides in part:

> Subject to subsections (a) and (c) of this section, the plan may—
>
> (2) modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims;
>
> (3) provide for the curing or waiving of any default;
>
> . . .
>
> (5) notwithstanding paragraph (2) of this subsection, 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;

11 U.S.C. § 1322(b).

[2] Section 1322(c) provides:

> Notwithstanding subsection (b)(2) and applicable nonbankruptcy law— (1) a default with respect to, or that gave rise to, a lien on the debtor's principal residence may be cured under paragraph (3) or (5) of subsection (b) until such residence is sold at a foreclosure sale that is conducted in accordance with applicable nonbankruptcy law; . . .

11 U.S.C. § 1322(c) (emphasis added).

debt is reinstated to its pre-default position, thereby returning the debtor and creditor to their respective positions before the default.

The filing of a chapter 13 case operates to "de-accelerate" a mortgage that was accelerated by the debtor's prepetition default:

> Section 1322(b)(5) begins with the phrase "notwithstanding paragraph (2) of subsection." Additionally, § 1322(c) begins with the phrase "Notwithstanding subsection (b)(2) ..." referencing the same subsection. It is apparent from the plain reading of the Bankruptcy Code that the limiting language of subsection § 1322(b)(2) does not disallow the cure of the default of a debtor's residence. This section of the code safeguards a debtor's right in a chapter 13 case to cure a home mortgage default. The Tenth Circuit has long-standing law that states that 1322(b)(3) and (5) permit the plan to cure an default. If a residential mortgage is in default triggering contractual acceleration of the mortgage debt, a chapter 13 plan to "de-accelerate" by paying the amount of the original default rather than the entire accelerated debt, is a permissible cure, not a prohibited modification.

In re Monson, No. 09-20487, 2009 WL 4663864, at *2 (Bankr. D. Wyo. Dec. 7, 2009); s*ee also* Oliveiri, David, *Right of Debtor to "De-acceleration" of Residential Mortgage Indebtedness under Chapter 13 of Bankruptcy*, 67 A.L.R. Fed. 217 (Originally published in 1984).

Where In The Code Does It Say:	**Statute(s)**
What it means to pay a claim "outside the plan"?	**11 U.S.C. §§ 1322(b)(2); 1322(b)(5); 1326(c)**

Under the Bankruptcy Act of 1938, if a secured creditor objected to a plan in a Chapter XIII case, the plan could not be confirmed. To deal with the objecting creditor, the solution was to not pay the claim through the plan and to make payments to the creditor directly. Eventually the phrase "outside the plan" came into favor as descriptive of the exclusion of an objecting creditor from the plan. *See* Keith M. Lundin & William H. Brown, *Chapter 13 Bankruptcy*, 4th Ed. § 103.2 at para. 2 (rev. Jan. 5, 2011), www.ch13online.com.

Under the present Bankruptcy Code, the use of the phrase "outside the plan" is a misnomer to describe the payment of a claim directly by the debtor to the creditor. The chapter 13 plan needs to designate how each secured claim is to be treated. The claim is not "outside the plan"; instead, the plan provides that the debtor will pay the creditor directly. *Foster v. Heitkamp (In re Foster)*, 670 F.2d 478 (5th Cir. 1982).

Start with 11 U.S.C. § 1322, which describes what a plan may do. Section 1322(b)(2) provides that a plan may modify the rights of holders of claims ". . . or leave unaffected the rights of holders of any class of claims."

Under section 1322(b)(5), the 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." 11 U.S.C. § 1322(b)(5).

Section 1322(b)(2) and 1322(b)(5) describe how a plan may treat claims, but neither paragraph mentions who is to make payments on those claims.

Go next to 11 U.S.C. § 1326 ("Payments"). Subsection (c) states: "Except as otherwise provided in the plan or in the order confirming the plan, the trustee shall make payments to creditors under the plan." 11 U.S.C. § 1326(c) (emphasis added). Thus, it would appear that a plan may provide that the debtor will make payments to directly to creditors.

That right is not absolute. It is within the bankruptcy court's discretion whether to allow a debtor to be the "disbursing agent" based on factors "such as administrative efficiency, tracking of payments, fairness and treatment of creditors, and the determination that there is a reduction of plan failure when all payments are made through the plan." *Cohen v. Lopez (In re Lopez)*, 550 F.3d 1202 (9th Cir. BAP 2008); see also *Foster v. Heitkamp (In re Foster)*, 670 F.2d 478 (5th Cir. 1982). Another factor, discussed elsewhere in these materials, is whether it is "feasible" for the debtor to make payments directly to creditors as well as plan payments. *See, e.g.*, *In re Carey*, 402 B.R. 327 (Bankr. W.D. Mo. 2009).

Whether or not the debtor makes direct payments on their home mortgages usually depends on the customs and rules of the local jurisdiction. Having the trustee make the debtor's mortgage payments while in a chapter 13 case (with the debtor taking over after completion of the plan) is often referred to as paying mortgages "through the plan" or making "conduit" mortgage payments through the trustee (in addition to saying the debtor is paying the mortgage "outside the plan").

The various arguments for and against permitting a debtor to make direct payments on secured claims is beyond the scope of this handout. However, practitioners should be aware of the prevailing law in their jurisdictions as to whether the automatic stay is affected by the decision to make direct payments. In *Telfair v. First Union Mortgage Corp.*, 216 F.3d 1333 (11th Cir. 2000), the 11th Circuit Court of Appeals concluded that the automatic stay terminates as to a creditor receiving direct payments from the debtor when confirmation vested property of the estate in the debtor.[3]

Proposing to make direct payments to an unsecured creditor will often trigger an objection to confirmation by the trustee. Treating one unsecured creditor differently from other unsecured creditors is a separate "classification" of the claim. Title 11 U.S.C. § 1322(b)(1) provides that a plan may "designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated . . . ." Paying one unsecured creditor in full by direct payments to the creditor would be unfair to those creditors receiving less than payment in full through the plan.

However, in some jurisdictions plans providing for the payment of long-term unsecured debts pursuant to 11 U.S.C. § 1322(b)(5), such as student loans, are confirmed.

[3] *See* 11 U.S.C. § 1327(b) ("Except as otherwise provided by the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor"), and 11 U.S.C. § 362(c)(1) ("(c) Except as provided in subsections (d), (e), (f), and (h) of this section – (1) the stay of an act against property of the estate under subsection (a) of this section continues until such property is no longer property of the estate.").

Where In The Code Does It Say:	**Statute(s)**
Debtors may "cram down" a secured claim to the value of the collateral?	**11 U.S.C. §§ 1322(b)(2); 1325(a)(5)(B)(ii); 506(a).**

First of all, just what is a "cram down"? There is no definition of the phrase in 11 U.S.C. § 101. The term came into use with respect to an amendment to section 77 of the old Bankruptcy Act in 1935 dealing with business reorganizations.[4] As one district judge described in a 1976 pre-Bankruptcy Code opinion:

> "Cram down" is a term used by some bankruptcy lawyers and bankruptcy commentators to describe the application of § 461 under Chapter XII and § 216 under Chapter X of the [Bankruptcy] Act upon a dissenting class of creditors where the proposed plan failed to receive approval of the requisite majority. The Court has found no judicial or other authoritative definition or discussion of the term or, indeed, few articles which discuss the term oft used by lawyers. Nevertheless, it is a self-evident, vivid connotation of the involuntary administration of bad medicine upon a recalcitrant victim, the secured creditor who opposes the effects of the reorganization proceedings in the Bankruptcy Court.

In the Matter of Pine Gate Assoc, Ltd., 1976 WL 359641 (N.D. Ga. 1976) (emphasis added). Although the term "cram down" is most commonly used in connection with chapter 11, its use has crept into the parlance of chapter 13 practitioners.

A "cram down" is a bifurcation or splitting of a claim into a secured claim to the extent of the value of the collateral, and an unsecured claim as to any deficiency. Debtors propose plans to retain property and pay for it through the plan. The amount that must be paid as a secured claim is equal to the value of the property being retained. Creditors often object, arguing that the collateral is worth more than what the debtors are proposing to pay for the collateral. It is not uncommon for courts to conduct evidentiary hearings to determine the value of the collateral.

So where is the "cram down" power in chapter 13 cases found in the Bankruptcy Code?

[4] *See Callaway v. Benton*, 336 U.S. 132 (1949).

Start with 11 U.S.C. § 1322(b), which describes what a chapter 13 plan may do. Section 1322(b)(2) provides that the plan may "modify the rights of holders of secured claims . . . ."[5] (emphasis added).

Then look at the confirmation requirements of 11 U.S.C. § 1325. Under section 1325(a), the court shall confirm a plan if a number of conditions are met. Right now, we are only concerned with relevant parts of 11 U.S.C. § 1325(a)(5), which provides in part: "(5) with respect to each allowed secured claim provided for by the plan - . . . (ii) the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim; . . . ." (emphasis added).

To determine the allowed amount of a secured claim, we go to 11 U.S.C. § 506(a)(1) (which was just § 506(a) prior to BAPCPA). The Supreme Court has pointed out that the phrase "allowed secured claim" is found throughout the Bankruptcy Code. As Justice Scalia described in his dissent in *Dewsnup v. Timm*,

> Congress did not leave the meaning of "allowed secured claim" to speculation. Section 506(a) says that an "allowed secured claim" (the meaning of which is obvious) is also a secured claim "to the extent of *the value of [the] creditor's interest in the estate's interest in [the securing] property."* (Emphasis added.) (This means, generally speaking, that an allowed claim "is secured only to the extent of the value of the property on which the lien is fixed; the remainder of that claim is considered unsecured." *United States v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 239, 109 S.Ct. 1026, 1029, 103 L. Ed.2d 290 (1989)).

Dewsnup v. Timm, 502 U.S. 410, 420-21 (1992) (Scalia, J., dissenting) (emphasis and bracketed words original).

The cram down power in chapter 13 cases was discussed in the case of *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997), a case in which the method of valuing collateral was decided. Section 506 was amended in 2005 by BAPCPA to provide for a "replacement value" standard for valuation in chapter 13 cases. *See* 11 U.S.C. § 506(a)(2).

There are exceptions to the claim bifurcation or "cram down" power. In particular, a plan may not modify the rights of a creditor holding a claim secured only by a security interest in real property that is the debtor's principal residence. 11 U.S.C. § 1322(b)(2). This is often referred to as the "anti-modification" clause of § 1322(b)(2). And section 506 does not apply to a secured claim if the creditor has a purchase money security interest in the debt, the debt was incurred within 910 days prior to the filing of the bankruptcy petition, and the collateral is a motor vehicle

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[5] The plan may: . . .

> (2) modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims;

11 U.S.C. § 1322(b)(2).

acquired for the personal use of the debtor (often referred to as "910-claims"); nor does section 506 apply if the collateral is "any other thing of value" and the debt was incurred within one year of the petition. 11 U.S.C. § 1325 (unnumbered paragraph following (a)(9)).

The process of bifurcating a claim in chapter 13 in a way mimics what would occur to the creditor's claim outside of bankruptcy. A secured creditor would repossess its collateral, sell it, and thereby realize the value of the collateral through the sale. Any remaining unpaid portion of the debt would be (in most jurisdictions) an unsecured deficiency claim. The creditor would have state law remedies of garnishment, execution, etc., and may collect all or part of the unsecured claim, or the debt may turn out to be uncollectible.

In a chapter 13 case, the creditor will receive the value of its collateral through plan payments over time, and to compensate the creditor for the delay in realizing the full value of the collateral, the creditor is paid through the plan with interest (discussed elsewhere in these handouts). The creditor has an unsecured deficiency claim, and it might receive a distribution on its unsecured claim through the plan. When considered from this perspective, a chapter 13 "cram down" is not quite the "involuntary administration of bad medicine upon a recalcitrant victim" described above.

Where In The Code Does It Say:	Statute(s)
Debtors can "strip off" a second lien and treat it as unsecured?	**11 U.S.C. §§ 506 and 1322(b)**

One notable exception of loans for property that cannot be crammed down under chapter 13 is with respect to liens secured only by a security interest in real property that is the debtor's principal residence (11 U.S.C. § 1322(b)(2), the "anti-modification clause"). The Supreme Court in *Nobelman v. Am. Sav. Bank*, 508 U.S. 324 (1993), interpreted § 1322(b)(2) as precluding a "strip down" of a partially secured lien against a principal residence in chapter 13. That is, a debtor may not reduce an underwater mortgage to the value of the principal residence because partially secured lien-holders are "holders of secured claims" protected against lien modification.

Nobelman notwithstanding, however, courts have generally permitted a "strip off" of completely valueless liens in chapter 13 cases because, unlike the lienholder in *Nobelman*, holders of such liens are not "holders of secured claims" and, therefore, are not entitled to the protection of § 1322(b)(2). A number of circuit courts of appeal and bankruptcy appellate panels have weighed in since *Nobelman* and every circuit court that has addressed the issue has held that § 1322(b)(2)'s anti-modification provisions do not bar a chapter 13 debtor from stripping off wholly unsecured liens on the debtor's principal residence.[6]

To exercise this authority, bankruptcy courts rely on §§ 506 and 1322(b) of the Bankruptcy Code. First, courts apply the valuation procedure in § 506(a) to bifurcate a claim into a secured and unsecured portion. Sections 506(a)(1) and (d) provide:

> (a)(1) An allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to setoff is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.
>
> . . .
>
> (d) To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void. . . .

[6] *TD Bank, N.A. v. Davis (In re Davis)*, 716 F.3d 331 (4th Cir. 2013); *Zimmer v. PSB Lending Corp. (In re Zimmer)*, 313 F.3d 1220 (9th Cir. 2002); *Lane v. W. Interstate Bancorp (In re Lane)*, 280 F.3d 663 (6th Cir. 2002); *Pond v. Farm Specialist Realty (In re Pond)*, 252 F.3d 122 (2d Cir. 2001); *Tanner v. FirstPlus Fin. (In re Tanner)*, 217 F.3d 1357 (11th Cir. 2000); *Bartee v. Tara Colony Homeowners Ass'n (In re Bartee)*, 212 F.3d 277 (5th Cir. 2000); *McDonald v. Master Fin. (In re McDonald)*, 205 F.3d 606 (3d Cir. 2000).

11 U.S.C. § 506(a)(1), (d) (emphasis added).

Next, courts look to § 1322(b)(2), which provides that, subject to certain exceptions, a chapter 13 bankruptcy plan may modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims. Section 1322(b) provides that:

> Subject to subsections (a) and (c) of this section, the plan may—
>
> . . .
>
> (2) modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims;

11 U.S.C. § 1322(b)(2) (emphasis added).

Applying this framework, a completely valueless lien is classified as an unsecured claim under § 506(a). Only then does a bankruptcy court consider the rights of lienholders under § 1322, which affords protection to holders of secured claims against principal residences. Section 1322, however, expressly permits modification of the rights of unsecured creditors. The end result is that § 506(a), which classifies valueless liens as unsecured claims, operates with § 1322(b)(2) to permit a bankruptcy court, in a chapter 13 case, to strip off a lien against a primary residence with no value.

Where In The Code Does It Say:	Statute(s)
Debtors may file a "Chapter 20" to strip-off a lien that could not be stripped off in a chapter 7?	**11 U.S.C. §§ 506, 1322(b), 1328(f), 1325(a)(5)(B)(i).**

As of the date of these materials, a debtor in a chapter 7 case may not strip off a junior lien that is wholly unsecured, *Dewsnup v. Timm*, 502 U.S. 410, 112 S.Ct. 773 (1992), except in the 11th Circuit.[7]

One solution debtors have employed is to file a chapter 7 case, obtain a discharge, and soon thereafter file a chapter 13 case for the sole or primary purpose of stripping off the junior lien. This chapter 7 + chapter 13 has come to be known as a "chapter 20."

The Supreme Court recognized the viability of a "chapter 20" case in *Johnson v. Home State Bank*, 501 U.S. 78, 111 S.Ct. 2150 (1991), holding that a mortgage lien which survived the discharge of personal liability in a chapter 7 case remains a claim that can be dealt with in a successive chapter 13 plan.

Although debtors who file a chapter 13 in the first instance may strip-off the junior lien, debtors who make use of a chapter 20 are not always successful in stripping off the lien, and the reason lies in changes made to the availability of a discharge in a chapter 13 case following BAPCPA.

Since the enactment of BAPCPA, a debtor in chapter 13 may not receive a discharge if s/he received a discharge in a case filed under chapter 7, 11, or 12 during the 4-year period prior to the chapter 13 petition. 11 U.S.C. § 1328(f)(1).

Some courts have held that a chapter 20 debtor may not strip off a wholly unsecured junior lien because the debtor is not entitled to receive a discharge in the successive chapter 13 case. *See, e.g.*, *In re Gerardin*, 447 B.R. 342 (Bankr. S.D. Fla. 2011). These courts read section 1328(f)(1) in conjunction with the lien retention provisions in 11 U.S.C. § 1325(a)(5)(B)(i) to conclude that a debtor who cannot get a chapter 13 discharge may not strip off a lien.

Other courts have held that section 1325(a)(5) has no applicability because the debt is unsecured, and that the debtor's eligibility for a discharge has no bearing on the issue. Hence, the lien can be stripped off. *In re Davis*, 716 F.3d 331 (4th Cir. 2013).

[7] The 11th Circuit allows lien-stripping in chapter 7 cases. *In re McNeal*, 735 F.3d 1263 (11th Cir. 2012). The Supreme Court recently heard arguments in two cases arising from the 11th Circuit: *In re Caulkett (Bank of America, N.A. v. Caulkett)*, 566 Fed.Appx. 879 (Mem. 2014) *cert. granted*, 135 S.Ct. 674 (November 17, 2014), and *In re Toledo-Cardona (Bank of America, N.A. v. Toledo-Cardona)*, 566 Fed.Appx. 911 (Mem. 2014), *cert. granted* 135 S.Ct. 677 (November 17, 2014) to consider whether *Dewsnup* precludes a strip-off of a wholly unsecured lien in a chapter 7 case. A decision is expected before the end of this term.

The use of a chapter 20 to strip off underwater liens may or may not have continued viability depending on how the Supreme Court rules in the *Caulkett* and *Toledo-Cardona* cases this term.

Where In The Code Does It Say:	Statute(s)
Interest must be paid on secured claims?	**11 U.S.C. § 1325(a)(5)(B)(ii)**

In a chapter 13, the debtor can pay for the value of a secured claim (i.e., usually the value of the secured property) by paying the present value of the collateral rather than the whole debt through the plan. This in a procedure that is referred to as a "cramdown" because the terms of the repayment are forced on the creditor, or crammed down its throat.

Since the creditor will only be receiving full payment over the time that the debtor pays the claim, which is usually over the span of the plan, the creditor is entitled to an interest rate on the value of the allowed secured claim. In essence, the present value of the debtor's payments must equal the value of the collateral, which means that the payments must be discounted by an interest rate that will be equal to the allowed secured claim.

Section 1325(a) of the Bankruptcy Code sets forth the requirements for confirmation of a chapter 13 plan.[8] Unless a secured creditor consents to different treatment, where the debtor retains the property securing the claim, the plan must provide that (a) a creditor of an allowed secured claim retains the lien securing the claim until the claim is paid in full or discharged, § 1325(a)(5)(B)(i)(I); (b) "the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim," § 1325(a)(5)(B)(ii); and (c) the creditor must receive periodic payments in equal monthly amounts, § 1325(a)(5)(B)(iii)(I). With only a few exceptions, § 506(a) applies and provides, in

[8] Section 1325 provides in part:

> (a) Except as provided in subsection (b), the court shall confirm a plan if—
> . . .
> (5) with respect to each allowed secured claim provided for by the plan—
> (A) the holder of such claim has accepted the plan;
> (B) (i) the plan provides that—
> (I) the holder of such claim retain the lien securing such claim until the earlier of—
> (aa) the payment of the underlying debt determined under nonbankruptcy law; or
> (bb) discharge under section 1328; and
> (II) if the case under this chapter is dismissed or converted without completion of the plan, such lien shall also be retained by such holder to the extent recognized by applicable nonbankruptcy law;
> (ii) the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim; and
> (iii) if—
> (I) property to be distributed pursuant to this subsection is in the form of periodic payments, such payments shall be in equal monthly amounts; and
> (II) the holder of the claim is secured by personal property, the amount of such payments shall not be less than an amount sufficient to provide to the holder of such claim adequate protection during the period of the plan; or
> (C) the debtor surrenders the property securing such claim to such holder;

11 U.S.C. § 1325(a)(5) (emphasis added).

pertinent part, that "an allowed claim of a creditor secured by a lien on property . . . is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property . . . and is an unsecured claim to the extent that the value of such creditor's interest . . . is less than the amount of such allowed claim." § 506(a)(1).

Where a chapter 13 debtor retains property subject to a secured claim, the creditor retains a lien securing the claim, and the debtor must compensate the creditor with installment payments throughout the plan. The amount of each installment must be calibrated to ensure that, over time, the creditor receives disbursements whose total present value equals or exceeds that of the allowed claim. Thus, although not expressly stated in the Code, § 1325(a)(5)(B)(ii) suggests that the debtor must pay interest on a secured claim that is paid in installments. The Bankruptcy Code, however, does not provide guidance on how to determine this interest rate.

In *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004), a pre-BAPCPA case, the Supreme Court addressed the appropriate method for determining the interest rate on the secured portion of a claim that was bifurcated under § 506. There, the debtor's chapter 13 plan proposed a 9.5% interest rate on the secured portion of the claim, calculated using a "formula rate." However, the creditor argued that the 21% contract rate should apply. *Id.* at 470–71. After considering four different methods used by lower courts for determining the proper interest rate, a plurality of the Court decided that the formula approach is the appropriate method for calculating interest on the secured portion of a loan. *Id.* at 479–80. The *Till* Court defined the formula approach as the national prime rate plus an additional risk adjustment rate, which accounts for the debtor's risk of nonpayment. *Id.* at 479. The national prime rate "reflects the financial market's estimate of the amount a commercial bank should charge a creditworthy commercial borrower." *Id.* The risk adjustment rate reflects that bankrupt debtors typically pose a greater risk of defaulting than commercial debtors. *Id.* In selecting the formula approach, the Court reasoned that § 1325(a)(5)(B) does not require a court to use the rate provided in the original loan, nor consider the creditor's individual circumstances, prior dealings with the debtor, or alternative loans if permitted to foreclose. *Id.* at 476–77. The Court concluded that § 1325(a)(5)(B) only requires that the distributions under the claim equal the present value of the secured claim. *Id.* at 474. The *Till* Court did not define how to compute the risk adjustment, but provided some guidance in noting that § 1325 "obligates the court to select a rate high enough to compensate the creditor for its risk but not so high as to doom the plan." 541 U.S. at 480.

With *Till* as guidance, courts have used different methods to calculate the appropriate interest rate. The formula method (aka prime plus) uses the current prime rate plus a certain amount; courts generally add 1% to 3%, but allow the creditor to prove that a higher percentage is more appropriate. Since the prime rate already compensates for opportunity cost and for inflation according to the market's view of those factors, the additional percentage is added to compensate the creditor for the greater risk of default by the debtor, since the prime rate is only available to the most creditworthy corporations. Other methods include the presumptive contract rate method which uses the interest rate specified in the original contract, the coerced loan method which considers what the creditor could earn if it were allowed to immediately foreclose on the property and then invest the proceeds by lending the proceeds out with the same risk and duration as the cramdown payments, and the cost of funds method which considers what it would cost the creditor to borrow the amount of money equal to its allowed secured claim.

Where In The Code Does It Say:	Statute(s)
Whether interest must be paid on arrearage claims?	**11 U.S.C. §1322(e).**

If a loan contract has been entered into after October 22, 1994, and the plan proposes to cure defaults and maintain payments on the claim,[9] state law and the terms of the agreement control whether the creditor is entitled to interest on arrearages (as well as costs, fees, and other charges). Where in the Code does it say that?

Title 11 U.S.C. § 506(b) authorizes interest on oversecured claims, and any reasonable fees, costs or charges provided for by the agreement or state law.[10] In *United States v. Ron Pair Enterprises, Inc.*, 489 U.S. 235 (1989), the Supreme Court interpreted section 506 to provide for interest on oversecured claims, plus reasonable fees, costs and charges if provided for in the agreement or applicable state law.[11]

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[9] 11 U.S.C. § 1322(b)(5) provides that a plan may:

> **(5)** notwithstanding paragraph (2) of this subsection, 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;

11 U.S.C. § 1322(b)(5). As discussed elsewhere in these materials, paragraph (2) of section 1322(b) says that a plan may "modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence. . . ." 11 U.S.C. § 1322(b)(2).

[10] 11 U.S.C. § 506(b) provides:

> (b) To the extent that an allowed secured claim is secured by property the value of which, after any recovery under subsection (c) of this section, is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement or State statute under which such claim arose.

11 U.S.C. § 506(b). Interest is also required on secured claims provided for under 11 U.S.C. § 1325(a)(5), which is addressed elsewhere in these materials.

[11] In *Ron Pair Enterprises*, the Supreme Court explained:

> The relevant phrase in § 506(b) is "[T]here shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement under which such claim arose." "Such claim" refers to an oversecured claim. The natural reading of the phrase entitles the holder of an oversecured claim to postpetition interest and, in addition, gives one having a secured claim created pursuant to an agreement the right to reasonable fees, costs, and charges provided for in that agreement. Recovery of postpetition interest is unqualified. Recovery of fees, costs, and charges, however, is allowed only if they are reasonable and provided for in the agreement under which the claim arose. Therefore, in the absence of an agreement, postpetition interest is the only added recovery available.

Ron Pair Enterprises, 489 U.S. 235, at 241 (emphasis added).

In *Rake v. Wade*, 508 U.S. 464 (1993), the Supreme Court applied its ruling in *Ron Pair Enterprises* to oversecured mortgage claims and held that section 506(b) authorizes the payment of interest on the amounts necessary to cure defaults ("arrearages"), even if interest is not authorized by the agreement or applicable state law.

Thereafter, Congress enacted subsection (e) of section 1322, which now provides:

> (e) Notwithstanding subsection (b)(2) of this section and sections 506(b) and 1325(a)(5) of this title, if it is proposed in a plan to cure a default, the amount necessary to cure the default, shall be determined in accordance with the underlying agreement and applicable nonbankruptcy law.

11 U.S.C. § 1322(e) (emphasis added). The legislative history makes clear that 1322(e) was enacted to overrule *Rake v. Wade*. The statute was made applicable prospectively only, so it applies only to mortgages entered into after October 22, 1994.[12]

Pursuant to 11 U.S.C. § 1322(e), interest must be paid on arrearages only if required by the underlying agreement and authorized under applicable nonbankruptcy law.

Mortgage arrearage claims consist of missed payments, each of which comprises interest and (in most instances) principal. But arrearage claims might also include various fees (including attorneys' fees, late fees, etc.), costs, and numerous other charges. It is rare for state

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[12] Section 305 of HR 5116 amended 11 U.S.C. § 1322 by adding subsection (e). It also amended 11 U.S.C. §§ 1123 and 1222 in like fashion. The commentary included in the House Report accompanying the bill explained the purpose of the amendments as follows:

> Section 305. Interest on interest.
>
> This section will have the effect of overruling the decision of the Supreme Court in *Rake v. Wade*, 113 S.Ct. 2187 (1993). In that case, the Court held that the Bankruptcy Code required that interest be paid on mortgage arrearages paid by debtors curing defaults on their mortgages. Notwithstanding State law, this case has had the effect of providing a windfall to secured creditors at the expense of unsecured creditors by forcing debtors to pay the bulk of their income to satisfy the secured creditors' claims. This had the effect of giving secured creditors interest on interest payments, and interest on the late charges and other fees, even where applicable laws prohibits such interest and even when it was something that was not contemplated by either party in the original transaction. This provision will be applicable prospectively only, i.e., it will be applicable to all future contracts, including transactions that refinance existing contracts. It will limit the secured creditor to the benefit of the initial bargain with no court contrived windfall. It is the Committee's intention that a cure pursuant to a plan should operate to put the debtor in the same position as if the default had never occurred.

H.R. Rep. No. 103-835, Pub. L. 103-394 (1994) ("Bankruptcy Reform Act of 1994"). The law became effective on October 22, 1994.

laws (such as usury laws) as well as loan agreements to authorize the recovery of "interest on interest." Although the general rule since the enactment of section 1322(e) is that no interest is payable on arrearage claims, attorneys representing debtors and creditors need to review the note and mortgage documents as well as applicable state law to determine what other fees, costs, and charges are permissibly included in the arrearage claim,[13] whether those fees must be reasonable, and whether interest is allowed on any component of the arrearage claim.[14]

[13] *See Deutsche Bank National Trust Company v. Tucker*, 621 F.3d 460 (6th Cir. 2010) (arrearage claim of an undersecured mortgage creditor may include attorneys' fees which are authorized by the note and state law).

[14] *Compare In re Bumgarner*, 225 B.R. 327 (Bankr. D. S.C. 1998) (no interest on arrearages authorized); *In re Trabal*, 254 B.R. 99 (D. N.J. 2000) (interest on certain fees and charges included in the arrearage claim authorized); *In re Hence*, 225 Fed. Appx. 28 (5th Cir. 2007) (interest due on arrearages only after maturity date per the agreement); *In re Koster*, 294 B.R. 734 (Bankr. E.D. Mo. 2003) (agreement and state law permitted interest on the principal component of the arrearage claim as well as on attorney fees and advanced costs, but not on late fees and other additional charges); *In re Boyd*, 401 B.R. 137 (Bankr. D. N.J. 2008) (note authorized recovery of reasonable attorney's fees plus interest).

Where In The Code Does It Say:	**Statute(s)**
A chapter 13 plan must be "feasible" to be confirmed?	**11 U.S.C. § 1325(a)(6)**

The idea for including feasibility in this discussion came from the case of *In re Jones (Southeast Bank v. Jones)*, 105 B.R. 1007 (N.D. Ala. 1989), where the district judge, in reciting the facts of a case on appeal, said:

> Instead of granting the relief requested by Southeast Bank, the bankruptcy court, on the sudden and gratuitous motion of the Trustee, orally dismissed [the case]. . . . [T]he record reflects that the only ground for the requested dismissal stated by the Trustee was that the plan then was "not feasible" (whatever that meant) . . . .

In re Jones, 105 B.R. at 1009 (emphasis added). "Feasibility" is not a term used in the statutory requirements for confirmation of a chapter 13 plan, yet confirmation is denied frequently on the grounds that a plan is "not feasible."

So where in the Code does it say that a plan cannot be confirmed if it is "not feasible"?

Title 11 U.S.C. § 1325(a)(6) provides that a plan can be confirmed if, among other conditions, "(6) the debtor will be able to make all payments under the plan and to comply with the plan." 11 U.S.C. § 1325(a)(6). One aspect of the feasibility test is that the debtor must be able to afford to make plan payments.

> To satisfy feasibility, a debtor's plan must have a reasonable likelihood of success, i.e., that it is likely that the debtor will have the necessary resources to make all payments as directed by the plan. . . . Before confirmation, the bankruptcy court should be satisfied that the debtor has the present as well as the future financial capacity to comply with the terms of the plan.

In re Fantasia, 211 B.R. 420, 422-23 (1st Cir. BAP 1997) (citations omitted).

Feasibility under section 1325(a)(6) and eligibility to be a debtor in a chapter 13 case sometimes go hand in hand. *See, e.g., In re Crowder*, 179 B.R. 571, 574 (Bankr. E.D. Ark. 1995). Title 11 U.S.C. § 109(e) provides in pertinent part:

> (e) Only an individual with regular income . . . or an individual with regular income and such individual's spouse, except a stockbroker or a commodity broker, . . . may be a debtor under chapter 13 of this title.

11 U.S.C. § 109(e) (emphasis added). There is actually a definition in 11 U.S.C. § 101 of "individual with regular income."

> (30) The term "individual with regular income" means individual whose income is sufficiently stable and regular to enable such individual to make payments under a plan under chapter 13 of this title, other than a stockbroker or a commodity broker.

11 U.S.C. § 101(30).

A corollary to the rule that the debtor must be able to afford payments is that the payments the debtor proposes must be adequate to fund the plan to completion within the maximum time allowed by statute.

A plan may not provide for payments over a period that is longer than 5 years. 11 U.S.C. § 1322(d)(1), (d)(2). Within that time, the plan must provide for the full payment of (almost) all claims entitled to priority, 11 U.S.C. § 1322(a)(2);[15] secured claims being paid through the plan must be paid in full, 11 U.S.C. § 1325(a)(5); and unsecured creditors must receive: at least as much as what they would receive in a chapter 7 liquidation (11 U.S.C. § 1325(a)(4), the so-called "liquidation test" or "best-interest-of-creditors test," discussed elsewhere in these handouts), or the amount required by the disposable income test (11 U.S.C. § 1325(b)).

For example, if the debtor's proposed monthly plan payments will not pay a secured claim in full within the 5-year maximum duration of the plan, the plan is said to be not feasible. *See, e.g.*, *In re Shelly*, 458 B.R. 740 (Bankr. N.D. Ohio 2011). Therefore, the plan must be mathematically feasible, and the debtor must be able to make all payments under the plan and comply with the plan. 11 U.S.C. § 1325(a)(6).

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[15] Title 11 U.S.C. § 1322 provides in pertinent part:

> (a) The plan –
>
> . . .
>
> (2) shall provide for the full payment, in deferred cash payments, of all claims entitled to priority under section 507 of this title, unless the holder of a particular claim agrees to a different treatment of such claim;
>
> . . .
>
> (4) notwithstanding any other provision of this section, may provide for less than full payment of all amounts owed for a claim entitled to priority under section 507(a)(1)(B) only if the plan provides that all of the debtor's projected disposable income for a 5-year period beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

11 U.S.C. § 1322(a).

Where In The Code Does It Say:	Statute(s)
A plan must meet a "liquidation test" (aka "best interest of creditors" test) to be confirmed?	**11 U.S.C. § 1325(a)(4)**

Under chapter 7, a debtor liquidates his nonexempt assets to pay his unsecured creditors. Under chapter 13, the debtor gets to keep all of his property, but pays his creditors with his future income over a 3 or 5 year period. Section 1325(a)(4) requires that unsecured creditors receive at least the present value of what they would have received under a chapter 7 liquidation.16

Commonly known as the best-interests-of-creditors test or the liquidation test, this provision of the Code requires two separate calculations. First, the court must consider the value, as of the effective date of the proposed chapter 13 plan, of the property to be distributed to each unsecured creditor in chapter 13, taking into account the chapter 13 administrative expenses. Because the property to be distributed must have a certain value "as of the effective date of the plan," § 1325(a)(4), application of the liquidation test requires that creditors receive payments having a present value at least equal to what they would receive in a chapter 7 case which depends on the discount rate used. Next, the court must consider the amount that would be paid on each allowed unsecured claim if the debtor's estate were liquidated in a hypothetical chapter 7 case, taking into account the chapter 7 administrative expenses. In determining this amount, practitioners should keep in mind that under chapter 7, a trustee in bankruptcy would have the power to avoid fraudulent and preferential transfers, thereby increasing the assets in the estate and the overall payout to creditors. Where such avoidance actions would be successful in chapter 7, a chapter 13 debtor must propose a plan which would equal or exceed the payout to creditors under chapter 7, taking into account the value of the avoidance actions.

After the present value of the amount that is to be distributed under a chapter 13 plan is calculated and the amount that would be paid in chapter 7 is estimated, the two amounts must be compared. The chapter 13 plan will meet the best interests of creditors test if the distribution amount determined in the first, chapter 13, calculation is not less than the amount in the second, chapter 7, calculation. By contrast, if the present value of the amount to be distributed under the chapter 13 plan is less than the estimated amount that unsecured creditors would receive in a chapter 7 liquidation, the plan will not pass muster under § 1325(a)(4).

If, to satisfy the liquidation test, the debtor must pay 100% to unsecured creditors, how far can the debtor go in objecting to claims to lower his/her liability? Very likely objections filed

[16] Section 1325(a) provides: "Except as provided in subsection (b), the court shall confirm a plan if— (4) the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title on such date[.]"

without sound reason will implicate the good faith requirement for confirmation. *See In re Hill*, Case #13-50707, Doc. #59 (Memorandum Opinion and Order) (Bankr. E.D. Ky., February 28, 2014) (debtor's schedules can be used as admissions that debts are owed; proofs of claims satisfied Fed. R. Bankr. P. 3002(c)(3); "The Debtor's objections appear to be attempts to prevent legitimate claims from being paid, and to create costs and time consuming difficulties for creditors in having to prove their claims in ways not required by the Bankruptcy Rules." Opinion at p.9; objections overruled).

Where In The Code Does It Say:	**Statute(s)**
Debtors may recover a car that was repossessed prepetition, and a creditor's failure to turn over the car is a violation of the automatic stay?	**11 U.S.C. §§ 541 (dependent on applicable state law); 542(a); 363; 1303; 362(a)(3)**

One of the benefits of filing a chapter 13 case in most jurisdictions is that the debtor may recover a car needed to get to and from work that was repossessed prior to bankruptcy, provided the car has not yet been disposed of by the creditor. The debtor's right to recover the property is very much dependent upon applicable state law.

Title 11 U.S.C. § 541 ("Property of the estate") provides in pertinent part as follows:

> (a) The commencement of a case . . . creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:
>
> (1) . . . all legal or equitable interests of the debtor in property as of the commencement of the case.

11 U.S.C. § 541(a)(1).

Property interests are created and defined by state law. *Butner v. United States*, 440 U.S. 48, at 54-55 (1979). State law also defines a creditor's security interest. *Id*. However, when there is a direct conflict between state law and bankruptcy law, bankruptcy law controls. *Id*.

Title 11 U.S.C. § 542 provides in pertinent part as follows:

> (a) . . . [A]n entity, other than a custodian, in possession, custody, or control, during the case, of property that the trustee may use, sell, or lease under section 363 of this title, or that the debtor may exempt under section 522 of this title, shall deliver to the trustee, and account for, such property or the value of such property, unless such property is of inconsequential value or benefit to the estate.

11 U.S.C. § 542(a) (emphasis added). Property of the debtor repossessed by a secured creditor falls under section 542 and may be drawn into the estate even though the debtor does not have a possessory interest in the property at the time of the commencement of the bankruptcy case. *United States v. Whiting Pools, Inc.*, 462 U.S. 198, at 205-07 (1983).

"In effect, § 542(a) grants to the estate a possessory interest in certain property of the debtor that was not held by the debtor at the commencement of the reorganization proceedings." *Id.* Although *Whiting Pools* was a chapter 11 case, it has been held to be applicable in chapter

13 cases. *See, e.g.*, *In re Sharon (TranSouth Financial Corp. v. Sharon)*, 234 B.R. 676 (6th Cir. BAP 1999).[17]

Section 542 makes reference to "the trustee." In a chapter 13 case, section 1303 gives the debtor the sole right to use, sell, or lease property of the estate under section 363.[18]

Substituting "chapter 13 debtor" for "trustee", section 363 as applicable in a chapter 13 case would read:

> (b)(1) The [~~trustee~~ chapter 13 debtor], after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate . . . .
> . . .
> (e) Notwithstanding any other provision of this section, at any time, on request of an entity that has an interest in property used, sold, or leased, or proposed to be used, sold, or leased, by the [~~trustee~~ chapter 13 debtor], the court, with or without a hearing, shall prohibit or condition such use, sale, or lease as is necessary to provide <u>adequate protection</u> of such interest. . . .

11 U.S.C. § 363 (emphasis and bracketed materials added).[19] Our focus is on property that the debtor intends to use during the chapter 13 case.

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[17] *But see In re Barringer*, 244 B.R. 402 (Bankr. E.D. Mich. 1999) (declining to follow the 6th Circuit BAP's opinion in *Sharon*).

[18] Title 11 U.S.C. § 1303 ("Rights and powers of debtor") provides:

> Subject to any limitations on a trustee under this chapter, the debtor shall have, exclusive of the trustee, the rights and powers of a trustee under sections 363(b), 363(d), 363(e), 363(f), and 363(l), of this title.

11 U.S.C. § 1303.

[19] Section 361 describes "adequate protection" as follows:

> When adequate protection is required under section 362, 363, or 364 of this title of an interest of an entity in property, such adequate protection may be provided by--
>
> (1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that the stay under section 362 of this title, use, sale, or lease under section 363 of this title, or any grant of a lien under section 364 of this title results in a decrease in the value of such entity's interest in such property;
>
> (2) providing to such entity an additional or replacement lien to the extent that such stay, use, sale, lease, or grant results in a decrease in the value of such entity's interest in such property; or
>
> (3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property.

11 U.S.C. § 361. Requiring the debtor to maintain full coverage insurance on the vehicle is a grant of adequate protection to the creditor.

A creditor with a security interest in property the debtor has the right to use must rely on the Bankruptcy Code's adequate protection provisions rather than the nonbankruptcy remedy of possession to protect its interest in the property. *United States v. Whiting Pools, Inc.*, 462 U.S. 198, 204 (1983).

In most jurisdictions, under section 9-623 of the UCC, a debtor may redeem collateral up until the time the creditor has disposed of the collateral. If under state law the debtor no longer has any rights in the collateral (e.g., the creditor has already sold the car, or if under state law the mere act of repossession constitutes a transfer of ownership to the creditor), the debtor may not recover the car. *See, e.g.*, *In re Curry (Tidewater Finance Co. v. Curry)*, 347 B.R. 596 (6th Cir. BAP 2006) (discussing rulings of the 11th Circuit that reached different conclusions depending on applicable state law).

If the debtor has the right to seek a return of the repossessed vehicle, the majority rule is that the creditor must immediately return possession to the debtor, then seek adequate protection. *See, e.g.*, *Thompson v. General Motors Acceptance Corp.*, 566 F.3d 699 (7th Cir. 2009).[20] The mere act of retaining the car is a violation of the automatic stay.

Title 11 U.S.C. § 362, the automatic stay, prohibits a creditor from taking any action "to exercise control over property of the estate."[21] "Holding onto an asset, refusing to return it, and otherwise prohibiting a debtor's beneficial use of an asset all fit within this definition [of "exercising control"]. *Id*. at 702.

The creditor may seek a termination or modification of the automatic stay on the grounds that its interest is not adequately protected, 11 U.S.C. § 362(d)(1); or that the debtor has no equity in the property and it is not necessary for an effective reorganization. 11 U.S.C. § 362(d)(2). [22] Usually a car needed for transportation to and from work is considered necessary to

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[20] *But see* the dissenting opinion in *In re Sharon (TranSouth Financial Corp. v. Sharon)*, 234 B.R. 676, 688-90 (6th Cir. BAP 1999) (Stosberg, J. dissenting).

[21] Section 362 provides in pertinent 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;

11 U.S.C. § 362(a)(3) (emphasis added).

[22] Title 11 U.S.C. § 362(d) provides in pertinent part:

> (d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay--
>
> (1) for cause, including the lack of adequate protection of an interest in property of such party in interest; [or]
>
> (2) with respect to a stay of an act against property under subsection (a) of this section, if--

a chapter 13 debtor's effective reorganization, leaving the creditor only with the argument that its interest is not adequately protected. At a minimum, the debtor will likely be required to show proof of full-coverage insurance as a form of adequate protection. In some jurisdictions, the creditor is not required to give the car back to the debtor unless and until the debtor shows proof of insurance.

Once the debtor recovers the vehicle, the plan may modify the claim pursuant to 11 U.S.C. § 1322(b)(2), although the claim may not be "crammed down" to the value if it is a so-called "910-claim" (discussed elsewhere in these materials). The analysis becomes much more complicated if the creditor's lien was not timely perfected or is otherwise avoidable by the trustee. That issue is beyond the scope of these materials, but practitioners should be aware of the potential issues.

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization.

. . . .

11 U.S.C. § 362(d)(1) and (d)(2).

Where In The Code Does It Say:	**Statute(s)**
Debtors' attorneys may be compensated through the plan for services rendered prepetition?	**11 U.S.C. § 330(a)(4)(B)**

Attorneys representing debtors in chapter 7 cases generally need to be paid in full prior to the filing of the petition for services they render in connection with the bankruptcy case since they cannot be paid from the estate for those services. *Lamie v. U.S. Trustee*, 540 U.S. 526, 124 S.Ct. 1023 (2004). If not, the debt owed to the attorney is a dischargeable debt. *Rittenhouse v. Eisen*, 404 F.3d. 395 (6th Cir. 2005).

Attorneys representing debtors-in-possession in chapter 11 cases must not hold an interest adverse to the estate and must be disinterested. 11 U.S.C. § 327(a). An attorney who is owed fees for services rendered prepetition has a claim against the debtor as of the petition date. Therefore, the attorney is a creditor and is not disinterested. 11 U.S.C. § 101(14). Often the solution is for the attorney to waive its claim for the prepetition fee owed. *See, e.g.*,, C.R. "Chip" Bowles, *Getting Paid: Retention and Compensation in Bankruptcy Cases*," American Bankruptcy Institute (2012).

Attorneys representing debtors in chapter 13 cases are lucky – they can get paid from property of the estate for fees earned in rendering services prepetition as well as for fees earned postpetition during the case – an advantage to filing a chapter 13 for eligible consumers.

Where in the Code does it say that? First, an attorney representing a debtor in chapter 13 is not a "professional person" whose employment is subject to the disinterestedness standard of 11 U.S.C. § 327(a). Section 327(a) applies to the employment of professional persons by the trustee. Although the chapter 13 debtor has some of the rights and duties of the trustee,[23] the trustee in chapter 13 cases is a separate entity from the debtor, 11 U.S.C. § 1302, and section 327(a) is just not applicable to attorneys employed by debtors in connection with chapter 13 cases.

Second, 11 U.S.C. § 330 authorizes compensation to attorneys representing debtors in chapter 13 cases. *See In re Busetta-Silvia*, 314 B.R. 218 (10th Cir. BAP 2004). Section 330(a)(4)(B) provides:

> (B) In a chapter 12 or chapter 13 case in which the debtor is an individual, the court may allow reasonable compensation to the debtor's attorney for representing the interests of the debtor in connection with the bankruptcy

[23] "[T]he debtor shall have, exclusive of the trustee, the rights and powers of a trustee under sections 363(b), 363(d), 363(e), 363(f), and 363(l) of this title." 11 U.S.C. § 1303. By negative implication, the debtor does not have the rights and powers of the trustee under 11 U.S.C. § 327. Debtors may also have certain avoidance powers they may exercise with regard to exempt property. See 11 U.S.C. §§ 522(g), 522(h), and 522(i).

> case based on a consideration of the benefit and necessity of such services to the debtor and the other factors set forth in this section.

11 U.S.C. § 330(a)(4)(B). The "other factors" in section 330 that the court must consider presumably are as follows:

> (A) the time spent on such services;
> (B) the rates charged for such services;
> (C) whether such services were necessary to the administration of, or beneficial at the time at which the service was rendered toward the completion of, a case under this title;
> (D) whether the services were performed within a reasonable amount of time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed;
> (E) with respect to a professional person, whether the person is board certified or otherwise has demonstrated skill and experience in the bankruptcy field; and
> (F) whether the compensation is reasonable based on the customary compensation charged by comparably skilled practitioners in cases other than cases under this title.

11 U.S.C. § 330(a)(3).

There are times when a person needs immediate bankruptcy relief but is unable to file a chapter 7 case because s/he cannot afford to pay the attorney in full. Can the debtor file a chapter 13 case solely to finance the payment of attorneys' fees? Some trustees and courts find it objectionable on the grounds that the chapter 13 plan has not been proposed in good faith, 11 U.S.C. § 1325(a)(3), the action of the debtor in filing the petition was not in good faith, 11 U.S.C. § 1325(a)(7), and/or that the debtor will not be able to make all payments under the plan and comply with the plan, 11 U.S.C. § 1325(a)(6). *Compare In re Puffer (Berliner v. Pappalardo)*, 675 F.3d 78 (1st Cir. 2012) ("fee only" plans are not per se filed in bad faith); *with In re Brown (Brown v. Gore)*, 742 F.3d 1309 (11th Cir. 2014) (bankruptcy court's finding that a "fee-only" case was not proposed in good faith was not clearly erroneous).

Rather than challenging the debtor's good faith, a better option would seem to be to consider the reasonableness of the compensation the debtor's attorney is seeking in a chapter 13 case that is merely a chapter 7 case filed to collect attorneys' fees. If the compensation paid or agreed to be paid exceeds the reasonable value of the services rendered or to be rendered in contemplation of or in connection with the bankruptcy case, the court may cancel the agreement, or order the return of any payment, to the extent excessive, to the estate or to the debtor. See 11 U.S.C. § 329(b).

Where In The Code Does It Say:	**Statute(s)**
Debtors can request a "hardship discharge"?	**11 U.S.C. § 1328(b)**

Search the Bankruptcy Code for "hardship discharge" and the results will be nil. When asking for a hardship discharge, the debtor is actually seeking a discharge under 11 U.S.C. § 1328(b), which provides:

> (b) Subject to subsection (d), at any time after the confirmation of the plan and after notice and a hearing, the court may grant a discharge to a debtor that has not completed payments under the plan only if—
>
> (1) the debtor's failure to complete such payments is due to circumstances for which the debtor should not justly be held accountable;
>
> (2) the value, as of the effective date of the plan, of property actually distributed under the plan on account of each allowed unsecured claim is not less than the amount that would have been paid on such claim if the estate of the debtor had been liquidated under chapter 7 of this title on such date; and
>
> (3) modification of the plan under section 1329 of this title is not practicable.

11 U.S.C. § 1328(b). It is not sufficient to merely state in the motion that the debtor can no longer afford to make plan payments. The debtor must show: that the inability to make payments is due to circumstances for which s/he should not be justly held accountable; that unsecured creditors have already received at least as much as they would have received in a chapter 7 liquidation test; and that modification of the plan is not practicable.

A "hardship discharge" is not as broad as a discharge in which the debtor has completed payments under the plan. As discussed elsewhere in these materials, a hardship discharge does not discharge any debts listed under 11 U.S.C. § 523(a), whereas some of those debts are discharged if the debtor completes plan payments.

Where In The Code Does It Say:	Statute(s)
Debtors can discharge divorce-related property settlement claims (unless they get a "hardship discharge")?	**11 U.S.C. § 1328(a)(2) (by negative implication); § 1328(b); § 523(a)**

In a chapter 13 bankruptcy, a debtor can discharge most debts after s/he completes bankruptcy plan payments (provided certain other conditions are met and s/he is not barred from receiving a discharge by reason of having had a prior discharge within certain time limits, see 11 U.S.C. § 1328(f)), but among the debts that cannot be discharged are domestic support obligations. Some practitioners will recall that under pre-BAPCPA law there was a distinction between property settlements (dischargeable under certain circumstances) and debts for support payments (non-dischargeable). This has not changed for chapter 13 debtors.

Generally speaking, the Bankruptcy Code provides that debts are not dischargeable if they are "for a domestic support obligation," § 523(a)(5), or if they are owed "to a . . . former spouse . . . of the debtor and not of the kind described in paragraph (5) that is incurred by the debtor . . . in connection with a . . . divorce decree." § 523(a)(15).[24] "Domestic support obligation" is a defined term meaning a debt owed to a former spouse that is "in the nature of alimony, maintenance or support" of the former spouse "without regard to whether such debt is expressly so designated." § 101(14A)(B). So § 523(a) provides that alimony, maintenance, and support debts ("DSOs") and spousal debts other than DSOs (such as property settlements) are non-dischargeable. However, spousal divorce obligations other than DSOs are dischargeable in chapter 13 cases because § 1328(a)(2) incorporates § 523(a)(5), but not § 523(a)(15). A reading of the statute illustrates this point. Section 1328(a) provides:

> Subject to subsection (d), as soon as practicable after completion by the debtor of all payments under the plan, and in the case of a debtor who is required by a judicial or administrative order, or by statute, to pay a domestic support obligation, after such debtor certifies that all amounts payable under such order or such statute that are due on or before the date

[24] Section § 523(a) provides in part:

> (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—
>
> (5) for a domestic support obligation;
>
> . . .
>
> (15) to a spouse, former spouse, or child of the debtor and not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, or a determination made in accordance with State or territorial law by a governmental unit;

11 U.S.C. § 523(a)(5), (a) (15).

> of the certification (including amounts due before the petition was filed, but only to the extent provided for by the plan) have been paid, unless the court approves a written waiver of discharge executed by the debtor after the order for relief under this chapter, the court shall grant the debtor a discharge of all debts provided for by the plan or disallowed under section 502 of this title, except any debt—
>
> . . .
>
> (2) of the kind specified in section 507(a)(8)(C) or in paragraph (1)(B), (1)(C), (2), (3), (4), (5), (8), or (9) of section 523 (a);

11 U.S.C. § 1328(a) (emphasis added). Overwhelming case law supports this statutory construction. *See, e.g., Benson v. Benson (In re Benson),* No. 11-12284, 2011 WL 4435560, *1 (11th Cir. Sept. 26, 2011) (recognizing that "[i]n a Chapter 13 bankruptcy, a debtor can discharge most of his debts after he completes his bankruptcy plan payments[,] [b]ut among the debts that cannot be discharged are domestic support obligations."). In a chapter 13 case, a former spouse and creditor of the debtor will likely want to litigate the issue of whether the debt is characterized as one under § 523(a)(15) (dischargeable) or under § 523(a)(5) (non-dischargeable).

In determining whether a debt is actually in the nature of alimony or support, a court will look beyond the label the parties have given to a particular debt. *Cummings v. Cummings*, 244 F.3d 1263, 1265 (11th Cir. 2001). A debt is a domestic support obligation if the parties intended it to function as support or alimony, even if they called it something else. The court's decision should also be informed by state law. But there are other factors a court should consider as well. They include: (1) the agreement's language; (2) the parties' financial positions when the agreement was made; (3) the amount of the division; (4) whether the obligation ends upon death or remarriage of the beneficiary; (5) the frequency and number of payments; (6) whether the agreement waives other support rights; (7) whether the obligation can be modified or enforced in state court; and finally (8) how the obligation is treated for tax purposes.

A discharge of § 523(a)(15) property settlement debts is possible under 11 U.S.C. § 1328(a) only if the debtor completes payments under the plan (and satisfies other conditions). A debtor has another option for a discharge in chapter 13: what is commonly referred to as a "hardship discharge" pursuant to 11 U.S.C. § 1328(b).[25] A § 523(a)(15) property settlement

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[25] Section 1328(b) provides:

> **(b) [A]**t any time after the confirmation of the plan and after notice and a hearing, the court may grant a discharge to a debtor that has not completed payments under the plan only if—
>
> **(1)** the debtor's failure to complete such payments is due to circumstances for which the debtor should not justly be held accountable;
>
> **(2)** the value, as of the effective date of the plan, of property actually distributed under the plan on account of each allowed unsecured claim is not less than the amount that would have been paid on such claim if the estate of the debtor had been liquidated under chapter 7 of this title on such date; and
>
> **(3)** modification of the plan under section 1229 of this title is not practicable.

11 U.S.C. § 1328(b).

agreement is not dischargeable by a so-called "hardship discharge" under § 1328(b). In fact, all § 523(a) debts are nondischargeable if the debtor gets a § 1328(b) hardship discharge. Section 1328(c) provides as follows:

> **(c)** A discharge granted under subsection (b) of this section discharges the debtor from all unsecured debts provided for by the plan or disallowed under section 502 of this title, except any debt—
>
> **(1)** provided for under section 1322(b)(5) of this title; or
>
> **(2)** of a kind specified in section 523(a) of this title.

11 U.S.C. § 1328(c). This is consistent with the opening sentence of § 523(a) which says "A discharge under section . . . 1328(b) of this title does not discharge an individual debtor from any debt. . ." enumerated in § 523(a).

Where In The Code Does It Say:	Statute(s)
Debtors can discharge § 523(a)(6) debts for "willful and malicious injury by the debtor to another entity or to the property of another entity" (unless they get a "hardship discharge")?	**11 U.S.C. § 1328(a)(2) (by negative implication); § 1328(b); § 523(a)**

Section 1328(a) provides:

> Subject to subsection (d), as soon as practicable after completion by the debtor of all payments under the plan, . . . , the court shall grant the debtor a discharge of all debts provided for by the plan or disallowed under section 502 of this title, except any debt—
>
> . . .
>
> (2) of the kind specified in section 507(a)(8)(C) or in paragraph (1)(B), (1)(C), (2), (3), (4), (5), (8), or (9) of section 523(a);

11 U.S.C. § 1328(a)(2) (emphasis added). Paragraph (6) of section 523(a) is absent from the list of debts excepted from discharge in a chapter 13 case in which the debtor completes payments under the plan. It is paragraph (6) of section 523(a) which excepts debts for "willful and malicious injury by the debtor to another entity or to the property of another entity."

Attorneys who are accustomed to dealing with nondischargeability actions are aware of the time deadlines for filing certain adversary complaints. Section 523(c) affirmatively discharges section 523(a)(2), (4), or (6) debts unless on request of a creditor and after notice and hearing the court determines the debt is nondischargeable. 11 U.S.C. § 523(c). Rule 4007 of the Federal Rules of Bankruptcy Procedure provides in part:

> (c) Time for Filing Complaint Under § 523(c) in a Chapter 7. . . ., or Chapter 13 . . . . Except as otherwise provided in subdivision (d), a complaint to determine the dischargeability of a debt under § 523(c) shall be filed no later than 60 days after the first date set for the meeting of creditors under § 341(a). . . .
>
> (d) Time for Filing Complaint Under § 523(a)(6) in a Chapter 13 Individual's Debt Adjustment Case. . . . On motion by a debtor for a discharge under § 1328(b), the court shall enter an order fixing the time to file a complaint to determine the dischargeability of any debt under § 523(a)(6). . . .

Fed. R. Bankr. P. 4007 (emphasis added). Consequently, the 60-day deadline for filing dischargeability complaints under § 523(a)(6) does not apply in chapter 13 cases UNLESS AND UNTIL the debtor files a motion for discharge under § 1328(b) (the "hardship discharge" section).

In contrast to section 523(a)(6) willful and malicious injury debts, a chapter 13 discharge in which the debtor completes plan payments does not discharge debts:

> (4) for restitution, or damages, awarded in a civil action against the debtor as a result of willful or malicious injury by the debtor that caused personal injury to an individual or the death of an individual.

11 U.S.C. § 1328(a)(4).

Rule 4007, which sets forth the deadlines for objecting to the dischargeability of debts under section 523, does not mention any deadline for filing a complaint to determine the dischargeability of a debt under section 1328(a)(4).

Section 523(a)(6) debts are not dischargeable by a so-called "hardship discharge" under § 1328(b). In fact, all § 523(a) debts are nondischargeable if the debtor gets a § 1328(b) hardship discharge. Section 1328(c) provides as follows:

> **(c)** A discharge granted under subsection (b) of this section discharges the debtor from all unsecured debts provided for by the plan or disallowed under section 502 of this title, except any debt—
>
> **(1)** provided for under section 1322(b)(5) of this title; or
>
> **(2)** of a kind specified in section 523(a) of this title.

11 U.S.C. § 1328(c). This is consistent with the opening sentence of § 523(a) which says "A discharge under section . . . 1328(b) of this title does not discharge an individual debtor from any debt. . ." enumerated in § 523(a). And as noted above, when the debtor files a motion requesting a hardship discharge, the court enters an order setting the deadline for filing complaints to determine the dischargeability of debts under § 523(a)(6) as required by § 523(c). See Fed.R. Bankr. P. 4007(d).

Where In The Code Does It Say:	Statute(s)
Who gets money the chapter 13 trustee has on hand when a case converts to chapter 7 after confirmation?	**11 U.S.C. § 348; § 1326**

It's a common scenario: the debtor makes plan payments, but before the trustee can disburse all funds (for various reasons), the debtor converts the case to chapter 7.[26] To whom should the chapter 13 trustee send the funds on hand: to the chapter 7 trustee? To creditors pursuant to the terms of the confirmed plan? Or back to the debtor?

The chapter 7 trustee's interest in the funds is limited after 11 U.S.C. § 348 was amended in 1994 to provide in part:

> (f)
> (1) Except as provided in paragraph (2), when a case under chapter 13 of this title is converted to a case under another chapter of this title –
> (A) property of the estate in the converted case shall consist of property of the estate, as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion;
> . . . .
> (2) If the debtor converts a case under chapter 13 of this title to a case under another chapter under this title in bad faith, the property of the estate in the converted case shall consist of the property of the estate as of the date of conversion.

11 U.S.C. § 348(f). Assuming the funds being held by the chapter 13 trustee were derived from the debtor's wages, the chapter 7 trustee has no interest in the funds, unless the debtor converted the case in bad faith.

That leaves us with two options: disburse the funds to the creditors under the terms of the confirmed plan, or give the funds back to the debtor. The answer is in the hands of the Supreme Court in the case of *Viegelahn v. Harris (In re Harris)*, 757 F.3d 468 (5th Cir. 2014), *cert. granted* 135 S.Ct. 782, No. 14-400, December 12, 2014. In *Harris*, the Fifth Circuit Court of Appeals held that the chapter 13 trustee was obligated to disburse the funds on hand to creditors. In contrast, the Third Circuit Court of Appeals had earlier ruled that funds held by a chapter 13 trustee at the time of conversion must be returned to the debtor. *In re Michael*, 699 F.3d 305 (3d Cir. 2012). The Supreme Court recently heard oral argument in the *Harris* case, and a decision is expected before the end of this term.

[26] 11 U.S.C. § 1307(a) provides: "The debtor may convert a case under this chapter to a case under chapter 7 of this title at any time. Any waiver of the right to convert under this subsection is unenforceable."

The Bankruptcy Code does not provide a clear answer. On the one hand, the chapter 13 trustee has at least an inherent, if not a statutory, duty to distribute funds received from the debtor to creditors pursuant to the terms of a confirmed plan. Section 1326 provides in part:

> (2) A payment made under paragraph (1)(A)[27] shall be retained by the trustee until confirmation or denial of confirmation. If a plan is confirmed, the trustee shall distribute any such payment in accordance with the plan as soon as is practicable. If a plan is not confirmed, the trustee shall return any such payments not previously paid and not yet due and owing to creditors pursuant to paragraph (3) to the debtor, after deducting any unpaid claim allowed under section 503(b).

11 U.S.C. § 1326(a)(2). Courts disagree whether section 1326 even applies to payments made by the debtor after confirmation, and they disagree as to whether section 1326 vests in creditors a right to receive distributions of funds the debtor pays into the plan following confirmation. *See Harris v. Viegelahn*, 757 F.3d at 475-76.

On the other hand, section 348(e) provides:

> (e) Conversion of a case under section 706, 1112, 1208, or 1307 of this title terminates the service of any trustee or examiner that is serving in the case before such conversion.

11 U.S.C. § 348(e). The debtor in the *Harris* case argued that section 348(e) cut off the chapter 13 trustee's authorization to make further disbursements to creditors. However, taken literally, if the conversion to chapter 7 immediately terminates the service of the chapter 13 trustee, the chapter 13 trustee is unable to disburse funds on hand to anyone – whether to the debtor or to creditors.

In Kentucky, courts have held that post-petition wages paid to the chapter 13 trustee before conversion must be distributed to creditors pursuant to the confirmed plan even after conversion of the case to one under chapter 7, *In re Galloway*, 134 B.R. 602 (Bankr. W.D.Ky.1991); *In re Hardin*, 200 B.R. 312 (Bankr. E.D.Ky.1996), and that has been the practice of the respective trustees in both the Eastern and Western Districts.

The Supreme Court's decision is expected soon.

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[27] Section 1326(a)(1) provides in part:

> (a) (1) Unless the court orders otherwise, the debtor shall commence making payments not later than 30 days after the date of the filing of the plan or the order for relief, whichever is earlier, in the amount—
>
> (A) proposed by the plan to the trustee;
>
> . . . .

11 U.S.C. § 1326(a)(1).

Where In The Code Does It Say:	**Statute(s)**
The court may enter a "drop-dead" order?	**11 U.S.C. § 362(d); § 105(a)**

Entry of what is commonly called a "drop-dead" order is not unusual in resolving a creditor's motion for relief from the automatic stay. Section 362 provides in part:

> (d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay [for reasons enumerated therein] . . . .

11 U.S.C. § 362(d) (emphasis added).

> Section 362 of the Bankruptcy Code gives the Court the authority to enter an order conditioning the stay for the future if the Court finds that relief from the stay should not be granted outright. Such orders can take many forms, but the most frequently used are those commonly referred to as "drop dead" orders. This Court prefers the term "future relief" order. Others use terms such as "doomsday," "strict compliance" or "prospective." Whatever they are called, the effect is the same. The orders condition the stay in such a way that if the debtor fails to make a future payment, the stay will be granted without further notice or order from the court.

In re Sharpe, 391 B.R. 117 (Bankr. N.D. Ala. 2008).

> Such conditional orders are commonly called, in this District, "drop dead orders." . . . [Debtor] refers to such provisions as "time bombs" in his complaint. While the Court does not wish to unduly quibble as to matters of nonstandard terminology, neither of the terms "time bomb" or "drop dead" are contained in the Bankruptcy Code. However, the term "drop dead" is commonly used here while "time bomb" is not.

In re Avery, 2009 WL 190038 (Bankr. M.D. Ala. 2009).

> The "drop dead" terminology is unfortunate, as it implies harsher results to debtors than intended by the creditors or by the courts; therefore, this Court will refer to such an order as one of "last opportunity."

In re Friend, 191 B.R. 391 (Bankr. W.D. Tenn. 1996).

It is not necessary that the debtor agree to entry of a drop-dead order. A bankruptcy court's decision to enter an order conditioning the automatic stay will be upheld on appeal unless its order was clearly erroneous. *In re Mendoza*, 111 F.3d. 1264 (5th Cir. 1997).

Nor is the court required to enter such an order merely because it is requested by a creditor. *In re Lucier*, 2007 WL 4868323 (Bankr. D.N.D. 2007). And the court has the discretion to condition the stay by entering a drop-dead order instead of terminating the automatic stay as requested by the creditor. *In re Bivens*, 317 B.R. 755 (Bankr. N.D. Ill. 2005).

Drop-dead orders are not limited to conditioning the automatic stay (although the statutory authority for entering conditional orders on motions for relief from stay is clear). In the Eastern District of Kentucky, the court enters "probation orders" to debtors who have become delinquent in their plan payments. If, during the next year, the debtors become delinquent again, the trustee tenders a report of delinquent plan payments, and the court dismisses the case without further notice or hearing. A similar order was upheld by the District Court in the Eastern District of Texas in the case of *Ferrell v. Countryman*, 398 B.R. 857, 865 (E.D. Tex. 2009).

This is one instance where the court's equitable powers are needed to fashion remedies that are not necessarily provided in the Code.

> Because of the equitable nature of bankruptcy in seeking a balance between debtors and creditors, bankruptcy courts should be afforded the latitude to fashion remedies they consider appropriate under the circumstances, including "drop dead" orders, as long as the bankruptcy court follows the Bankruptcy Code's statutory mandate.

In re Mendoza, 111 F.3d. 1264, 1270 (5th Cir. 1997). Sometimes there are simply no other provisions in the Code but section 105, which provides in part:

> (a) The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. . . .

11 U.S.C. § 105(a). However, section 105 does not empower the bankruptcy court to override specific mandates or prohibitions of other sections of the Bankruptcy Code. *See Law v. Siegel*, 134 S.Ct. 1188 (2014).

Saturday July 4th

4:05-5:05 Conversion from Chapter 13 to Chapter 7 and Vice Versa: What Trustees Look For and Why Exemption Claims Make a Difference.

Moderator: Gregory A. Burrell, Chapter 13 Standing Trustee for the District of Minnesota (Minneapolis)

Melissa A. Herman, Herman & Russo, PC (Woodstock and Alpharetta, GA)

Jill D. Olsen, The Olsen Law Firm, LLC/Chapter 7 Panel Trustee (Kansas City, MO)

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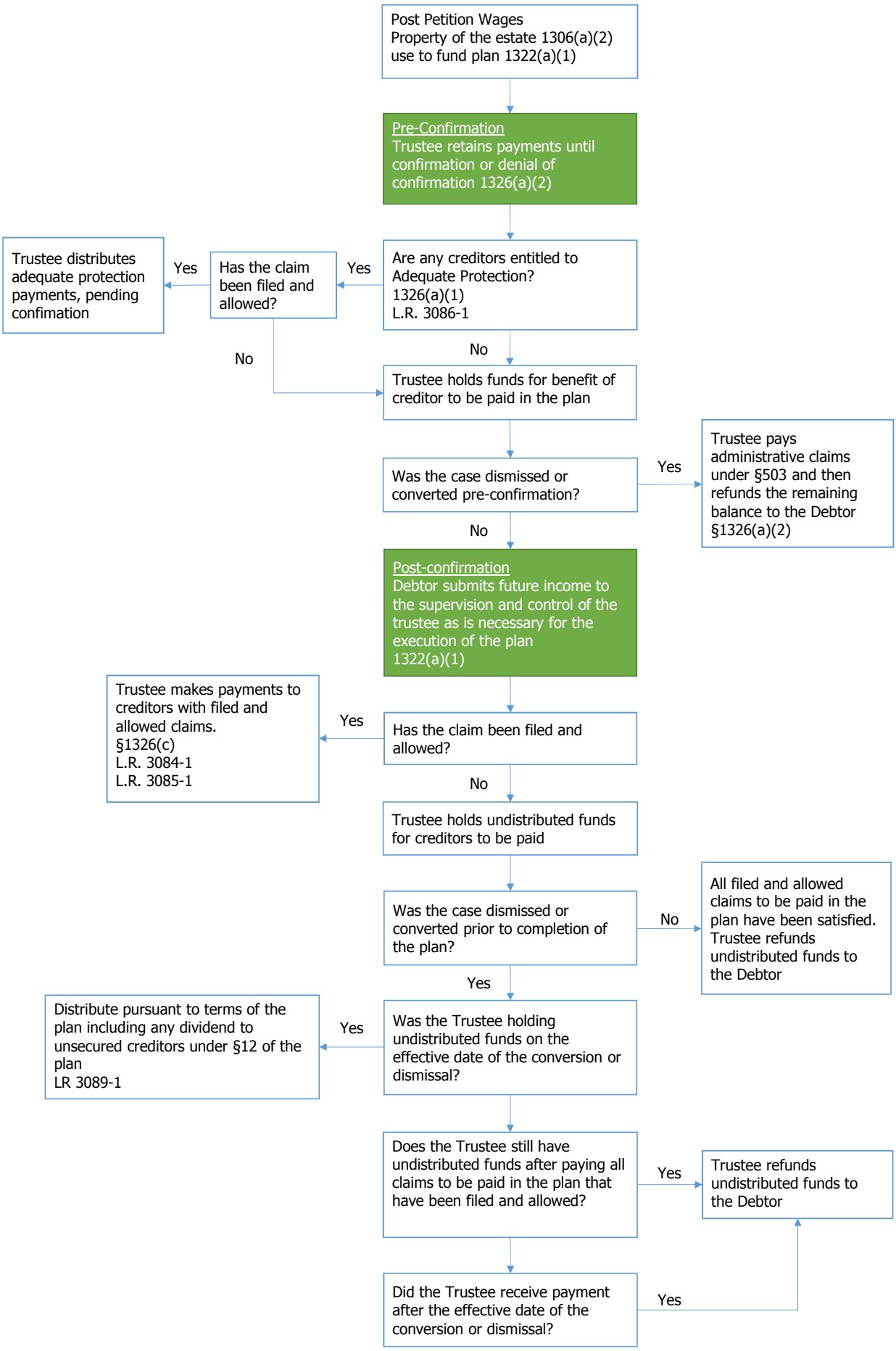
WESTERN DISTRICT OF MISSOURI - FEBRUARY 2015



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CONVERSION FROM CHAPTER 13 TO CHAPTER 7 AND VICE VERSA

What trustees look for and why exemption claims make a difference

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Moderator: Gregory Burrell
Ch. 13 Trustee, Minneapolis, MN

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Is there an absolute right to convert?

- 11 U.S. Code § 1307 (a) - Conversion
- The debtor may convert a case under this chapter to a case under chapter 7 of this title at any time.
- Any waiver of the right to convert under this subsection is unenforceable.

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- Need only file notice (Fed Rule Bk. Proc. 1017 (f)(3)
- Not a new case
- Existing case takes different route
- Chapter 13 Trustee's service terminates immediately
- Doesn't change filing date of petition
- Post-petition debts arising before conversion are treated as if they arose pre-petition

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- But see *Marrama v. Citizens Bank of Massachusetts*, SC 2007 WL 517340, 549 U.S. 365 (2007)

- Chapter 7 Debtor made misrepresentations in schedules
- Debtor moves to convert when Chapter 7 trustee states intent to administer
- Trustee and creditor allege bad faith and object to conversion
- Bankruptcy Judge agrees with Trustee
- BAP and SCOTUS affirm
- 11 U.S.C. 706 (a) and (d)

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- 11 U.S.C. 706 Conversion
- (a) The Debtor may convert a case under this chapter to a case under chapter 11, 12 ,or 13 of this title at any time, if the case has not been converted under section 1112, 1208, or 1307 of this title. Any waiver of a right to convert is unenforceable.
- (d) Notwithstanding any other provision of this section, a case may not be converted to a case under another chapter of this title unless the Debtor may be a Debtor under such chapter.
- Debtor who acted in bad faith in chapter 7 does not qualify as Debtor under chapter 13.

Which exemptions apply at conversion?

- Debtor's right to exemptions determined by facts as they existed on the date of original bankruptcy petition - *in re Brinkley,* 323 B.R. at 691

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Valuation of property upon conversion

- Is valuation at time of petition filing?

Debtor's condo, pre-petition

Or is it value at time of conversion?

Condo, post-petition, with luxury carpeting and improvements

11 U.S.C. 348 (f)(1)(b)

- **11 U.S.C 348 (f)**
- **(1)** Except as provided in paragraph (2), when a case under chapter 13 of this title is converted to a case under another chapter under this title—
- **(A)** property of the estate in the converted case shall consist of property of the estate, as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion;
- **(B)** valuations of property and of allowed secured claims in the chapter 13 case shall apply only in a case converted to a case under chapter 11 or 12, but not in a case converted to a case under chapter 7, with allowed secured claims in cases under chapters 11 and 12 reduced to the extent that they have been paid in accordance with the chapter 13 plan; and

Post-Petition increase in equity

- *In re Zisumbo, 519 B.R. 851 (Bankr. D. Utah. 2014) (Chapter 7 Trustee not entitled to sell the* debtors' home; the increase in equity ($54,316.81) that accrued from debtors' payment of their mortgage during their Chapter 13 was not property of the Chapter 7 estate).
- *See also In re Wegner, 243 B.R. at 734-35; in re Niles,* 342 B.R. 72 (Bankr. D. Ariz 2000), *In re Page,* 250 B.R. 465, (Bankr. D.N.H 2000)

- Debtor receives large bonus and doesn't disclose this to either his attorney or Ch. 13 Trustee because he doesn't want Ch. 13 Trustee to take it. Debtor puts the money into home improvements, then converts.
- Same result?

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11 U.S.C. 348 (f) (2)

- **C)** with respect to cases converted from chapter 13—
- **(2)** If the debtor converts a case under chapter 13 of this title to a case under another chapter under this title in bad faith, the property of the estate in the converted case shall consist of the property of the estate as of the date of conversion.

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Debtor receives inheritance post petition and pre conversion

- Inheritance received after Chapter 13 petition was filed was not part of Chapter 7 Estate after conversion.

  In re Stillwaggon, , No. 10-bk-12289, 2014 WL 1087898, at *3 (Bankr. M.D. Fla. March 19, 2014.
- In contrast, In re Lybrook, 951 F.2d 136, 137 (7th Cir. 1991) says property inherited by Debtors post petition in a Chapter 13 remains property of the estate after conversion to Chapter 7 even though inheritance would not have been part of the estate had Debtor filed Chapter 7 from the outset.

Personal Injury Claims

Debtor's tort claims that accrued during a Chapter 13 proceeding do not remain property of the estate after conversion to Chapter 7

In re Bobroff, 766 F.2d. 797, 803 (3rd Cir. 1985)
11 U.S.C. 348 (f)(1)(A) essentially codified Bobroff
* Public policy to encourage repayment of debt
* Disincentive to file Chapter 13 if post petition injury claim proceeds to go trustee

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LIFE Insurance proceeds

- Halfway through Debtor's chapter 13, Debtor learns that he had a rich uncle that died and that he was named as a beneficiary to a life insurance policy. Is Debtor required to turn over the proceeds to a chapter 7 trustee if he converts?

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- No. Life insurance proceeds received by Debtor after filing Chapter 13 petition were not part of the estate upon conversion to Chapter 7. Debtor not required to turn over funds to Chapter 7 trustee. *In re Morrison,* 403 B.R. 895, 904 (Bankr. M.D. Fla. 2009), In re Brinkley, 323 B.R. 685, (Bankr. W.D. Ark 2005)
- Different outcome if right to life insurance proceeds vested within 180 days of filing date of chapter 13. 11 USC 541 (a)(5))

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Who gets undistributed funds at the time of conversion?

- **3RD CIRCUIT VS. 5TH CIRCUIT**

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5TH CIRCUIT - Harris vs. Viegelahn
Funds go to creditors

- 757 F. 3d 468
- Equity and policy render creditors' claims to undistributed funds superior to debtor's.
- Reversed Bankruptcy Court's decision.

3RD Circuit – *In re Michael*
Funds go to Debtor

- *In re Michael (Michael II), 699 F.3d 305 (3d Cir. 2012) (Roth, J., dissenting).*
- Undistributed funds go to Debtor, absent bad faith
- Internal tension in code leading to divergent results
- Court analyzed § 348(f), and legislative history
- Legislative history indicates preference to return undistributed funds to the debtor.

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SCOTUS DECIDES

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Harris v. Viegelahn, Chapter 13 Trustee 575 U.S.___(2015)

- Heard on April 1, 2015
- Decided on May 18, 2015
- Unanimous decision held: A debtor who converts to Chapter 7 is entitled to return of any post-petition wages not yet distributed by the Chapter 13 Trustee.

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- 348(f) limits a converted Ch.7 estate to property belonging to Debtor "as of the date" of filing of original Ch. 13 petition, absent bad faith.
- Post-petition undistributed wages are not usually property of the estate.
- Allowing a terminated Ch. 13 Trustee to disburse these earnings in incompatible with statutory design.
- 348(e) Terminates the service of a Ch. 13 Trustee upon conversion.
- 1327(a) & 1326(a)(2) cease to apply once a case is converted and thus no disbursement is required
- Moreover, distributing funds to creditors is not one of the Trustee's post-conversion responsibilities specified by F.R.B.P.
- Debtor not receiving windfall, creditors can require regular distributions