AMERICAN BANKRUPTCY INSTITUTE

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Case Law Update: Business and Consumer Law Developments

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ABI Case Update - Consumer Cases

Henson v. Santander Consumer USA, Inc., No. 16-349, _ U.S. _ (U.S. June 12, 2017). Owner of a purchased debt is not a debt collector when it attempts to collect that debt.

A. Facts

1. CitiFinancial **Auto** loaned money to Petitioners seeking to buy what else - **cars**; Santander purchased the defaulted loans from CitiFinancial.
2. Four Maryland consumers commenced the action against Santander Consumer USA, Inc., and its agents, alleging the Defendants violated the Fair Debt Collection Practices Act.
3. The District Court granted Santander's Motion to Dismiss the Action under Fed., R. Civ. P. 12(b)(6) holding Santander, as purchaser/owner of the debts, was not attempting to collect a debt within the scope of the Fair Debt Collection Practices Act. The Fourth Circuit affirmed.
4. In order to address a split among Circuit Courts, the Supreme Court granted certiorari.
5. On certiorari Petitioners did not raise the theory that Santander was a "debt collector" not only because it regularly collects its own purchased debts, but also because it regularly acts as a third party collection agent for other creditors. Nor did Petitioners raise the issue of whether Santander under 15 U.S.C. § 1692(a)(6) was a debt collector because it engaged "in any business the principal purpose of which is the collection of any debts." The Court did not address these issues.
6. Justice Gorsuch delivered the opinion for a unanimous Court.

B. Holding

1. Petitioners argued the word "owed" is the **past participle** of the verb "to owe," therefore the definition of "debt collector" includes anyone who regularly seeks to collect debts previously "owed . . . another," even if you later buy the debt. Needless to say this was not convincing.
2. Petitioners argued that debt purchasers qualify as debt collectors at least when they regularly purchase and seek to collect **defaulted** debts, because "creditor" in 15 U.S.C. §1692a(4) excludes those who seek to collect a debt obtained "in default." The Court rejected this argument too.
3. Petitioners made a policy argument that the Act did not anticipate the "advent" of the market for defaulted debt, so such activity would have been within the scope of the act. The Court's response: "it is never our job to rewrite a constitutionally valid statutory text under the banner of speculation about what Congress might have done had it faced a question that, on everyone's account, it never faced."
4. Once again using a plain language approach to the statute, the

Court held the term “debt collector” means “third party collection agents working for a debt owner— not on a debt owner seeking to collect debts for itself.”

C. Practice Implications

1. The Fair Debt Collection Practices Act has many definitions and exclusions which must be read carefully.
2. Make it your policy that policy arguments are not your big gun.
3. If one of your best arguments is based on the issue of the use of a past participle, get a really big retainer

Midland Funding, LLC v. Johnson, No. 16-348, 2017 WL 2039159, 581 U.S. _ (U.S. May 15, 2017) filing obviously stale dated claim in chapter 13 case does not violate FDCPA.

A. Facts

1. Midland Funding filed a proof of claim for a purchased credit-card debt of $1,879.71. The statement added the last time any charge appeared on the account was in May 2003, more than 10 years before Johnson filed for bankruptcy. The Alabama statute of limitations is six years.
2. The Chapter 13 Debtor, through Counsel, objected to the claim; Midland did not respond; the Bankruptcy Court disallowed the claim.
3. Johnson brought a lawsuit in District Court against Midland seeking actual damages, statutory damages, attorney's fees, and costs for a violation of the Fair Debt Collection Practices Act. See 15 U.S.C. § 1692k.
4. The District Court held the Act did not apply and dismissed the action. The Court of Appeals for the Eleventh Circuit disagreed and reversed the District Court. The Supreme Court, in an opinion written by Justice Breyer, and joined in by Chief Justice Roberts and Justices Kennedy, Thomas and Alito, reversed the 11th Circuit..

B. Holding

1. "[W]e conclude that filing (in a Chapter 13 bankruptcy proceeding) a proof of claim that is obviously time barred is not a false, deceptive, misleading, unfair, or unconscionable debt collection practice within the meaning of the Fair Debt Collection Practices Act."
2. The act of filing a proof of claim (even one clearly time barred was not “false,” “deceptive,” “misleading,” “unconscionable,” or “unfair.
3. Under §§502, 558, Statutes of Limitations are treated as affirmative defenses under Bankruptcy Law and generally treated as affirmative defenses which must be asserted under state laws. To change this procedure “would require creditors (who assert a claim) to investigate the merits of an affirmative defense (typically the debtor's job to assert and prove) lest the creditor later be found to have known the claim was untimely. The upshot could well be added complexity, changes in settlement incentives, and a shift from the debtor to the creditor the obligation to investigate the staleness of a claim.”
4. “Claim” = “Claim” ≠ “Enforceable Claim.”

5. The Court specifically did not address whether it violates the FDCPA for a debt collector to assert a claim known to be stale "in a civil suit."
6. Features "of a Chapter 13 bankruptcy make it considerably more likely that an effort to collect upon a stale claim in bankruptcy will be met with resistance, objection, and disallowance.... The bankruptcy system, as we have already noted, treats untimeliness as an affirmative defense. The trustee normally bears the burden of investigating claims and pointing out that a claim is stale.... Moreover, protections available in a Chapter 13 bankruptcy proceeding minimize the risk to the debtor."
7. The Court rejected the argument that the 2009 Amendment to Fed. R. Bankr. P. 9011(b) imposed "an affirmative obligation on a creditor to make a prefiling investigation of a potential time-bar defense."

C. Practice Implications

1. "State law usually determines" if there is a right to payment. "The relevant state law is the law of Alabama. And Alabama's law, like the law of many States, provides that a creditor has the right to payment of a debt even after the limitations period has expired." Based on the above quote, it appears as if the holding may **not** apply in states where the expiration of the limitations period extinguishes the remedy **and** the right. Ex. Mississippi and Wisconsin. **Compare**, In re Dubois, 834 F.3d 522 (4th Cir. 2016)("[T]he automatic stay simply bars actions to collect debt outside of the bankruptcy proceeding. The automatic stay helps channel debt collection activity into the bankruptcy process. It does not strip such activity of its debt collection nature for purposes of the FDCPA." Court also held filing of stale dated proof of claim was collection activity regulated by FDCPA but that the filing of a stale dated claim did not violate the FDCPA stating: "We conclude that filing a proof of claim in a Chapter 13 bankruptcy based on a debt that is time-barred does not violate the FDCPA when the statute of limitations [Maryland] does not extinguish the debt."); In re Vaughn, 15-02896-D, 536 B.R. 670, 677 (Bankr. D.S.C. 2015)(" S.C. Code Ann. § 15–3–530 (2015) ... only effects the remedy available to a collecting party rather than the underlying right: it does not erase the debt."); Knox v. McCall 's Adm'r, 3 S.C.L. 531,532 (S.C. Const. Ct. App. 1805) ("[Although it [statutes of limitation] takes away the remedy, [it] does not destroy the right: for a debt, or duty, once fairly contracted, remains such ... notwithstanding the means of its enforcement be removed") (emphasis original); In re Mazyck, 521 B.R. 726,730 (Bankr. D.S.C. 2014) ("When applicable, the bar of a statute of limitation does not extinguish a creditor's underlying right to payment, but it does cause the remedy- enforcement of the right to payment -to be withheld.") (emphasis original). **Note** Statute of limitations for a contract under Article 2 of the UCC is **six years** not three years. See, S.C. Code § 36-2-725(1). See also, Coastal Federal Credit Union v. Brown, 417 S.C. 544, 790 S.E.2d 417(S.C. Ct. App. 2016)("[A]lthough CFCU captioned its complaint as a 'debt collection" action, it alleged Brown defaulted under the contract, CFCU repossessed and sold the vehicle 'in accordance with

the terms of the [c]ontract and applicable law,' CFCU applied the proceeds 'to the [c]ontract,' and Brown owed an outstanding balance that included interest and collection costs pursuant to the contract. Accordingly, CFCU's action relates to the sales contract and is governed by SCUCC Article 2. Because CFCU's action was filed within the six-year statute of limitations in section 36-2-725, we reverse the circuit court's grant of summary judgment to Brown.").

2. Do **all** trustees (not just Chapter 13 trustees) now have a heightened duty to review and object to stale dated claims? "The audience in Chapter 13 bankruptcy cases includes a trustee ... **who must examine proofs of claim and, where appropriate, pose an objection**, §§ 704(a)(5), 1302(b)(1) (including any timeliness objection, §§ 502(b)(1), 558). And that trustee is likely to understand that, as the Code says, a proof of claim is a statement by the creditor that he or she has a right to payment subject to disallowance (including disallowance based upon, and following, the trustee's objection for untimeliness). §§ 101(5)(A), 502(b), 704(a)(5), 1302(b)(1)." Emphasis added.
3. While Fed. R. Bankr. P. 9011(b) does not impose "an affirmative obligation on a creditor to make a prefiling investigation of a potential time-bar defense," it does impose "a general 'obligation on a claimant to undertake an inquiry reasonable under the circumstances to determine ... that a claim is warranted by existing law and that factual contentions have evidentiary support,' and to certify as much on the proof of claim."

Husky Int'l Elecs., Inc. v. Ritz, 136 S. Ct. 1581 (2016) - Section 523(a)(2) does not require a misrepresentation

A. Facts
   1. A corporation that was partly owned by Ritz, the debtor, incurred a debt to Husky.
   2. Subsequently, debtor allegedly drained assets from the corporation to other entities that debtor owned.
   3. Husky sued Ritz in state court for fraud, even though debtor was neither transferor nor transferee of assets.
   4. State court never decided if there was cause of action, which would have required piercing corporate veil.
   5. Ritz filed a chapter 7 petition.
   6. Husky filed a dischargeability complaint under section 523(a)(2) based on "actual fraud".
   7. Fifth Circuit held that, because there was no misrepresentation, debt was dischargeable, creating a split in circuits.

B. Holding
   1. Supreme Court held fraud under section 523(a)(2) encompassed a fraudulent scheme.
   2. The term "actual fraud" incorporates a fraudulent conveyance.
   3. The word "actual" has a simple meaning in the context of common-law fraud: It denotes any fraud that "involv[es] moral turpitude or intentional

wrong."

C. Practice Implications
   1. Facts are far removed from consumer cases.
   2. NCBRC was concerned it could extend to constructive fraudulent transfers.
   3. Language about actual fraud pretty clearly limits decision to intentional fraud.

LVNV Funding, LLC v. Harling (In re Harling), 16-1346, 852 F.3d 367 (4th Cir. 3/30/17) - Does res judicata effect of confirmation of Chapter 13 Plan prohibit Debtors from later objecting to unsecured Proof of Claim based on debt barred by Statute of Limitations?

A. Facts
   1. One week after their Plan was confirmed, Chapter 13 Debtors objected to an assigned unsecured claim which was not scheduled, alleging the claim was unenforceable as being barred by the Statute of Limitations of SC Code 15-3-530.
   2. Creditor responded the Confirmation Order barred the Debtors from objecting to the Claim based on the Fourth Circuit opinion of Covert v. LVNV Funding, LLC, 779 F.3d 242 (4th Cir. 2015).
   3. Bankruptcy Court found the Objection was timely and was not barred by res judicata due to the clause in the Plan reserving the right of parties to object to a Claim after confirmation.
   4. Creditor filed an Appeal, and with the consent of all parties, the appeal was sent directly to the Fourth Circuit Court of Appeals along with a related case.

B. Holding
   1. Court of Appeals reviewed “the bankruptcy court’s application of res judicata de novo.”
   2. “[A] bankruptcy case may contain many ‘final decisions’ that do not necessarily fit squarely into the conventional formulation of res judicata, which is a product of ‘ordinary civil litigation.”
   3. “Chapter 13 confirmation orders have a preclusive effect on those issues litigated by or determined at confirmation, as the plan confirmation order is a ‘final determination’ as to those matters it actually addresses.... “
   4. “Res judicata applies where three conditions are met: (1) there is a prior judgment, which was final, on the merits, ‘and rendered by a court of competent jurisdiction in accordance with the requirements of due process’; (2) the parties to the second matter are identical to, or in privity with, the parties in the first action; and (3) ‘the claims in the second matter are based upon the same cause of action involved in the earlier proceeding....’ The Court found there was no dispute the first two conditions were met.
   5. The claims in the Claims objection (second matter) were not addressed in the claims decided in the Confirmation Order (first matter). “The Confirmation Orders only affected those matters that were decided under § 1325 as part of the plan confirmation, which did not consider anything

regarding the validity of a contested individual unsecured claim regardless of when that claim was filed. Thus, considered under the clear framework of the Bankruptcy Code, res judicata cannot apply to bar the Debtors' objections to LVNV's claims."

6. Giving preferential treatment to claims filed before confirmation would violate §1322(a)(3) and §1322(b)(1). "LVNV would create a separate class of disfavored unsecured creditors whose claims are filed after confirmation and, therefore, are open to challenge at any time prior to the debtor's § 1328 discharge .... Nothing in the Bankruptcy Code authorizes that result and contradicts the single class of unsecured creditors approved by the bankruptcy court in the Confirmation Orders."
7. Distinguished its earlier opinion of Covert stating: "[T]he plaintiffs never objected to LVNV's unsecured claims in their bankruptcy proceedings and did not include the FDCPA claim as an asset of their Chapter 13 estates. Instead, the plaintiffs waited for their Chapter 13 plans to pay out and obtained § 1328 discharges for any liability to LVNV before making their claims outside the bankruptcy court against LVNV. The district court dismissed the plaintiffs' claims against LVNV, and we affirmed based on the doctrine of res judicata." Citations omitted.
8. Emphasized the importance of debtors not circumventing the requirement to make all of their assets (even causes of action under the Fair Debt Collection Practices Act) available to their creditors as required by §1325(a)(4) stating: "Had the Covert plaintiffs met their obligations as Chapter 13 debtors, the FDCPA claims would have been part of their Chapter 13 estates and included in the § 1325(a)(4) determination-whether the debtors' proposed plans were in the 'best interest' of their creditors-by the bankruptcy court in plan confirmation.... Therefore, the Court in Covert was correct to reject the plaintiffs' claims. Here, the Debtors have timely objected to LVNV's claim in the bankruptcy court. And they have not brought a proceeding outside of the bankruptcy court to circumvent the requirements of their Chapter 13 plans to obtain a personal benefit to the detriment of their other creditors."
9. It was unnecessary to determine the validity of the Form Plan's reservation clause.
10. In spite of my *amicus* assistance to the Trustee on behalf of the Debtors, the Court reached the right conclusion.

C. Practice Implications

1. Res judicata in bankruptcy is flexible.
2. If faced with a res judicata argument carefully examine if the claims in the second matter were addressed in the claims decided in first matter.
3. Make sure your client discloses those possible causes of action and schedule them.

Lynch v. Jackson, 853 F.3d 116 (4th Cir. Jan. 4, 2017) - May debtors use National and Local Standards for the means test when their actual expenses are lower?

A. Facts

1. The debtors earned more than the North Carolina median household income, so their chapter 7 petition was subject to the expenses portion of the means test.
2. On their Form 22-A-2, the debtors included the local standard mortgage deduction of $1,548.00 when their actual mortgage expense was $878.00 per month. The debtors also listed the local standard expense of $488.00 per month for each of their two cars, when their actual monthly auto loan payments consisted of $111.000 for one car and $90.50 for the other.
3. The bankruptcy administrator moved to dismiss their Chapter 7 petition as abusive, arguing that a Chapter 7 debtor is "limited to deducting their actual expenses or the applicable National or Local standard, whichever is less."
4. The bankruptcy court ruled for the debtors, and the Fourth Circuit granted a direct appeal because of division on the issue among North Carolina courts.

B. Holding
1. Debtors are entitled to the full National and Local Standard amount for a category of expenses if they incur an expense in that category, even if the actual amounts incurred are less than the standard amounts.
2. The court began by stating that Ransom v. FIA Card Servs. declined to consider the issue of "the proper deduction for a debtor who has expenses that are lower than the amounts listed in the local standards." 562 U.S. 61, 70 (2011) (emphasis added in Lynch).
3. Turning to the plain language of the statute, the 4th Circuit reasoned that its interpretation was necessary to give full effect to Congress's decision to use both the words "applicable" and "actual" in the same sentence.
4. The court further reasoned that interpreting "applicable expenses" to mean "actual expenses" would punish frugal debtors by offering greater protection for prolific debtors who spend up to or beyond the cap.

C. Practice Implications
1. This is the first circuit court of appeals opinion to address a crucial question left open by Ransom and thus is an important victory for consumer debtors.
2. The Fourth Circuit's opinion suggests that, when the plain meaning of the statute conflicts with the debtors' factual circumstances, courts may stick with the plain meaning rather than expanding the forward-looking trend exemplified by Lanning and Ransom beyond the actual holdings of those cases.
3. Even though Lynch was a chapter 7 case, the same reasoning applies in chapter 13.

Birmingham v. PNC Bank, N.A. (In re Birmingham), 846 F.3d 88 (4th Cir. 2017) - Does a security interest in escrow funds, insurance proceeds, and miscellaneous proceeds constitute additional collateral so as to remove a residential mortgage from the anti-modification protection of §1322(b)(2)?

A. Facts
1. Standard Fannie Mae/Freddie Mac Residential first mortgage (Deed of Trust) in the amount of $343,101 contained typical boilerplate language including escrow funds, insurance proceeds, and miscellaneous proceeds (condemnation, damages for misrepresentation as to condition of home, etc.) as collateral.
2. Chapter 13 Debtor filed a Plan and Complaint for Declaratory Judgment claiming the escrow funds and proceeds constituted additional security for the mortgage debt, and the debt should be valued at $206,400.
3. The Mortgage Creditor filed a Motion to Dismiss the Complaint under Fed. R. Civ. P. 12(b)(6). The Maryland Bankruptcy Court dismissed the Complaint. The Debtor appealed the Bankruptcy Court's Order of Dismissal, and the District Court affirmed the Bankruptcy Court's dismissal of the Complaint. The Debtor again appealed and the Court of Appeals affirmed the lower court orders.

B. Holding
1. Standard of review. "Because the district court sits as an appellate tribunal in bankruptcy, our review of the district court's decision is plenary. 'We apply the same standard of review as the district court applied to the bankruptcy court's decision.' 'Findings of fact are reviewed for clear error, and conclusions of law are reviewed de novo.'" Citations omitted.
2. The 4th Circuit reaffirmed the application of Nobelman v. Am. Sav. Bank, 508 U.S. 324, 332 (1993) that §1322(b)(2) "prohibits ... modification where ... the lender's claim is secured only by a lien on the debtor's principal residence."
3. The Court, in an U.C.C. - like definitional examination, reviewed "security interest" as used in §1322(b)(2) and stated: "The Code defines a security interest as a 'lien created by an agreement....' Moreover, a lien is defined as a 'charge against or interest in property to secure a payment of a debt or performance of an obligation....' " The Court then examined the term "debtor's principal residence," as defined in §101(13A)(A) and which included "incidental property" as defined in §101(27B).
4. Bankruptcy law trumped state law in determining if there was additional collateral securing the mortgage.
5. The Court agreed with authority from other circuits that §1322(b)(2) protects a Deed of Trust if it does not expressly attempt to take a security interest in additional collateral but only covers items typically covered by residential mortgages to preserve the property, since any other interpretation would "eviscerate" the anti-modification purpose §1322(b)(2).
6. The Court distinguished the following North Carolina cases cited by the Debtor: In re Bradsher, 427 B.R. 386 (Bankr. M.D.N.C. 2010); Bradshaw v. Asset Ventures, LLC (In re Bradshaw), Nos. 13–06176–8–RDD, 14–00023–8–RDD, 2014 WL 2532227 (Bankr. E.D.N.C. June 4, 2014); In re Murray, No. 10–10125–8–JRL, 2011 WL 5909638 (Bankr. E.D.N.C. May 31, 2011); In re Martin, 444 B.R. 538 (Bankr. M.D.N.C. 2011); In re

Hughes, 333 B.R. 360 (Bankr. M.D.N.C. 2005). The Court of Appeals held the loan documents in both Bradsher and Hughes "**expressly provided that escrow payments constituted additional security for the loan,**" and " the North Carolina bankruptcy courts agree that the anti-modification clause applies to the Fannie Mae/Freddie Mac Deed of Trust before us in this case." Emphasis added.

7. Blessedly no footnotes to parse.

C. Practice Implications

1. Make sure you have good language in mortgage before claiming that additional security exists.
2. Especially important in light of split in case law on whether North Carolina cases are correct.
3. Make sure you read any defined term such as: "security interest," "debtor's principal residence," "incidental property," etc. carefully.
4. SC cases:

In re Kelly, 15-06419-D, 2016 WL 2893984 (Bankr. D.S.C. 5/12/16)(Creditor, as Assignee of a prior Mortgagee, was secured by a lien on Chapter 13 Debtor's Real Estate and filed Motion for Relief from Stay. After a convoluted series of transfers, Debtor owned a one half interest in the Real Estate he used as his residence. The other half interest was owned by the Daughter of the Debtor's deceased wife who used it as a boarding house while the Debtor resided there. The Creditor objected to the Plan alleging §1322(b)(2) prevented valuation of the Real Estate, and the Plan was not feasible or proposed in good faith. The Court initially discussed whether the anti-modification provision of §1322(b)(2) prevented the valuation of the Creditor's Mortgage claim. The Court reviewed its earlier decision under §1123(b)(5) in In re Crump, 529 B.R. 106 (Bankr. D.S.C. 2015) and held a similar result was required in the instant case stating: "While Royals' predecessor originally held a mortgage on both the Pinewood Property and the McCords Ferry Property, everything but the McCords Ferry Property was sold as part of a settlement between the parties, and the liens on the Pinewood Property were released. The fact that the loans were originally secured by additional property is immaterial. Royals' claim is now secured only by the McCords Ferry Property." The Court also rejected Debtor's argument the assignment of rents clauses in the original mortgage documents constituted additional collateral thus taking the Real Estate outside the protection of §1322(b)(2) stating: "Section 101(27B), the bankruptcy code's definition of incidental property, specifically includes 'rents' in connection with a determination concerning what is included in a debtor's principal residence.... The assignment of rents clauses contained in the original mortgage documents are incidental and do not change the character of Royals' security interest or serve as additional collateral." Footnote omitted. The Court rejected the Debtor's argument the use of the Real Estate as a boarding house changed its character as a principal residence stating: "This Court agrees with those courts that hold that if property is the only collateral for a secured creditor's claim and is used as the debtor's principal residence, the mere fact that the property or a portion of the property is used for some other purpose does not preclude the application of the anti-modification provisions in section 1123(b)(5) and section 1322(b). The split in the decisions turns on whether a court adopts the view that the statutes exclude modification of claims only secured by real property that is the debtor's principal residence or secured by property that is only the debtor's principal residence. This difference is significant. The placement of the word ‘only' in the statute indicates that Congress intended the former, not that it intended to allow a debtor to modify a claim on his principal residence if he uses it for any purpose other than his home.... While Debtor does have at least one other individual residing in one of the bedrooms in the home, that fact does not change the property's character as a single family residence.... Because the McCords Ferry Property is the only collateral securing Royals' claim and is Debtor's principal residence, Debtor cannot modify Royals' claim by bifurcating it into secured and unsecured components in his chapter 13 plan. As a result, confirmation of the March 30, 2016 amended plan is denied." Footnote omitted. The Court granted the Creditor's Request for Relief from the Stay pursuant to §362(d)(2) finding the Debtor could not bifurcate the claim and did not have sufficient income to service the entire debt.).

In re Crump, 14-05007-D, 2015 WL 1756436 (Bankr. D.S.C. 4/16/15)(DD)(Prior to filing her **Chapter 11 case**, Debtor executed a Mortgage debt secured by her residence and non-residential real property; the lien on the non-residential real property was released prior to the bankruptcy filing. The Mortgage debt matured prior to the filing of the Chapter 11 case. The Chapter 11 Plan valued the lien on the residence and paid the secured portion in 48 monthly payments with a balloon payment; the unsecured portion was also to be paid by a balloon payment at the end of the 48th month of the Plan. The Mortgage Creditor objected to the Plan arguing the Plan impermissibly modified its residential Mortgage Claim. The Court held the relevant date of inquiry was **the date of the petition**. The Court also held the debt was secured solely by the Debtor's residence stating: "Ameris Bank has a claim. It is presently secured only by the Debtor's principal residence. The mortgage documents show that Ameris Bank's claim was originally also secured by a second mortgage on the Broughton Road property. However, Ameris Bank released its right to enforce its lien against the Broughton Road property....Thus, upon the release of the Broughton Road property, Ameris Bank no longer had any rights or interest with regards to that property. Ameris Bank's lien presently extends only to the Joe Rivers Road property: the principal residence of the Debtor. Its claim is secured only by a security interest in real property that is the Debtor's principal residence." Citations omitted. The Court then addressed whether the Debtor's Plan cured the default or modified the treatment of the matured debt. The Court found the Plan impermissibly modified the matured residential Mortgage debt stating:

"The Court finds support for viewing the Debtor's proposed plan as modifying creditor rights rather than curing a default in the Bankruptcy Code itself.... Although the Debtor argues that § 1123(a)(5)(G) allows her to treat the loan as she proposes, chapter 13 contains the same provision yet Congress felt the need to add § 1322(c)(2) so debtors could reinstate, modify, and pay fully matured home loan debt, if only in one narrow way. Because chapter 11 does not include a provision similar to § 1322(c)(2), the Court concludes that this chapter 11 plan's modification of a fully matured home loan secured by the debtor's principal residence by extending the terms and due date is not permitted. The plan proposes to extend the life of the Ameris Bank loan and significantly alter the payment schedule. This is barred by § 1123(b)(5)." Citations and Footnote omitted.).

Anderson v. Hancock (In re Hancock), 820 F.3d 670 (4th Cir. 2016) - Does curing under § 1322(b)(5) permit the debtor to return to the initial contract interest rate once the mortgagee has imposed the default rate?

A. Facts
   1. A seller-financed mortgage had an initial interest rate of five percent and a default rate of seven percent.
   2. The debtors defaulted, and the mortgagees imposed the seven percent interest rate.
   3. After a few months of non-payment by the debtors, the creditor filed for foreclosure, and the debtors filed for bankruptcy under chapter 13.
   4. The debtors' five-year bankruptcy plan calculated the arrears and post-petition payments using the five percent interest rate.
   5. The mortgagees objected, and the bankruptcy court ruled for the creditors. The district court affirmed, although with a small variation in its holding based on the specific mortgage language (and hence not relevant for many future cases).

B. Holding
   1. The 4th Circuit affirmed, holding that reducing the interest rate on a mortgage of a primary residence as part of a chapter 13 plan is a modification barred by §1322(b)(2). (The court reversed the district court's holding as to the dates the default rate applied).
   2. The court found that the meaning of "cure" as contemplated by § 1322(b)(3) focuses on the ability of a debtor to decelerate and continue paying a loan, thereby avoiding foreclosure. The court cited Collier in support of this proposition.
   3. Looking to the relevant legislative history, the court determined that while Congress intended to allow debtors to decelerate and have a second chance at loan payment, Congress also intended to give "home-mortgagor lenders" special protection against modification, specifically modifications that would "reduc[e] installment payments."
   4. In order to cure and maintain payments, the debtors must "make the same principal and interest payments as provided in the note." Therefore,

abandoning Anderson's contractually agreed upon default rate of interest would be an impermissible modification of the terms of their promissory note.

5. The court responded to debtors' arguments that requiring the default rate of interest would harm the fresh start by stating that not requiring it could cause mortgage lenders to increase their initial interest rates.

C. Practice Implications

1. This appears to be a matter of first impression, at least at the circuit level. The court did not cite any cases directly on point but rather reasoned from cases and secondary sources that cited deceleration as the benefit of cure under §§ 1322(b)(3) and (b)(5).
2. The text of §§ 1322(b)(3) and (b)(5) does not explicitly mention acceleration, unlike their chapter 11 counterpart in § 1124(2). So attorneys outside the 4th Circuit may be able to argue that the Code does not mandate this result. However, the instruction in § 1322(e) that courts determine the amount necessary to cure "in accordance with the underlying agreement and applicable nonbankruptcy law" may bar this argument because default interest rates are established by contract.

Lovegrove v. Ocwen Home Loans Servicing, L.L.C., No. 15-2158, 2016 WL 7378098 (4th Cir. Dec. 20, 2016)(unpub.) - Does informational correspondence containing a bankruptcy disclaimer violate the discharge injunction or the FDCPA, and at what point must a discharge of debt be reported to avoid a violation of the FCRA.

A. Facts.

1. After defaulting on his **$1.2 million home mortgage**, Debtor filed a Chapter 7 case and received a discharge in March 2011.
2. After the discharge, in October 2012, the Defendant, as Servicer of the Mortgage, sent the Debtor an accounting of the debt which also contained a provision for disputing the debt. The Defendant also sent Debtor a letter about "Alternatives to Foreclosure." The Defendant also sent an escrow account disclosure statement in July 2014. All three of these communications contained bankruptcy caveat language which stated: "... [I]f the debt ... has been discharged through bankruptcy, this communication is not intended as and does not constitute an attempt to collect a debt." The Defendant also sent the Debtor monthly statements which also contained a bankruptcy disclaimer which stated: ""If ... the obligation referenced in this statement has been discharged in bankruptcy, this statement is for informational purposes only and is not an attempt to collect a debt."
3. The Defendant incorrectly reported to Consumer Reporting Agencies that the Debtor still owed on the discharged debt. The Debtor wrote multiple letters to the Defendant requesting that the Defendant "stop collection [and] reporting debt to the credit bureau's [sic]."
4. In June 2014, the Debtor wrote to the 3 major Credit Reporting Agencies that Defendant was misrepresenting a discharged debt. On July 21, 2014, Defendant received a dispute notification from Experian, and on that same

day, sent a notice to “all consumer reporting agencies to which it reports removing any reporting as to [ ] Lovegrove's discharged mortgage debt.”

5. **While still living in the home**, the Debtor filed an action in District Court alleging Defendant violated the Fair Debt Collection Practices act by attempting to collect a discharged debt and violated the Fair Credit Reporting Act by misreporting the status of the debt.
6. The District Court granted the Defendant's Motion for Summary Judgment on both causes of action, and the Debtor appealed.

B. Holding

1. A consumer is presumed to have read the notices from a lender and to have a "basic level of understanding."
2. The communications from the Defendant when viewed in light of the bankruptcy disclaimers should have been understood by the Debtor to have been for informational purposes. "Armed with that knowledge and the understanding that his debt had been discharged in bankruptcy, Lovegrove should have known that Ocwen was not attempting to collect a debt from him.”
3. Since there was no attempt to collect a debt, the FDCPA was "not implicated." "Although there is no bright-line rule, '[d]etermining whether a communication constitutes an attempt to collect a debt is a commonsense inquiry that evaluates the nature of the parties' relationship, the [objective] purpose and context of the communication [ ], and whether the communication includes a demand for payment....' Applying this commonsense inquiry, we hold that Ocwen's communications do not constitute an attempt to collect a debt." Citations, footnote, and internal quotation marks omitted.
4. People who are smart enough to still be living in million dollar homes without paying the mortgage payments for several years should be smart enough to understand bankruptcy disclaimers. "Rather, this is a case where a debtor, who has been discharged in bankruptcy but continues to live in a million-dollar home, received documents that contain clear disclaimers indicating that they are not an attempt to collect a debt."
5. Those generic bankruptcy disclaimers actually seem to work. In a Footnote, the Court stated: "The only communications that could possibly be viewed as a demand for payment are the monthly account statements.... Even though the monthly statements generally request payments, we believe that the disclaimer is sufficient to provide notice that, for customers in bankruptcy, Ocwen was providing an updated account summary and not demanding payment."
6. Surprise, surprise - In yet another Footnote, the Court stated: "Foreclosure proceedings against Lovegrove are still possible because foreclosure is an in rem action that survives a bankruptcy discharge.... The FDCPA does not completely prohibit debt collectors from communicating with or seeking payment from a debtor who has been discharged in bankruptcy. Such communications, if they are in connection with the collection of a debt, must simply comply with the FDCPA, for example, they must not be

false, deceptive, or misleading."

7. The Debtor did not have a private right of action for the reporting of inaccurate information until after the dispute had been made to the Credit Reporting Agency reported to the Defendant. After that happened, the Defendant corrected the information regarding the discharge of the debt. "The undisputed facts support the conclusion that Ocwen complied with § 1681s–2(b) when Ocwen immediately corrected the credit reporting error once notified by a CRA of the dispute." See also, Peterkin v. JPMorgan Chase Bank (In re Peterkin), 10-06544-W, Adv. No. 16-80041-W (Bankr. D.S.C. 12/16/16)(JW)(After receiving their discharges, Pro Se Chapter 13 Debtors filed a Complaint alleging numerous causes of action against Mortgage Creditors on two Mortgage Debts on which the arrearages were cured in the Chapter 13 Plan. The Debtors did not name or serve one of the Mortgage Creditors. The Debtors and the one Mortgage Creditor Defendant filed Motions for Summary Judgment. The Court granted the Defendant's Motion for Summary Judgment on the Plaintiffs' causes of action under the Fair Credit Reporting Act stating: "While the FCRA permits consumers to sue furnishers for their failure to comply with 15 U.S.C. § 1681s-2(b), it does not provide consumers with a private right of action for a furnisher's failure to comply with § 1681s-2(a).... Because there is no private right of action for violations of 15 U.S.C. § 1681s-2(a), Plaintiffs claim against Chase under this code section must fail as a matter of law. In addition, because there is no evidence either that Plaintiffs submitted a notice of dispute with the credit reporting agency, or that Chase received notice of Plaintiffs' disputes from the credit reporting agency and failed to act, Plaintiffs claims under 15 U.S.C. § 1681s-2(b) fail as a matter of law. Chase is entitled to summary judgment on the FCRA claims.").

C. Practice implications.

1. Nip it, nip it in the bud, by disclaiming and disclaiming. If you represent a creditor make sure your client's notices, correspondence, Christmas cards contain bankruptcy disclaimers. Disclaim the automatic stay, disclaim the discharge, if you represent a lender which advertises, disclaim your client's cheesy commercials, .
2. Don't expect much sympathy if you represent a debtor who lives in a million dollar house.
3. If you are suing under the FCRA, carefully review under which sections a consumer has a private right of action.
4. In Fourth Circuit Opinions, read those footnotes.
5. Although unpublished opinions of the Fourth Circuit Court of Appeals are not binding precedent, they may provide helpful guidance. In re Serra Builders, Inc., 970 F.2d 1309 (4th Cir. 1992).

In re Versace, 16-05593-B, 2017 WL 1501386 (Bankr. D.S.C. 4/26/17)(HB) - May Chapter 13 Debtor claim family members with whom she does not reside as dependents for purposes of calculating disposable income?

A. Facts

1. Chapter 13 Debtor resided in an apartment with her 10 year old son, but she also claimed as dependents her father, her 20 year old daughter, and her granddaughter. As a result, the Debtor claimed to be a below median debtor and proposed a 36 month plan which paid less than 100% to unsecured creditors.
2. The Debtor also claimed the house which she purchased with her father and in which her father, her 20 year old daughter, and her granddaughter resided as her homestead.
3. A Credit Union with an unsecured claim objected to the Plan alleging the Plan violated the disposable income requirement of §1325(b) in that the expenses of the Debtor were inaccurate. The Credit Union also objected to the Debtor's claim of a homestead exemption.

B. Holding

1. The Court held the Credit Union did not satisfy its burden the homestead exemption was not properly claimed stating: "As of the Petition Date, Versace's daughter and grandchild relied on Versace and her father to provide their reasonable necessities of life. Applicable law instructs the Court to construe the exemption liberally in Versace's favor."
2. To determine whether the Plan satisfied the disposable income requirement of §1325(b), the Court first discussed the issue of who were dependents of the Debtor under the "economic unit" test set forth by the Fourth Circuit Court of Appeals in Johnson v. Zimmer, 686 F.3d 224 (4th Cir. 2012). The Bankruptcy Court found the Debtor's father, 20 year old daughter, and granddaughter were not dependents of the Debtor stating: "Versace asks the Court - at the expense of her creditors - to expand her household size to include individuals that do not live with her at all, and who she has no legal obligation to support. Further, the evidence shows that the two households do not 'inter-mingle' their funds, are not 'interdependent,' and do not operate as a single 'economic unit.' Rather, Versace merely supplements the expenses and debts of the members of the Waxhaw household. The instruction provided by the Fourth Circuit gives no indication that the economic unit approach should be stretched this far. Based on these facts, Versace's household size is two: Versace and her 10 year-old son, who reside in an apartment in Fort Mill together most of the time."
3. In light of the overstatement of her expenses, the Court held the Debtor did not meet her burden of proving the Plan satisfied the disposable income requirement of §1325(b) stating: "[T]he Court finds Versace has overstated her household size to present herself as a below-median income debtor, inappropriately reducing her repayment period from 60 to 36 months. 11 U.S.C. § 1325(b)(4)."
4. The Court also held the Plan did not satisfy the disposable income or good faith requirements for another reason stating: "[T]he plan cannot be confirmed for other reasons, including the fact that without just cause, Versace proposes use of a portion of her income to pay her father's

creditors ahead of her own. Accordingly, the Court cannot find that her plan is presented in good faith and all of her projected disposable income is applied to the plan. As proposed, the current plan provides Versace with a 'head start' as opposed to a 'fresh start' and cannot be confirmed pursuant to § 1325(a)(3) and (b)(1) and (2)." Footnote omitted.

5. In a Footnote, the Court also held the determination of the reasonably necessary expenses of a below median debtor are determined the "old fashioned way" by "using Schedules I and J." See also, In re Cleary, 06-03200-D slip op. at 4-5, 357 B.R. 369 (Bankr. D.S.C. 11/16/06)(" In sum, for an above median income debtor, the expenses are those supplied using the 'means test' calculation with reference to standard Internal Revenue Service expenses recognized for debt collection purposes and to other defined expenses. For a below median income debtor, as we have here, the amounts reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor are determined in the context of the estimated average monthly expenses reported on Schedule J. These expenses must undergo judicial analysis, in the face of an objection, as to reasonableness and necessity; or as some might say, 'the old fashion way.' This Court considers Schedules I and J in the confirmation process for both above and below median income debtors." Citations omitted.); In re Edmunds, 350 B.R. 636, 640 (Bankr. D.S.C. 2006) (JW)“"Disposable income,"” for above median income debtors, is defined as a debtor's 'current monthly income,' also a defined term under § 101(10A), less amounts reasonably necessary 'to be expended' as determined by § 707(b)(2)(A) and (B). See 11 U.S.C. § 1325(b)(3)...." Disposable income for above median debtors is calculated using the standardized expenses set forth on Form B 22C (now Form B122C-2), while calculation of below median income debtors is based on review of I and J Schedules.): In re Girodes, 350 B.R. 31, 36 (Bankr. M.D.N.C. 2006)(With respect to reasonably necessary expenses, the Court stated: "Section 1325(b)(3) specifically defines what constitutes ‘amounts reasonably necessary to be expended' under paragraph (b)(2) for an above-median debtor. That definition has been incorporated into Form B22C. Section 1325(b)(3) does not apply to a below-median debtor. Therefore, reasonably necessary expenses for the below-median debtor are the expenses that the debtor has set forth on Schedule J, and are subject to review by the court. To arrive at a projected disposable income figure for a below-median debtor, the debtor's monthly expenses from Schedule J must be subtracted from CMI as calculated pursuant to Part I of Form B22C.");

C. Practice Implications

1. Remember the homestead exemption statute in S.C. is interpreted broadly.
2. Good discussion of the term "dependent" and application of 4th Circuit authority.
3. The distinction between above median and below median is of great importance.

4. After BAPCPA, the issue of whether the good faith test of § 1325(a)(3) is still implicated in the review of disposable income is a topic of much debate. Some courts hold the strict formulaic approach of BAPCPA prohibits or limits the review of the disposable income requirement through the often cloudy lens of good faith. See Cranmer v. Anderson, 463 B.R. 548 (D. Utah 2011) (District court held bankruptcy court erred in holding that while Social Security Income of Chapter 13 Debtor and his nondebtor Spouse should be excluded from calculating Current Monthly Income and Disposable Income, the Social Security Income should be included in calculating Projected Disposable Income. The District Court stated: "[T]he Court concludes that the bankruptcy court misapplied Hamilton, Appellant should not have been required to include social security income in his calculation of projected disposable income, and that failure to contribute all of Appellant's social security income did not constitute bad faith."); Mancl v. Chatterton (In re Mancl), 381 B.R. 537 (W.D. Wis. 2008) (District Court held good faith analysis of § 1325(a)(3) may no longer be used to review the "sufficiency of resources to unsecured creditors."); In re Winokur, 364 B.R. 204 (Bankr. E.D. Va. 2007) (Following Alexander and Barr cases, Court stated: "If the sole objection to the debtor's good faith is that the debtor proposes to pay the amount Congress requires by the mathematical formula, the debtor has complied with the good faith requirement. He has done everything Congress asked him to do. Congress could have written the law differently. It could have separated the gateway test from the plan payment computation. It could have required a plan payment that was the greater of the mathematical formula or the debtor's actual ability to pay. It did not."). Like the Court in Versace, other courts have held the more rigid analysis of disposable income did not obviate a good faith review of what income the debtor was devoting to the plan and the amount and nature of the expenses being paid by the debtor. See Germeraad v. Powers, 826 F.3d 962, 974 (7th Cir. 2016) (In holding Bankruptcy Court erred in denying Chapter 13 Trustee's Motion to Modify confirmed Chapter 13 Plan to increase payments after tax returns showed Debtors' income increased by $50,000, Court of Appeals held, independent of §1325(b), and based solely on the equities of the situation, " a bankruptcy court may allow modification to increase the debtor's payments if, in its discretion, it concludes that a change in the debtor's financial circumstances makes an increase in payments affordable."); In re Pliler, 487 B.R. 682, 704 (Bankr. E.D.N.C. 2013), aff'd and remanded sub nom. Pliler v. Stearns, 747 F.3d 260 (4th Cir. 2014)(Certified direct appeal to 4th Circuit Court of Appeals due to conflict in Fourth Circuit on "issue of whether ... meeting the disposable income test alone does not mean a debtor has satisfied the good faith requirement of § 1325(a)(3) if it is clear a debtor could reasonably afford a larger plan payment" and other issues.); In re Namie, 395 B.R. 594 (Bankr. D.S.C. 2008) ("Notwithstanding the test formulated under 11 U.S.C. § 1325(b), a debtor must propose a plan in good faith pursuant to

11 U.S.C. § 1325(a)(3)."); In re Anstett, 383 B.R. 380 (Bankr. D.S.C. 2008) ("The strict, mechanical application of § 1325(b)(1)(B) following computation of disposable income using artificial expenditures does not necessarily satisfy the requirement to propose a plan in good faith."); In re Edmunds, 350 B.R. 636 (Bankr. D.S.C. 2006) ("Congress intended to leave intact the past bankruptcy practice of considering a debtor's projected financial situation for purposes of §§ 1325(a)(3) and 1325(b)(1). Therefore, the Court finds that the Deans factors are each still relevant in cases filed after the effective date of the Reform Act.").

5. Never file a case for a debtor who has the same name as any Italian designer, or any designer for that matter.

In re Washington, 16-02667-W, 2017 WL 1130144 (Bankr. D.S.C. 3/24/17) - Should a guaranty claim be disallowed due to issuance of IRS Form 1099-C or as violative of the Statute of Limitations.

A. Facts

1. Debtor's first Chapter 11 case was dismissed. In the second Chapter 11 case (filed with his Wife on February 3, 2011), a Plan was confirmed and the Court entered a Final Decree Closing case, but the Plan still remained in effect pending its completion, after which the Debtors could request a discharge under §1141(d)(5). In the second Chapter 11 case, the City of Columbia filed an Unsecured Claim for $190,199 which was secured by a Mortgage on commercial real estate owned by a non-debtor party and guaranteed by the Debtor and his Wife; the Plan provided for $1,000 per year to be paid pro rata to the City and the other unsecured creditors. The Debtors did not object to the City's Claim and had not requested a discharge.

2. In 2013 an IRS 1099-C Cancellation of Debt tax form was issued to the non-debtor party indicating $157,911 of the debt was discharged due to "Bankruptcy."

3. Debtor and his Wife filed a third Chapter 11 case which was dismissed; the City filed an Unsecured Proof of Claim in the amount of $182,276 in that case.

4. On May 30, 2016, the Debtor filed a Chapter 13 case; the City filed an Unsecured Claim for $182,276. The Debtor objected to the Claim arguing the debt was cancelled and was stale and uncollectible under S.C. Code 15-3-530. The City responded the issuance of Form 1099-C and the actions at City Council Meetings did not cancel the debt, and the debt was based on a sealed instrument and thus subject to the 20 year Statute of Limitations under S.C. Code 15-3-520. The Court overruled the Debtor's Objection to the Claim.

B. Holding

1. Court held the issuance of the Form 1099-C did not cancel the debt stating: "According to the majority of court's reasoning, the IRS Form 1099-C is merely an IRS reporting document and not prima facie evidence of a cancellation of debt. After considering these analyses, this Court

agrees with the majority of cases and believes under South Carolina law, an IRS Form 1099-C would not be considered prima facie evidence that the loan was cancelled. Rather, the Court should look to the entire record to determine if the City cancelled the debt. It appears clear that the Form 1099-C was issued as a result of the Debtor's Confirmed Chapter 11 Plan in the Second Bankruptcy Case. Specifically, the Form 1099-C states that it was being issued because of ‘Bankruptcy.' In addition, the amount listed in the Form 1099-C reflects approximately 85% of the debt, the amount of the debt that was not to be paid through the terms of the Confirmed Chapter 11 Plan. This approach was confirmed by the testimony of Mr. Featheringill who indicated that Form 1099-C was issued only to comply with the IRS's reporting requirements resulting from the bankruptcy, and that the City intended to continue collection efforts. Therefore, it appears the Form 1099-C was issued as a result of the Confirmed Chapter 11 Plan and not as a result of an intentional decision by the City to cancel the debt." Citation and Footnotes omitted.

2. Court also held City's "writing off" of the debt for accounting purposes did not show intent to cancel the debt.
3. The Court rejected the City's argument the 20 year Statute of Limitations of S.C. Code 15-3-520 for Sealed Instruments applied finding there was no seal and no "additional indicia that the parties intended the document to be under seal."
4. The Court held while the 3 year Statute of Limitations of S.C. Code 15-3-530 did apply, the time period had been tolled by the Debtor's numerous bankruptcy cases stating: "In June of 2010, Debtor's First Bankruptcy Case was pending. The automatic stay in that case prevented the City from commencing an action against the Debtor and tolled the statute of limitations. As a result, the statute of limitations for an action accruing in June of 2010 did not begin to run until September 24, 2010, the date that the First Bankruptcy Case was dismissed and the automatic stay was terminated. As a result of the First Bankruptcy Case, the statute of limitations on a June 2010 default was extended to September 24, 2013. Thereafter, Debtor filed the Second Bankruptcy Case on February 3, 2011, which further tolled the statute of limitations. The automatic stay in the Second Bankruptcy Case terminated on July 17, 2012, when the case was closed, and the statute of limitations was tolled for 530 days. As a result of the Second Bankruptcy Case, the statute of limitation on a June 2010 default was further extended to March 8, 2015. On October 3, 2014, Debtor filed the Third Bankruptcy Case on, which further tolled the statute of limitations. The automatic stay terminated in the Third Bankruptcy Case upon the dismissal of that case on January 4, 2016. The statute of limitations was tolled for 458 days as a result of the Third Bankruptcy Case; and therefore, the statute of limitations was extended to June 8, 2016.... Due to the tolling applicable to Debtor, it appears that the City could commence an action based on a June 2010 default under the statute of limitations no later than June 8, 2016. As Debtor filed the present

petition on May 30, 2016, the statute of limitations had not elapsed to bar a collection action by the City before the filing of this Chapter 13 case. Under the specific circumstances of this case, where the extension of the statute of limitation under S.C. Code Ann. § 15-3-100 will be less than 30 days, the limitations period based on a June 2010 default is extended pursuant to 11 U.S.C. § 108(c)(2) an additional 30 days after the termination or expiration of the automatic stay in this case, neither of which has occurred." Footnote omitted.

5. While the Court did not base its ruling on voluntary payments by the Debtor extending the Statute of Limitations under SC Code 15-3-120, in a Footnote, the Court did discuss the argument stating: "In the context of a chapter 13 case, Courts have been reluctant to revive the statute of limitations upon a chapter 13 trustee payment because the payments are not 'voluntary.' However, in the present circumstances, Debtor, as an individual, made the payments directly to the City after the bankruptcy estate had vested all of its property back to Debtor under 11 U.S.C. § 1141(b) upon confirmation, and at a time when Debtor no longer operated as a debtor-in-possession. Therefore, there is an argument that Debtor's payments made pursuant to the Confirmed Chapter 11 Plan were voluntary and restarted the statute of limitations." Citations omitted.

C. Practice Implications

1. A Form 1099-C does not necessarily mean cancellation of a debt.
2. Carefully consider prior bankruptcy cases when calculating discharge of tax debts, statute of limitations, etc.
3. Know which statute of limitation applies to your debt.
4. Familiarize yourself with the shifting burden of proof in objections to claims.
5. Remember that while an individual's chapter 11 case may be closed before completion of plan payments, it can still affect your client.

In re Dowey, 12-02002-W (Bankr. D.S.C. 2/9/17) - Does failure to pay long term mortgage debt directly bar full compliance Chapter discharge under §1328(a)?

A. Facts.

1. Chapter 13 Debtors requested and received hardship discharges under §1328(b).
2. Debtors had failed to make their regular mortgage payments and mortgage creditor obtained relief from the automatic stay.
3. In response to Trustee's Notice of Final Cure under Fed. R.B.P. 3002.1, Mortgage Creditor filed a reply stating the all the direct Mortgage payments due had not been made.
4. Debtors filed a Certification of Plan Completion and Request for Discharge alleging their failure to make the post-petition mortgage payments under their Confirmed Plan did not prevent them from receiving a full compliance discharge under §1328(a), because they had made all the required payments to the Trustee.

B. Holding

1. Debtors' request for a full compliance discharge was rendered moot by the granting of the hardship discharge, but the Court, nonetheless addressed the issue of the Debtors' eligibility for a full compliance discharge stating: "Section 1328(b) allows the Court to 'grant a discharge to a debtor that has not completed payments under the plan.' Therefore, sections 1328(a) and 1328(b) are mutually exclusive-a debtor either completes or does not complete the 'payments under the plan.' By receiving a hardship discharge under § 1328(b), Debtors are bound to the position that they did not make all of the payments under the plan; and therefore, they would not qualify to receive a discharge under § 1328(a). Nevertheless, because this matter is of importance to the Bar and because of the significant memoranda and arguments presented in this matter, the Court will consider Debtors' arguments regarding § 1328(a), including whether § 1322(b)(5) maintenance payments are 'payments under the plan' for purposes of § 1328."
2. The Court then clearly and narrowly defined the issue as follows: "[T]he Court notes that the present matter is limited to whether § 1322(b)(5) maintenance payments are payments under the plan. A determination of whether other payments included in a chapter 13 plan constitute a 'payment under the plan' would depend on the language of the particular plan and the type of debt being paid. Therefore, the Court is not inclined to consider whether additional types of debts included in a plan are 'payments under the plan' at this time."
3. Long term debts under §1322(b)(5) are not analogous to Domestic Support Obligations and are "under the plan."
4. Long term payments made directly to a creditor under §1322(b)(5) are "payments under the plan" for purposes of determining eligibility for a full compliance discharge under §1328(a).
5. Failure to make § 1322(b)(5) maintenance payments can serve as grounds for dismissal under § 1307. "The promise to maintain post-petition payments to a mortgage creditor is a mandatory element of the treatment of claims addressed by § 1322(b)(5), and it is not severable. A failure to perform this promise is a material default of the plan.... The Court cannot reconcile that a debtor would be able to receive a discharge after failing to make the maintenance payments under § 1322(b)(5) when that same failure is grounds for dismissal of the debtor's entire case." Further, the computation of disposable income to pay unsecured creditors under § 1325(b) takes into account the promised direct payments for housing, including Debtors' § 1322(b)(5) maintenance payments. Failure to pay these housing payments may be a grounds to require a higher dividend to unsecured creditors. For these reasons, the Court concludes that 'payments under the plan' as stated in § 1328(a) include the ongoing maintenance payments under § 1322(b)(5) that the debtor makes directly to the creditor. As Debtors have not paid all of their ongoing mortgage payments to Mortgage Creditor, they have not made all their payments under the plan and are not entitled to a discharge under § 1328(a)." Citations and

Footnotes omitted.

C. Practice Implications

1. In a Footnote, the Court listed options available to a Chapter 13 Debtor who has failed to make "post-petition maintenance payments" stating: "the Court has previously recognized the following relief: (1) closing the case without a discharge; (2) seeking a hardship discharge if the debtor can satisf[y] the burden of proof required; (3) proposing a cure of the missed payments over a reasonable period of time during the remaining term of the chapter 13 case ... ; (4) amending the chapter 13 plan to surrender the collateral if § 1329(c) permits ... ; (5) amending the chapter 13 plan to pursue Loss Mitigation/Mortgage Modification if the LM/MM relief results in the cure or waiver of the subject post-petition arrearage; (6) presenting evidence of the mortgage creditor's written agreement to waive or forbear the payment of the subject post-petition arrearage; (7) converting the case to chapter 7 under § 1307(a); and (8) dismissing of the case under § 1307." Citations omitted.
2. Amend the Plan asap after the stay is lifted by a long term creditor.
3. Follows majority rule set forth in the following cases. In Matter of Kessler, 655 F. App'x 242, 244 (5th Cir. 2016)("[I]n Foster, we decided the larger question of whether payments on § 1322(b)(5) debts fall within a Chapter 13 plan. We held that post-petition payments of § 1322(b)(5) debts fall under the plan when pre-petition defaults are also provided for in the plan. Here, the Kesslers plainly included terms in their Chapter 13 plan for maintaining their post-petition mortgage payments; therefore, their post-petition payments are payments under the plan as required by Foster." Citing Matter of Foster, 670 F.2d 478, 493 (5th Cir. 1982)("[A] Chapter 13 plan may provide for the debtor to serve as disbursing agent as to some payments under the plan but may not provide for the making of current mortgage payments outside the plan while providing for the curing of the arrearage on the mortgage claim under the plan..."); Evans v. Stackhouse, 564 B.R. 513, 530 (E.D. Va. 2017)("Accordingly, this Court finds that the Bankruptcy Court properly concluded that Appellant's direct payments fall 'under the plan,' per the terms of 11 U.S.C. § 1328(a), and that Appellant's failure to complete her direct payments render Appellant ineligible to receive a discharge under Section 1328(a)."); <u>In re Ramos</u>, 540 B.R. 580 (Bankr. N.D. Tex.2015) (Debtors' direct post-petition mortgage payments were payments "payments under the plan" under § 1328(a).); In re Perez, 339 B.R. 385. 390 n. 4 (Bankr. S.D. Tex. 2006) affd sub nom, 373 B.R. 468 (S.D. Tex. 2007) ("'Every Chapter 13 plan which this Court has reviewed reflects which claims will be paid through the trustee and which claims will be paid directly by the debtor; therefore, when the plan is confirmed, all payments that are referenced in the plan, regardless of whether they are made by the trustee or directly by the debtor, are payments made 'under the plan.'").

CASE LAW UPDATE: BUSINESS LAW UPDATES

Midland Funding, LLC v. Johnson
No. 16-348, 2017 WL 2039159 (U.S. May 15, 2017)

A creditor filed a proof of claim for debt that was incurred 10 years before the debtor filed for Chapter 13 bankruptcy. The statute of limitations was six years.

- Filing a proof of claim, after the statute of limitations for collecting the debt has expired, is not "false, deceptive, misleading, unfair, or unconscionable" within the Federal Debt Collection Practices Act.
  - **Not false or deceptive:** A claim is a right to payment. State law determines whether there is a right to payment and some states provide creditors with a right to payment after the statute of limitations has expired. Congress intended "claim" to be defined in the broadest possible way. Unenforceability of a claim is an affirmative defense (i.e, timeliness).
  - **Not misleading**: Whether a statement is misleading "requires consideration of the legal sophistication of its audience." In Chapter 13, the audience is a trustee, who is likely to understand what a proof of claim means.
  - **Not unfair or unconscionable, but closer question**: A Chapter 13 bankruptcy proceeding is different from a civil suit both procedurally and substantively, therefore a debtor is more likely to object to a stale claim in a bankruptcy proceeding than in a debt collection civil suit. Also, asserting a stale claim can actually help the debtor because it could be disallowed and discharged. Rule 9011 imposes some limitations that may give rise to sanctions. Filing a time-barred claim without investigating potential time-bar defenses can give rise to sanctions under Rule 9011.

Henson, et al. v. Santander Consumer USA Inc.
United States Supreme Court - Case No. 16–349

The petitioners defaulted on auto loans from CitiFinancial. Santander purchased the defaulted loans from CitiFinancial and sought to collect on the auto loans. The petitioners asserted that Santander was a debt collector because the loans were "owed" to CitiFinancial initially.

- The Federal Debt Collection Practices Act regulates practices of debt collectors who regularly seek to collect debts "owe . .. to another." Based on both the plain terms of the statute and in-depth statutory interpretation, a debt purchaser is not governed by this statute because a debt purchaser seeks to collect debts, that it owns, for itself. It does not matter how a debt owner became a debt owner. "All that matters is whether the target of the lawsuit regularly seeks to collect debts for its own account or does so for 'another'" (i.e., third party collection agents hired by a debt owner, a "repo man").

Czyzewski v. Jevic Holding Corp.
United States Supreme Court - Case No. 15-649

The court approved a Chapter 11 dismissal that distributed property to high- and low-priority creditors while skipping over the middle-priority creditors.

- Bankruptcy courts cannot deviate from the ordinary distribution priority rules without the consent of the affected parties when dismissing a Chapter 11 case. A dismissal aims to return the property to the status quo, but that is not always possible, so bankruptcy courts sometimes employ conditional dismissals (i.e., "structured dismissal" or "hybrid dismissal with confirmation order"). This type of dismissal dismisses the case but approves certain property distributions to creditors. Chapter 7 dismissals must follow the prescribed distribution order and while Chapter 11 has more flexibility, a "bankruptcy court cannot confirm a plan that contains priority-violating distributions over the objection of an impaired creditor class." There is no "rare exception" or "dire circumstances" exception that permits bankruptcy courts to violate the distribution order without the impaired creditors' consent, particularly when the plan does not help to restore the status quo ante or protect reliance interests.

Texas v. Briseno (In Re Briseno)
2017 Bankr. LEXIS 1078 (Bankr. S.D. Tex. Apr. 19, 2017)

Plaintiff, the State of Texas initiated a state cause of action against Debtors—persons involved in a construction business. Shortly thereafter, Debtors filed petitions for Chapter 11 Bankruptcy, presumably to remove the state's actions and to initiate the automatic stay against the state's legal action.

- At issue before the Bankruptcy Court was whether the Debtors' removal to the court was valid pursuant 28 USCS § 1441 governing removal of civil actions and § 1452, which provides for the removal of claims related to bankruptcy cases. The court found that the Debtors needed to have their proceedings returned to state court because the § 1452 exception for "police or regulatory power" applied to Texas's cause of action against Debtors. Additionally, the court determined that § 1441 was inapplicable in this matter because only issues of Texas state law were implicated.

In re World Mktg. Chi., LLC,
564 B.R. 587 (Bankr. N.D. Ill. Feb. 24, 2017)

A bankruptcy trustee denied an Application for an administrative claim filed by employees of the Debtor corporation. The former, terminated employees comprised a Worker Adjustment and Retraining Notification ("WARN") Class. The employees alleged that their termination violated the WARN Act and thus entitled them to administrative priority under 11 USCS § 503(b)(1)(A)(ii). The trustee contended that damages were prepetition, not administrative and that the Debtors did not violate the WARN Act's notice requirement as the Debtors were liquidating their holdings.

- The Application seeking allowance of and payment for an administrative claim for WARN Act damages was granted. The court's reasoning turned on its application of the "liquidating fiduciary exception" provided by the WARN Act. The exception functions as follows:

> A] fiduciary whose sole function in the bankruptcy process is to liquidate a failed business for the benefit of creditors does not succeed to the notice obligations of the former employer because the fiduciary is not operating a "business enterprise" in the normal commercial sense. In other situations, where the fiduciary may continue to operate the business for the benefit of creditors, the fiduciary would succeed to the WARN obligations of the employer precisely because the fiduciary continues the business in operation. 54 Fed. Reg. 16,045 (1989). Commentary from the Department of Labor

- The court found that the exception should not govern this particular circumstance, because 1) the WARN Act is remedial legislation and as such, its exceptions should be narrowly construed and 2) allowing the exception to be applied here would encourage duplicitous actions for corporations.

***Kraz, LLC v. Branch Banking & Trust Co. (In re Kraz, LLC)*, 2017 Bankr. LEXIS 1066, (Bankr. M.D. Fla. Apr. 18, 2017)**

The Creditor, BB&T, acquired an FDIC secured loan owed by Debtor storage facility corporation. Several months before the loan matured, the Debtor received a $5.2 million offer for the property securing the Creditor's loan. In response, the Creditor sent the Debtor an estoppel letter that claimed that the Debtor owed 2.1 million more than the amount due on the loan. The court ruled on issues concerning whether the Creditor was entitled to default interest and the unpaid real estate taxes on the property.

- BB&T had acquired the assets of Colonial Bank after the FDIC took control over Colonial Bank's assets. The FDIC then sold Colonial Bank's assets to BB&T subject a commercial loss agreement. Under a commercial shared loss agreement, the acquiring bank is supposed to "use its best efforts to maximize recoveries on shared loss assets" while the FDIC commits to reimbursing a percentage of the loss that the bank realizes from the distressed assets. However, BB&T did not make an attempt at a loan workout with the Debtor, but sought a higher amount owed on the loan (via the estoppel letter).

- The Debtor filed the bankruptcy case to prevent BB&T from wrongfully foreclosing and counterclaimed for breach of contract. The Bankruptcy Court ruled that BB&T was not entitled to post default maturity interest, unpaid taxes and that it was liable for damages for breach of contract. "The Court is persuaded that had BB&T provided the Debtor an accurate estoppel letter, the Debtor could have sold its property to iStorage. And had the Debtor sold its property to iStorage, it could have paid off the BB&T loan and avoided foreclosure. In short, BB&T's breach ultimately forced the Debtor into bankruptcy, so the Debtor is entitled to recover as damages the fees and costs it has incurred in this case."

***Frontier Star, LLC*,**
2017 Bankr. LEXIS 323 (Bankr. D. Ariz. Feb. 2, 2017)

The Trustee sought to retroactively reject a lease that the Bankruptcy Court had previously ruled could not be rejected. At the same time, the Trustee objected to the Creditor's administrative claim against the estate.

- The Trustee argued that the Creditor was not entitled to an administrative claim under the theory that Creditors were judicially estopped (Trustee said that the Creditors had changed positions on the status of the lease and their position was clearly inconsistent). The Debtors were in fact guarantors of a lease between the Creditor and another party. The court declined to retroactively reject the lease because the lease was not an executory contract under Section 365 and the Debtor nor the Trustee revisited the questions relating to whether the lease assignment could be rejected. For those reasons, the Trustee could not reject the lease assignment nor could the Trustee object to the Creditor's administrative claim.

First S. Nat'l Bank v. Sunnyslope Hous. Ltd. (In re Sunnyslope Housing Ltd.)
9th Cir., No. 13-16180, 5/26/17

Sunnyslope sought to retain an apartment complex after default by exercising the cram-down provision in 11 U.S.C. § 1325(a)(5)(B). The valuation of the apartment complex was based on its continued use as low-income housing as required by a restrictive covenant, even though the potential foreclosure value could be higher.

- Cram-down valuations should be measured by a replacement-value standard rather than a hypothetical foreclosure standard. The value of the collateral is based on the proposed use of the property, subject to any restrictive covenants that may or may not be terminated by a foreclosure. Additionally, reorganization plans under the cram-down provision must be "fair and equitable." The creditor retains its lien and receives payments over time equaling the present value of the secured claim, therefore, "the interest rate chosen must ensure that the creditor receives the present value of its secured claim through the payments contemplated by the plan of reorganization." The "formula approach" is used to calculate the interest rate, "which begins with the national prime rate and adjusts up or down according to the risk of the plan's success." Furthermore, for the reorganization plan to be approved, the debtor must show that the plan "has a reasonable probability of success." Finally, a creditor may elect to have its claim treated as either fully or partially secured under § 1111(b) of the Bankruptcy Code. Courts should allow a creditor to modify its election "after a material alteration to the original plan."

In re: Greene
(Bankr. E.D.N.C. April 28, 2017)

A debtor made payments according to a Chapter 13 plan that was approved in 2011. In 2015, the court entered a discharge order. Sanctions were imposed after a debt servicer willfully violated the discharge injunction in an harassing attempt to collect arrears from the debtor, an Army veteran suffering from PTSD.

- Violations of the discharge injunction can give rise to sanctions if such violations meet the requirements of a two-prong test. "The Fourth Circuit has adopted a two-part test to determine whether contempt sanctions are appropriate: (1) whether the creditor violated the injunction, and (2) whether [it] did so willfully." Violations of the injunction are willful if the acts were intentional and the actor had knowledge of the discharge injunction.

In re: Versace
(Bankr. D.S.C. April 26, 2017)

A debtor misrepresented her household size so she would appear to have less disposable income. The plan could not be approve because it was not presented in good faith.

- A debtor may exempt from the bankruptcy estate any property that is exempt under state or federal law. Because South Carolina has opted out of federal exemptions, South Carolina law applies. Homestead exemptions are construed liberally in favor of debtors and the burden of proof is on the objecting party. The homestead exemption was not found to be improper, however a different standard applies under § 1325, which requires good faith and places the burden of proof on the debtor. Because the debtor misrepresented her household size, the plan cannot be confirmed.

In re: Paul E. Klaas and Beth Ann Klaas
3d Cir. Court of Appeals Case Nos. Nos. 15-3341 & 16-3482, June 1, 2017

The debtors consistently made monthly payments according to the bankruptcy plan, paying a total amount that exceeded the project plan base. Nonetheless the trustee realized that a small sum remained unpaid after 61 months. The Code requires that if the debtor's income is higher than the median income in the debtor's state of residence, "the plan may not provide for payments over a period that is longer than 5 years." 11 U.S.C. § 1322(d)(1). The debtors cured within 16 days of learning of the deficiency, but a creditor alleged that failing to completely fund the base plan within 5 years was a material default that calls for dismissal.

- The bankruptcy court did not abuse its discretion by denying the creditor's dismissal motion. Sometimes consistent monthly payments will not result in full payment of the base plan amount due to unexpected fees, administrative costs, etc. These issues may not become apparent until late in the case. Because the Code does not address this situation, bankruptcy courts "retain discretion under the Bankruptcy Code to grant a reasonable grace period for debtors to cure an arrearage."

Sundquist v. Bank of America, N.A.
Adv. Pro. No. 14-02278
Case No. 10-35624-B-13J (U.S. Bank., E.D. Calif)

A "mirage of promised mortgage modification lured the plaintiff debtors into a kafkaesque nightmare of stay-violating foreclosure and unlawful detainer, tardy foreclosure rescission kept secret for months, home looted while the debtors were dispossessed, emotional distress, lost income, apparent heart attack, suicide attempt, and post-traumatic stress disorder."

- The court awarded over $1 million in actual damages for the willful stay violation and $45 million in punitive damages based on the bank's "reckless-or-callous-disregard for the law or the rights of others." An act done in violation of an automatic stay is void ab initio. Furthermore, a willful violation of an automatic stay does not require specific intent.

In re Energy Future Holdings Corp.
842 F.3d 247 (3d Cir. 2016)

Omission of the term "prepayment" and use of the term "redemption" in the agreement meant that the parties intended for the make-whole provision to apply regardless of the note's maturity.

- Contract terms that are applicable before acceleration are applicable after acceleration. The ramifications of acceleration depend on the contractual language. If parties want a prepayment premium to survive acceleration and maturity, they must explicitly say so. Redemption, however, is different from prepayment because redemption may occur pre- or post- maturity. "Thus, while a premium contingent on 'prepayment' could not take effect after the debt's maturity, a premium tied to a 'redemption' would be unaffected by acceleration of a debt's maturity."

In re Lake Michigan Beach Pottawattamie Resort LLC
547 B.R. 899 (Bankr. N.D. Ill. 2016)

Debtor filed for Chapter 11 bankruptcy on eve of foreclosure to protect equity in its property. One member of the debtor, a "blocking director" acting on behalf of the creditor as provided for in the LLC's operating agreement, did not consent to the bankruptcy petition.

- A filing made in bad faith can constitute "cause" for dismissal under § 1112(b) and courts make this determination on a case-by-case basis by looking at the totality of the circumstances. The *Tekena* factors and the factors described in § 1112(b) are neither exhaustive or mandatory. Filing a bankruptcy petition on the eve of foreclosure to is not alone indicative of bad faith.

- While corporations may not contract away bankruptcy rights, this policy is not necessarily binding when a corporate control document is what defeats the bankruptcy rights, but corporate control documents cannot include an absolute prohibition. A blocking director structure may be permissible but the blocking director must fulfil his fiduciary duties and not solely serve for the purpose of voting to block any potential bankruptcy filing. "The essential playbook for a successful blocking director structure is this: the director must be subject to normal director fiduciary duties and therefore in some circumstances vote in favor of a bankruptcy filing, even if it is not in the best interests of the creditor that they were chosen by." The agreement in question required the director to only consider the interests of the creditor and not the debtor, which the director had a fiduciary duty to. Therefore, the blocking director provision was void under both Michigan corporate governance law and federal bankruptcy law.

In re Intervention Energy Holdings, LLC
553 B.R. 258 (Bankr. D. Del. 2016)

In exchange for a forbearance agreement after the LLC defaulted, the creditor received one unit in the LLC and the LLC amended its company agreement to require unanimous consent of all unit holders to file for bankruptcy.

- A debtor may not contract away its right to discharge in bankruptcy. An agreement to waive bankruptcy rights is unenforceable as a matter of federal public policy because it frustrates the purpose of the Bankruptcy Act by attempting to contractually circumvent the object of the Bankruptcy Act. If this type of provision was permitted, the Bankruptcy Act would essentially be nullified. "A provision in a limited liability company governance document obtained by contract, the sole purpose and effect of which is to place into the hands of a single, minority equity holder the ultimate authority to eviscerate the right of that entity to seek federal bankruptcy relief, and the nature and substance of whose primary relationship with the debtor is that of creditor—not equity holder—and which owes no duty to anyone but itself in connection with an LLC's decision to seek federal bankruptcy relief, is tantamount to an absolute waiver of that right, and, even if arguably permitted by state law, is void as contrary to federal public policy."

In re Tribune Co. Fraudulent Conveyance Litigation
818 F.3d 98 (2d Cir. 2016)

Unsecured creditors brought state law fraudulent conveyance claims seeking to unwind payments the Chapter 11 debtor made to stockholders in a leveraged buyout. There were ongoing avoidance proceedings for the same transfers brought by the bankruptcy trustee under a different legal theory.

- The unsecured creditors had standing to bring the state law fraudulent conveyance claims because the automatic stay had been lifted by the court for cause, however the state law claims were preempted by § 546(e). Creditors' rights have been regulated by the federal government for over 200 years and this congressional power is enumerated in the Constitution. § 546(e) "shields from avoidance proceedings brought by a bankruptcy trustee transfers by or to financial intermediaries effectuating settlement payments in securities transactions or made in connection with a securities contract, except through an intentional fraudulent conveyance claim." The intermediary settlement method is essential to securities markets, an important federal interest. State law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" in this situation because "unwinding settled securities transactions by claims such as appellants' would seriously undermine—a substantial understatement—markets in which certainty, speed, finality, and stability are necessary to attract capital." Allowing these state law claims to proceed would conflict with federal law that aims to minimize securities markets displacement due to bankruptcies. The state law claims were thereby dismissed under the implied preemption doctrine rather than standing grounds.

In re Physiotherapy Holdings, Inc.
2016 WL 3611831 (Bankr. D. Del. June 20, 2016).

Shareholders allegedly committed accounting fraud to overstate a privately-held company's value and solicit bids to purchase the company so shareholders would profit from the sale while the purchasers would unknowingly receive an insolvent company. The Trustee alleges that this fraud led to the chapter 11 petition and thus sought to "claw back payments made to the Selling Shareholders under both state and federal fraudulent transfer law."

- While the safe harbor section clearly applies to claims brought by a trustee, the law regarding post-confirmation assignees of creditor claims less clear. "The issue therefore is straightforward: would allowing the Litigation Trust to pursue its state fraudulent transfer claims have a destabilizing effect on the financial markets Congress sought to protect?" The court did not find evidence of clear congressional intent for § 546(e) to preempt state-law avoidance claims and because states have traditionally retained power over fraudulent transfer law. Therefore, the ordinary presumption against preemption is appropriate. The facts are distinguishable from *In re Tribune* and *In re Tribune* is not binding on this court. "[T]he safe harbor does not bar the litigation trust from asserting its state law fraudulent transfer claims on behalf of the Senior Noteholders. Specifically, the Court holds that a litigation trustee may assert state law fraudulent transfer claims in the capacity of a creditor assignee when: (1) the transaction sought to be avoided poses no threat of "ripple effects" in the relevant securities markets; (2) the transferees received payment for nonpublic securities, and (3) the transferees were corporate insiders that allegedly acted in bad faith. When these three factors are present, a finding of implied preemption is inappropriate."

In Matter of Motors Liquidation Company
829 F.3d 135 (2d Cir. 2016)

After 40 days in bankruptcy, "New GM" acquired "Old GM" "free and clear" from successor liability pursuant to a §363 sale. In the §363 sale agreement however, New GM agreed to assume liability for accidents occurring after the sale and for express vehicle warranties issued by Old GM. In 2014, GM issued a recall due to an ignition switch defect and subsequently dozens of class action lawsuits were filed claiming injury both before and after the §363 closing date. The court addressed the following claims: "(1) pre-closing accident claims, (2) economic loss claims arising from the ignition switch defect or other defects, (3) independent claims relating only to New GM's conduct, and (4) Used Car Purchasers' claims."

- The court held that the pre-closing accident claims and economic loss claims were covered by the free and clear provision but the independent claims and used car purchasers' claims were not covered by this provision. To constitute a claim that can be barred by a free and clear provision, due process requires minimum contact between a debtor and claimant that makes the claimants known and identifiable. "A bankruptcy court may approve a § 363 sale 'free and clear' of successor liability claims if those claims flow from the debtor's ownership of the sold assets. Such a claim must arise from a (1) right to payment (2) that arose before the filing of the petition or resulted from pre-petition conduct fairly giving rise to the claim."

- Publication notice was insufficient because GM knew or should have known about the ignition switch defect before filing for bankruptcy and thus should have provided direct mail notice to the readily identifiable affected vehicle owners. The notice requirement is also applicable to potential claimants with contingent claims. The insufficient notice amounted to a procedural due process violation because the plaintiffs were denied "*any* meaningful opportunity to be heard." Therefore, the pre-closing claims were not barred by the § 363 sale agreement.

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