Case Updates: Business and Consumer Developments

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CONSUMER LAW UPDATE

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I SUPREME COURT RULES THAT SECOND MORTGAGE LIENS CANNOT BE STRIPPED FROM HOMESTEADS IN CHAPTER 7

In Bank of America, N.A. v. Caulkett, the Supreme Court, on appeal from the Eleventh Circuit, ruled that an underwater junior mortgage lien could not be stripped in a Chapter 7 bankruptcy case. The Debtors had filed for Chapter 7 and each owned a house with a senior mortgage lien and a junior mortgage lien, the latter held by Bank of America. Because the amount owed on the senior mortgage is greater than each house's current market value, the bank would receive nothing if the property sold, thus the junior mortgage liens were totally under water. The Eleventh Circuit held that the Debtors could avoid their liens under § 506(d) of the Code, which provides "To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void." 11 U.S.C. § 506(d).

The Supreme Court reversed the Eleventh Circuit holding that the Court's construction of § 506(d)'s term "secured claim" in *Dewsnup v. Timm*, 502 U.S. 410, forecloses resolves the question. The Court in *Dewsnup* concluded that an allowed claim secured by a lien with recourse to the underlying collateral does not come within the scope of § 506(d). Thus, under *Dewsnup*, a secured claim is a claim supported by a security interest in property, regardless of whether the value of that property would be sufficient to cover the claim. The Debtors has asked the Court to limit *Dewsnup* to partially secured claims or underwater liens and the Court declined to adopt that distinction.

[1] Thank you to contributing attorneys, Alvin S. Goldstein; Mark P. Barmat; Alan R. Crane, Jason S. Rigoli; and Aaron A. Wernick

II DOMESTIC SUPPORT OBLIGATIONS

RELEVANT STATUTES ON DOMESTIC SUPPORT OBLIGATIONS

Section 523(a)(5) provides that a "domestic support obligation" is not dischargeable in bankruptcy.

Section 101(14A) defines a "domestic support obligation" as:

a debt that accrues before, on, or after the date of the order of relief … including interest that accrues on that debt as provided under applicable non-bankruptcy law … that is—

(A) owed to or recoverable by—

(i) a spouse, former spouse, or child of the debtor or such child's parent, legal guardian, or responsible relative; or

(ii) a governmental unit;

(B) in the nature of alimony, maintenance, or support (including assistance provided by a governmental unit) of such spouse, former spouse, or child of the debtor or such child's parent, without regard to whether such debt is expressly so designated;

(C) established or subject to establishment before, on, or after the date of the order for relief … by reason of applicable provisions of—

(i) a separation agreement, divorce decree, or property settlement agreement;

(ii) an order of a court of record; or

(iii) a determination made in accordance with applicable nonbankruptcy law by a governmental unit; and

(D) not assigned to a nongovernmental entity, unless that obligation is assigned voluntarily by the spouse, former spouse, child of the debtor, or such child's parent, legal guardian, or responsible relative for the purpose of collecting the debt.

However, even if the debt is dischargeable under section 523(a)(5), it may still be non-dischargeable under section 523(a)(15), which provides that a debt may still be non-dischargeable if it is incurred in connection with a divorce.

Recent Cases on Domestic Support Obligations

1. **In re Saggus**, 528 B.R. 452 (Bankr. M.D.Ala. 2015). A debt due in a marital settlement agreement emanating from the section entitled "Property Settlement" and having none of the indicia of alimony or support would not constitute a non-dischargeable domestic support obligation under section 523(a)(5) in a chapter 13 sproceeding. The Debtor defaulted on his obligations to make this payment to his ex-wife and a consent judgment was entered in state court prior to the bankruptcy filing. The Debtor was in default of the consent judgment at the time of the bankruptcy filing.
2. **In re Trentadue**, 527 B.R. 328 (Bankr. E.D.Wis. 2015). Chapter 13 debtor attempted to discharge an attorneys' fee award in favor of his ex-wife entered in their divorce proceeding due to his over-litigation. The Court held that it was a non-dischargeable support obligation because the award was not entered solely to punish the ex-husband for being overly litigious but to compensate the minor children for the detrimental effect the ex-husband's litigation tactics had on them.
3. **In re Wyly**, 525 B.R. 644 (Bankr. N.D.Tex. 2015). In a Chapter 11 proceeding, the Debtor had agreed in his divorce to act as a financial manager and investment advisor for his ex-wife and to guarantee a minimum return on the funds she had invested with him. The Debtor was required to make up any shortfall from his guaranteed minimum return. The Court held that this obligation constituted a non-dischargeable domestic support obligation as it was clearly intended to assist in her support, even though it was a contractual obligation.
4. **In re Barker**, 2015 WL 2208356 (Bankr. N.D.Ala. 2015). The Chapter 7 Debtor's ex-wife objected to payment of the interim fee applications of the estate's professionals because she was not receiving a payment. The Court overruled objection because the ex-wife failed to articulate which fees should not be paid and recognized that the professionals were entitled to compensation ahead of the domestic support obligations for fees and expenses incurred in administering assets for payment of her claim.
5. **In re Moser**, 2015 WL 2328694 (Bankr. D.Ore. 2105). Non-debtor spouse was awarded attorneys' fees in state court litigation to change custody of the minor child

from the Debtor to her former spouse. The Debtor attempt to discharge the attorney fee award in her Chapter 13 proceeding. The Court disagreed and, after examining the record in the state court, found that the attorneys' fee award was a non-dischargeable domestic support obligation because they were in the nature of support as they were a determination as to the best interests of the child.

6. **In re Kimmel**, 527 B.R. 215 (Bankr. E.D.N.C. 2015). The Chapter 13 Debtor's grandparents sought a determination that an attorneys' fee award in their favor in connection with litigating with the Chapter 13 Debtor over custody of her children constituted a non-dischargeable domestic support obligation. The Court agreed with the grandparents and determined that the fee award was non-dischargeable because the grandparents were the sole guardians of the minor children and the debt with compensation to the grandparents for the expenses they incurred in support of the minor children.
7. **In re Crane**, 2015 WL 1866044 (Bankr. D.N.J. 2015). Even though the property settlement agreement did not clearly designate that health insurance payments that the Debtor was required to make for the benefit of his former spouse were in the nature of support, the agreement did state that they were a "prime consideration", especially for the wife. Accordingly, the Court found that the payments constituted a non-dischargeable domestic support obligation.
8. **In re Millner**, 2015 WL 1395923 (Bankr. N.D.Ga. 2015). An psychologist appointed in the Chapter 7 Debtor's divorce proceedings to evaluate child custody and visitation sought to have the Debtor's debt to her for the evaluation deemed a non-dischargeable domestic support obligation. The Debtor filed a motion to dismiss claiming that the psychologist was not a parent, guardian, responsible relative or governmental unit entitled to protection under (a)(5). The Court disagreed and denied the motion to dismiss holding that it was the nature of the debt that was determinative and not the recipient and that, nevertheless, the debt would be non-dischargeable under (a)(15).
9. **In re Moy**, 2015 WL 1585525 (Bankr. N.D.Ill. 2015). A Debtor's failure to make mortgage and tax payments for residence in which his ex-spouse was living were not non-dischargeable domestic support obligations because the ex-spouse ultimately did not have to make the payments herself.

III §523/727 RECENT CASES

1. In re Chin Kun An, 526 B.R. 24 (Bankr. C.D.Cal. 2015) – 523 Discharge Deadline

Creditors instituted state court lawsuit against the Debtor, Chin Kun An, who subsequently filed for voluntary relief under Chapter 7 of the Bankruptcy Code. The Debtor did not list the Creditors on his schedules and the Debtors did not receive notice of the case to timely file a section 523 dischargeability complaint. The Debtor did file a suggestion of bankruptcy in the state court, staying the litigation and putting the Creditors on notice of the case. The Debtor received his discharge.

However, the Creditors continued to pursue the action in state court and the Debtor eventually filed a motion for sanctions for violating the discharge injunction. The bankruptcy court did not sanction the Creditors but did give the Creditors "60-days from the entry of the Order" to bring any cause of action to determine dischargeability of the debt. On the 60th day after the entry of the Order, the Creditors filed a pleading on the docket titled "complaint", however, the Creditors did not file an actual complain instituting an adversary proceeding and did not pay any filing fee.

The Court set a hearing to determine whether the Creditors had taken the appropriate steps necessary to file a complaint.

a. Federal Rule Bankruptcy Procedure 4007(c)

Fed. R. Bankr. P. 4007(c) requires any complaint to determine dischargeability to be filed not later than 60-days after the first date set for the meeting of creditors under § 341(a). Fed. R. Bankr. P. 4007(c) permits extension of the deadline only upon a showing of cause made prior to the expiration of the deadline. Fed. R. Bankr. P. 4007(c); 9006(b)(3).

The Court likened the 60-day deadline set forth in his Order to the 60-day deadline in Fed. R. Bankr. P. 4007(c). Accordingly, the Court determined that the same interpretation was required and the deadline could only be extended upon a showing of cause made prior to the expiration of the 60-day deadline stated in the Order.

The Court determined that the Creditors missed the deadline by failing to file a proper complaint to institute an adversary proceeding or pay the required filing fee. The Creditors argued they were entitled to relief due to "excusable neglect." The Court did not determine whether "excusable neglect" would apply in this case, because the Court determined that the

Creditors could not establish excusable neglect where they knew about the Bankruptcy Case for at least two years, the Creditors were well aware of the deadline, the Creditors' counsel waited until the last day of filing and couldn't figure out how to commence the adversary proceeding, and failed to take steps the next day to correct his errors.

2. **In re Mowdy, 526 B.R. 63 (Bankr. N.D. Okla. 2015) – 523(a)(2)(A) Exception for Credit Card Company**

American Express instituted an adversary proceeding against the Debtor under 11 U.S.C. §523(a)(2)(A), which excepts from discharge those debts - "for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by— (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition," and requires the following elements be satisfied: "(1) debtor made a false representation, (2) debtor made the representation with the intent to deceive creditor, (3) creditor relied on the representation, (4) creditor's reliance was justifiable, and (5) debtor's representation caused creditor to sustain a loss." Prepetition, the Debtor incurred 182 charges for $93,349.13 within a seven (7) week period on one credit card account and 49 charges for $2,9983.18 on a second account while his non-debtor wife incurred in excess of $30,000 in charges on this second account during that same period. The Debtor was unemployed at the time he incurred these charges and his non-debtor wife did not have the income to satisfy these debts.

The Debtor admitted that each time he used the credit cards; he made a representation to American Express that he intended to repay the debt. The implied fraudulent intent of the debtor is established through a multi-factor test: "(1) length of time between charges made and filing of bankruptcy, (2) whether debtor consulted attorney regarding bankruptcy prior to charges being made, (3) number of charges made, (4) amount of the charges, (5) financial condition of debtor at time charges were made, (6) whether charges were above credit limit of account, (7) whether debtor made multiple charges on any given day, (8) whether debtor was employed, (9) debtor's employment prospects, (10) debtor's financial sophistication, (11) whether there was a sudden change in debtor's buying habits, and (12) whether purchases were made for luxuries or necessities."

Chapter 7 debtor's prepetition credit card debts fell within the discharge exception for false representations; circumstances strongly suggested that the financially sophisticated debtor lacked intent to repay, as charges were incurred when debtor was unemployed, had no other

income source, and had reported monthly expenses of $4,650 exclusive of credit card payments, debtor racked up 182 charges totaling more than $93,000 over 45-day period on one account and 49 charges totaling nearly $3,000 over one-month period on second account, on which nondebtor wife also charged more than $30,000, charges were for luxury items such as electronics, hotel rooms, and airfare, wife's income was insufficient to satisfy these extraordinary charges, which were due in full each month, and charges were not consistent with prior charging history of debtor, a cardholder in good standing, debtor acted with intent to deceive, and creditor justifiably relied on debtor's representations, to its detriment.

In the credit card context, unless a debtor's credit card history is marked by "red flags," the creditor can establish justifiable reliance on the debtor's promise to pay the debt simply by showing that the debtor paid his credit cards in the past.

3. **"Surrender" of real property and foreclosure defense**

A debtor filing for relief under Chapter 7 or Chapter 13 of the Bankruptcy Code must state his intention with respect to secured property. Specifically, a Chapter 7 debtor must state whether he intends to surrender, reaffirm, or redeem property in which a creditor has a secured interest. 11 U.S.C. § 521(a)(2). A debtor filing for relief under Chapter 13 is not required to file a statement of intentions. Instead, the Chapter 13 debtor must propose a plan which declares his intention to surrender, reaffirm, or redeem any secured property in his possession. 11 U.S.C. § 1325(a)(5)(C). While this is straight-forward, a question arises as to what the term "surrender" actually means as "surrender" is not explicitly defined in 11 U.S.C. § 521(a)(2) or elsewhere in the Bankruptcy Code.

Recently, two Florida opinions have been rendered with respect to a debtor's responsibility if he has stated an intent to "surrender" his secured property.[2] *In re Failla*, --B.R.--, 2014 WL 8663569 (Bankr. S.D.Fla. Dec. 19, 2014) (Hyman, C.J.) and *In re Metzler*, --B.R.--, 2015 WL 2330131 (Bankr. M.D.Fla. May 13, 2015) (Williamson, J.) – jointly decided with *In re Patel*, Case No. 8:13-bk-09736-MGW.

Factually, all three cases involve real property in foreclosure, where the debtors did not challenge the validity of the secured debt. Each debtor indicated that it was his intention to "surrender" the real property. Each debtor also took advantage of Florida's "wild card"

[2] [2] *Failla* and *Patel* were Chapter 7 bankruptcy cases while *Metzler* was Chapter 13 case.

exemption, Fla. Stat. § 222.25(4). Even though the debtors stated it was their intention to surrender the real property, each debtor continued to defend or oppose the foreclosure or sale of the real property in state court.

The secured creditors moved to compel the "surrender" of the real property in the bankruptcy court. "The creditors contended that it would be unfair to permit the [d]ebtors to retain the [p]roperty for longer, if not permanently, while the [d]ebtors contest the foreclosure action in the State Court." *Failla*, at *4. The debtors in *Failla* argued that "surrender" as used in Section 521(a)(2) means the debtors were required to surrender the collateral to the trustee, and upon abandonment by the trustee the property reverted back to the debtor, as stated in Section 554(c). *Id*. The debtor in *Metzler* argued that "surrender" as used in 521(a)(2) meant that the collateral would be made available to the secured creditor by dissolving the automatic stay. *Metzler*, at *1.

Both bankruptcy courts found that while "surrender" does not require the physical delivery of the property to the creditor; it does require the debtor to cease the active defense or opposition to the foreclosure or sale of the surrendered property.[3] The debtor's continued defense after stating the intention to surrender such collateral could result in the loss of the debtor's discharge.

4. **In re Card, 2015 WL 2358078 (Bankr. D. Vt. 2015) – 523(a)(15) and (a)(4)**

A Vermont state court entered a divorce decree between the Debtor and her former husband, giving the Debtor use, possession, and title to the former marital residence, however, the Debtor was required to pay the former husband $54,494.00 within six (6) months, or alternatively sell the marital residence to pay the $54,494.00 and secured the former husband's interest by a first mortgage on the marital residence. Three weeks after the divorce decree was entered the former husband died. The Debtor did not make the $54,494.00 payment and the Debtor filed a Chapter 7 Bankruptcy. The estate of the former husband instituted an adversary proceeding to except the $54,494.00 debt from discharge under 11 U.S.C. §523(a)(15) and (a)(4). The Debtor filed a motion to dismiss the complaint.

a. 11 U.S.C. § 523(a)(15)

[3] Where the debtor is not challenging the validity of the debt.

Section 523(a)(15) as amended by BAPCPA excepts from discharge those debts "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." (emphasis added).

In the motion to dismiss the Debtor argued that the debt did not satisfy 523(a)(15) because it was not owed to a spouse or former spouse, rather it was owed to the estate and cited two cases for this argument. The Court rejected the argument and denied the Debtor's motion to dismiss as to this count, stating the case law relied upon by the Debtor was pre-BAPCPA and this was a matter of first impression under section 523(a)(15) post-BAPCPA.

b. 11 U.S.C. § 523(a)(4)

Section 523(a)(4) excepts from discharge any debt "for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny." The former husband's estate based its relief on the premise that the Court would grant a constructive trust, that it was also seeking, and that the Debtor's failure to sell or mortgage the former marital property would be a breach of the Debtor's fiduciary duties under the constructive trust.

The Debtor argued two points to dismiss this count: first, that the Court lacked jurisdiction if a constructive trust was granted because the property would be removed from the estate. The Court rejected this argument because 28 U.S.C. §157(b)(2)(I) grants the bankruptcy court authority to determine dischargeability of a debt even if the debt relates to property outside of the estate.

The Debtor next argued that because she had not absconded with the property a plausible claim did not exist under 11 U.S.C. § 523(a)(4). The Court again rejected this argument because absconding with property is not required under § 523(a)(4). The court denied the Debtor's motion to dismiss as to this count.

5. **Wieland v. Gordon (In re Gordon), 526 B.R. 376 (10th Cir. B.A.P. 2015) – 11 U.S.C. 727(a)(4)**

George David Gordon is a former CPA and attorney who was incarcerated for securities fraud associated with a "pump and dump" scheme and filed a voluntary relief under Chapter 7 of the Bankruptcy Code. The Debtor transferred a number of assets into the name of his wife more

than one (1) year prepetition; however, the Debtor retained a secret beneficial interest in the transferred assets.

The United States Trustee objected to the discharge of the Debtor under section 727(a)(2)(A). Section 727(a)(2)(A) states: "[t]he court shall grant the debtor a discharge, unless *** (2) the debtor, with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with custody of property under this title, has transferred, removed, destroyed, mutilated, or concealed, or has permitted to be transferred, removed, destroyed, mutilated, or concealed— (A) property of the debtor, **within one year before the date of the filing of the petition**." (emphasis added).

The United States Trustee complained that the Debtor failed to disclose the assets transferred to his wife on his schedules and therefore, his discharge should be denied. The Debtor disputed the United States Trustee's argument because the transfers were made more than one year pre-petition. The United States Trustee argued that by concealing his secret beneficial interest in the transferred assets the Debtor had been participating in a "continuous concealment" and therefore the Debtor's discharge should be denied. The Bankruptcy Court for the Northern District of Oklahoma agreed with United States Trustee and denied the Debtor's discharge, 509 B.R. 539 (Bankr. N.D.Okla. 2014), and affirmed by the Bankruptcy Appellate Panel for the 10th Circuit.

IV STUDENT LOAN UPDATE

1. History and Applicable Statutory law

Generally, student loans are not dischargeable. In a chapter 7, 11, or 13, when an individual receives a discharge, the discharge does not include debt incurred through student loans. As stated in Section 523:

> (a) A discharge … does not discharge an individual debtor from any debt –
> ***
> (8) unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents, for—
> (A)(i) an educational benefit overpayment or loan made, insured, or

> guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution; or
>
> (ii) an obligation to repay funds received as an educational benefit, scholarship, or stipend; or
>
> (B) any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual.

11 U.S.C. § 523(a)(8).

Note that the language of "undue hardship" allows for a discharge of student loans under certain circumstances, decided on a case by case basis, and only under very limited circumstances.

The history of student loans in bankruptcy shows a continual narrowing of exceptions to the non-dischargeability of these loans. Prior to 1976, student loans were completely dischargeable in bankruptcy. With the introduction of the US Bankruptcy Code (11 USC 101 *et seq.*) in 1978, student loans for higher education made by nonprofits or governmental units were deemed non-dischargeable, unless the loan first became due more than 5 years before the Petition Date, and/or non-dischargeability would cause "undue hardship".

The Bankruptcy Amendments and Federal Judgeship Act of 1984 further narrowed the exception, by removing the words "higher education", so that the definition of student loans would include all educational loans, not just those used for college. The relevant language was as follows:

> …for an educational loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or a nonprofit institution, unless
>
> A. such loan first became due before five years (exclusive of any applicable suspension of the repayment period) before the date of the filing of the petition; or
>
> B. excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents.

Further narrowing the exceptions to discharge of student loans, The Bankruptcy Abuse

Prevention and Consumer Protection Act of 2005 expanded the treatment of student loans as non-dischargeable to include all "qualified education loans", regardless of whether a nonprofit institution was involved in making the loans. That is, privately-made student loans became non-dischargeable. In addition, the five-year test (i.e., where student loans are due more than 5 years before the Petition Date) no longer applies. Therefore, a debtor must demonstrate "undue hardship" in order to discharge student loan debt.

Procedure

In order to obtain a determination that a student loan is dischargeable, a debtor must initiate an adversary proceeding against the lender per Federal Rules of Bankruptcy Procedure 4007 and 7001(6).

"Undue Hardship" and the *Brunner* Test

To qualify for dischargeability of student loans due to "undue hardship" under § 523(a)(8), a majority of bankruptcy courts have adopted the *Brunner* test, from the case *Brunner v. New York State Higher Educ. Servs. Corp.*, 831 F. 2d 395 (2d Cir. 1987). In *Brunner*, the Second Circuit affirmed the district court's ruling which reversed the bankruptcy court's determination that a Chapter 7 debtor could discharge her student loans. In affirming the district court, the Second Circuit adopted the district court's three part test in determining "undue hardship":

> (1) that the debtor cannot maintain, based on current income and expenses, a "minimal" standard of living for herself and her dependents if forced to repay the loans;
>
> (2) that additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and
>
> (3) that the debtor has made good faith efforts to repay the loans.
>
> *Id*. at 396.

To this day, most bankruptcy courts and a majority of the Circuits have adopted the *Brunner* test. *See, e.g. In re Roberson*, 999 F.2d 1132, 1135 (7th Cir. 1993); *Pa. Higher Educ. Assistance Agency v. Faish (In re Faish)*, 72 F.3d 298, 300 (3d Cir. 1995); *United Student Aid*

Funds v. Pena (In re Pena), 155 F.3d 1108, 1112 (9th Cir. 1998); *Hemar Ins. Corp. of Am. v. Cox (In re Cox)*, 338 F.3d 1238, 1241 (11th Cir. 2003); *United States Dept. of Educ. v. Gerhardt (In re Gerhardt)*, 348 F.3d 89, 91 (5th Cir. 2003); *Educ. Credit Mgmt. Corp. v. Polleys*, 356 F.3d 1302, 1311 (10th Cir. 2004); *Oyler v. Educ. Credit Mgmt. Corp. (In re Oyler)*, 397 F.3d 382, 385 (6th Cir.2005); *Educ. Credit Mgmt. Corp. v. Frushour (In re Frushour)*, 433 F.3d 393, 400 (4th Cir. 2005).

Recent Trends Away from *Brunner*: A Split Among the Circuits

Though the *Brunner* test is still the majority view, some courts have expressed their reluctance to apply the test due to its rigid and somewhat inflexible nature. In fact, there has emerged a split of the Circuits on this issue, with the First Circuit BAP, the Seventh Circuit, the Eighth Circuit, and the Ninth Circuit adopting more lenient standards. The first evidence of a circuit split occurred in 2003, in the case of *Long v. Educational Credit Management Corp. (In re Long)*, *Long v. Educ.,* 322 F.3d 549 (8th Cir. 2003), in which a single mother who had significant mental health problems obtained a discharge of her student loans. The Eighth Circuit, in affirming the bankruptcy court's ruling, stated that the *Brunner* test in this circumstance "diminish[ed] the inherent discretion contained in § 523(a)(8)(B)." The court in *Long* established a more lenient test which factored in the totality of the debtor's circumstances, including (1) the debtor's past, present and likely future financial circumstances; (2) her reasonably necessary living expenses; and (3) any other relevant facts and circumstances. *Id*. at 554.

In *Bronsdon v. Educational Credit Management Corp. (In re Bronsdon)*, 435 B.R. 791 (B.A.P. 1st Cir. 2010), the First Circuit BAP affirmed the lower courts' rulings that a 64-year-old woman, even though she had no "disability or debilitating medical condition" or any dependents, could still discharge her student loan debts based on the totality of her circumstances. *Id.* at 795. The debtor had failed the bar exam three times and could not afford the fee for a fourth attempt nor the expenses of exam preparation. In addition, the debtor was living with her father and could only find low-paying, temporary employment. The court, in justifying its ruling, stated that "*Brunner* takes the [undue hardship] test too far" by forcing debtors to show "extraordinary circumstances" that are not required by the Bankruptcy Code. *Id.* at 801. The Panel specifically declined to adopt the Brunner test, and established the "totality of circumstances" test as the determinant standard for discharging student loans. *Id.* at 799.

The Seventh Circuit has also adopted a broader approach than that outlined in *Brunner*.

In *Krieger v. Educ. Credit Mgmt. Corp.*, 713 F.3d 882 (7th Cir. 2013), the lender argued that the debtor, who was chronically unemployed and was caring for her elderly mother, failed the 3rd prong of the *Brunner* test by failing to commit to an income-based payment plan. The court, however, affirmed the determination of the debtor's discharge of her student loans, stating that though the debtor was unwilling to commit to a future plan based on forthcoming prospects, that said absence of commitment was not fatal to her case "because it is always possible to pay in the future should prospects improve." *Id*. at 884. The court also noted that cases following *Brunner* have turned section 523(a)(8)'s "undue hardship" into "certainty of hopelessness." *Id*. at 885.

In 2013, in the case of *Roth v. Educational Credit Management Corp. (In re Roth)*, 490 B.R. 908 (B.A.P. 9th Cir. 2013), the Ninth Circuit BAP reversed and remanded a bankruptcy court's denial of dischargeability of student loans. In *Roth*, the debtor, who was 64 years old, sought to discharge $95,000 of student loans incurred 15 years earlier due to both physical and mental ailments. Though the debtor's ability to repay appeared hopeless, the bankruptcy court denied the discharge because the debtor failed to renegotiate her loans or participate in a repayment program. The BAP, however, held that "failure to negotiate or accept an alternate payment plan is not dispositive" of a finding of good faith. *Id*. at 920. With a consideration of the debtor's circumstances, the BAP remanded the case with instructions to grant a discharge of the debtor's student loans.

Recent Cases That Still Follow *Brunner*

Though a split among the circuits exists, as outlined above, the majority view still follows *Brunner*. For example, the following two cases, decided this year, demonstrate some courts' unwillingness to discharge student loan debts specifically if the 3rd prong of the *Brunner* test isn't met; that is, if the debtor fails to demonstrate "good faith" in attempting to repay student loans:

In *Conner v. U.S. Dept. Education* (*In re Conner)*, 526 B.R. 218 (Bankr. E.D. Mich. 2015), the bankruptcy court denied the debtor's attempted discharge of her student loans because she (1) only made payments to her lenders through involuntary garnishment; (2) subsequently made 9 months of payments only to stop involuntary garnishment and obtain an additional deferral of collection; and (3) failed to participate in an income-based repayment plan. *See id.* at 230.

Similarly, in *Davis v. Nat'l. Collegiate Trust* (*In re Davis)*, Bankr. W.D. Pa. 2015), the bankruptcy court denied the debtor's attempt to discharge her student loans because she did not demonstrate a "good faith" attempt to repay her student debts, based on the facts that she (1) never made a single loan payment; (2) did not adequately show the court that she was unemployable; and (3) did not avail herself of the benefits of any loan consolidation programs before she filed bankruptcy. *See id.* at 141-2. The court also found that the debtor could not pass the first prong of the *Brunner* test (that she could not maintain a minimal standard of living), noting that even though her present expenses exceeded her income, that in applying this prong of the test, the court should not view her income and expenses as "unalterable". *Id*. at 142 (citing *Goforth v. U.S. Dept. of Educ. (In re Goforth),* 466 B.R. 328 (Bankr. W.D.Pa.2012)). Rather, the court "may consider whether it would be unconscionable to require the Debtor to take any steps to earn more income or to reduce her expenses. *Id.* (citing *Faish,* 72 F.3d at 307). Here, the debtor admitted that she was not looking for a job. In addition, the court noted that there was no medical condition which prevented her from working. *Id.* at 144. Finally, the bankruptcy court found that the debtor failed to prove the 2nd prong of the *Brunner* test, that her financial condition would persist, as the debtor was well-educated, had experience in running her own business, and was not involuntarily unemployed as she was not actively seeking a job.

Tuition Credits are not Excepted from Discharge

A recent case, determined by the Ninth Circuit B.A.P., established in that circuit that an obligation to repay tuition credits provided by a private university does not fall under the discharge exception of section 523(a)(8). In *Inst. of Imaginal Studies dba Meridian Univ. v. Christoff (In re Christoff)*, 527 B.R. 624 (9th Cir. B.A.P. 2015), the university appealed the bankruptcy court's holding that where the debtor did not actually receive funds, but rather financial aid in the form of class credit, the repayment of said "loan" was not excepted from discharge. In affirming, the B.A.P. found that a plain reading of the statute, under subsection (ii), showed that Congress intended that where the educational provider or lender was a private organization, actual funds and not credits alone would need to be received by the debtor for the transaction to fall under section 523(a)(8). *Id.* at 634.

Necessary Determination of the Existence of a Loan

Recent cases on cases on dischargeability of student loans have taken up the issue of when an indebtedness is a "loan" for purposes of section 523(a)(8). For example, in *D'Youville College v. Girdlestone (In re Girdlestone)*, 525 B.R. 208 (Bankr. W.D.N.Y. 2015), the bankruptcy court, in ruling that the debtor's obligations to her former university were dischargeable, found that there was no actual "loan" made and therefore the college's argument for non-dischargeability failed. In this case, the debtor had registered for a class and signed a documents acknowledging liability to the college; however, she did not execute a promissory note nor did she receive any funds. The bankruptcy court held that under the circumstances, no loan was made, citing *Cazenovia College v. Renshaw (In re Renshaw),* 222 F.3d 82 (2d Cir. 2000), where the Second Circuit held that a "loan" under section 523(a)(8) must be "(i) a contract, whereby (ii) one party transfers a defined quantity of money, goods, or services, to another, and (iii) the other party agrees to pay for the sum or items transferred at a later date." *Id.* at 88.

When are Student Loans Subject to Clawback?

Utilizing Chapter 5 avoidance powers, some bankruptcy trustees are attempting to clawback tuition payments made by students' parents who subsequently file bankruptcy. In *Gold v. Marquette Univ (In re Leonard)*, 454 B.R. 444 (Bankr. E.D.Mich 2011), the court held that approximately $20,000 in college tuition payments that parents made on behalf of their 18-year-old son constituted avoidable fraudulent transfers under Section 548 because the parents themselves received no economic value in exchange for the payments. Though the university argued that the "benefit" to the parents was "peace of mind" as well as the expectation that the son would become financially independent, the court stated that because the debtors/parents had no legal obligation to provide the child's tuition, and that said benefit was neither "economic", "concrete", nor "quantifiable", that the payments were therefore avoidable. *Id.* at 457.

Similarly, in *Banner v. Lindsay (In re Lindsay),* 2010 WL 1780065 (Bankr. S.D.N.Y. 2010), the bankruptcy court held that tuition payments were avoidable because debtor did not receive fair consideration and the debtor had no legal obligation to make the tuition payments. *Id.* at 9.

However, other cases have found that tuition payments are not avoidable. In *Sikirica v. Cohen (In re Cohen)*, 2012 WL 5360956 (Bankr. W.D.Pa. Oct. 31, 2012), *rev'd on other grounds*, 487 B.R. 615 (W.D.Pa. 2013), the bankruptcy court rejected the Chapter 7 trustee's attempt to recover payments made by the debtors for tuition for children's undergraduate education, holding that said payments were "reasonable and necessary" for maintenance of the debtor's family "for purposes of the fraudulent transfer of statute only." *Id.* at 10.

Similarly, In *Shearer v. Oberdick (In re Oberdick*), 490 B.R. 687 (Bankr. W.D.Pa. 2013), the court held that the debtor's payments for undergraduate tuition for children were not avoidable, as the tuition constituted expenditures for "necessities". The court noted that even though there may not be a legal obligation to provide for tuition for children, "this Court has little hesitation in recognizing that there is something of a societal expectation that parents will assist with such expenses if they are able to do so." *Id.* at 712.

Another case where it was found that tuition payments are not subject to clawback is *Geltzer v. Xaverian High School (In re Akanmu)*, 502 B.R. 124 (Bankr. E.D.N.Y. 2013), where the Court held that the payments of tuition for the debtor's children "satisfied their legal obligation to provide for their education" and were therefore not avoidable. *Id.* at 131. In addition, the court held that the parents and their children "must be viewed as a single economic unit for these purposes. In other words, goods and services purchased by parents for their minor children should generally be treated, for purposes of constructive fraudulent conveyance analysis, as though they had been purchased by the parents for themselves." *Id.* at 137.

V CONSUMER TAX ISSUES

A Late-Filed Tax Return May Not Be A Tax Return For Purposes of Dischargability

History and Applicable Statutory law

11 U.S.C. § 523(a)(1)(B)(i), states that a tax debt is excepted from discharge if it is a debt "with respect to which a return, or equivalent report or notice, if required (i) was not filed or given."

Prior to the enactment in 2005 of the Bankruptcy Abuse Prevention and Consumer Protection Act (hereinafter "BAPCPA"), the term "return" was not defined in the statute. In *United States v. Hindenlang (In re Hindenlang),* 164 F.3d 1029 (6th Cir.1999), the Sixth Circuit

examined federal tax law and reiterated the definition of "return" set forth in *Beard v. Commissioner,* 82 T.C. 766, 1984 WL 15573 (1984), *aff'd,* 793 F.2d 139 (6th Cir.1986). In order for a Form 1040 to qualify as a return:

> (1) it must purport to be a return; (2) it must be executed under penalty of perjury; (3) it must contain sufficient data to allow calculation of tax; and (4) it must represent an honest and reasonable attempt to satisfy the requirements of the tax law.

In re Hindenlang, 164 F.3d at 1033 (citation omitted).

In 2005, BAPCPA added a "hanging paragraph" to 11 U.S.C. § 523 which defines "return:"

> For purposes of this subsection, the term "return" means a return that satisfies the requirements of applicable nonbankruptcy law (including applicable filing requirements). Such term includes a return prepared pursuant to section 6020(a) of the Internal Revenue Code of 1986, or similar State or local law, or a written stipulation to a judgment or a final order entered by a nonbankruptcy tribunal, but does not include a return made pursuant to section 6020(b) of the Internal Revenue Code of 1986, or a similar State or local law.

11 U.S.C. § 523(a)(*). Thus, pursuant to 11 U.S.C. § 523(a)(*), to be a "return" for purposes of discharge, a document must satisfy the requirements of applicable nonbankrutpcy law and be filed in accordance with the applicable filing requirements.

Case Law

Based upon the language contained in the hanging paragraph which defines "return" to mean a return that satisfies the requirements of applicable nonbankruptcy law (including applicable filing requirements), the three Circuit Courts who have decided the issue of whether a late filed return satisfies the filing requirements of the Internal Revenue Code and thus can be considered a "return" for purposes of subsection 523(a).

Most recently, the First Circuit Court of Appeals in *In re Fahey*, 779 F.3d 1 (1st Cir. 2015) agreed with the Tenth and Fifth Circuits in holding that late-filed tax returns are, by definition, ones that fail to satisfy requirements of applicable non-bankruptcy law, and which do not qualify as "returns," for dischargability purposes. In *Mallo v. Internal Revenue Service (In re*

Mallo), 774 F.3d 1313, 1321 (10th Cir.2014), the Tenth Circuit explained, in reference to the I.R.C.'s deadline for income tax returns, that "the phrase 'shall be filed on or before' a particular date is a classic example of something that must be done with respect to filing a tax return and therefore, is an 'applicable filing requirement.' Similarly, the Fifth Circuit determined that a debtor's failure to comply with a Mississippi law stating that returns "shall be filed on or before April 15th" meant that the returns did not satisfy applicable filing requirements under the hanging paragraph's definition. *McCoy v. Miss. State Tax Comm'n (In re McCoy)*, 666 F.3d 924, 928, 932 (5th Cir.2012).

Likewise, lower courts in other jurisdictions have come to the same or similar conclusions. *Wendt v. U.S. (In re Wendt)*, 512 B.R. 716 (Bankr.S.D.Fla.2013) (Adopted the Fifth Circuit's *McCoy* decision, stating that it is "hard to imagine Congress intended any other result."); *see also Creekmore v. Internal Revenue Serv. (In re Creekmore)*, 401 B.R. 748, 751 (Bankr.N.D.Miss.2008) ("The definition of 'return' in amended § 523(a) apparently means that a late filed income tax return, unless it was filed pursuant to § 6020(a) of the Internal Revenue Code, can never qualify as a return for dischargeability purposes because it does not comply with the 'applicable filing requirements' set forth in the Internal Revenue Code."); *Cannon v. United States (In re Cannon),* 451 B.R. 204, 206 (Bankr.N.D.Ga.2011) ("The cases that have addressed the impact of the undesignated paragraph added by BAPCPA to define 'return' [in § 523(a)] have concluded that a late return can never qualify as a return unless it is filed under § 6020(a) safe harbor provision.... The reasoning in those cases is persuasive."); *Links v. United States (In re Links)*, 2009 WL 2966162 (Bankr.N.D.Ohio Aug. 21, 2009) ("The definition of 'return' under § 523(a) ... necessarily encompasses the filing deadlines for submitting returns contained in the Internal Revenue Code so that a late filed return cannot qualify as a return for purposes of a dischargeability determination.").

There is no split in the Circuit Courts, *i.e.*, no Circuit Courts have held contrary to the First, Fifth and Tenth. However, at least two bankruptcy courts have held, contrary to the Circuit Courts, that the mere fact that a tax return was filed late did not disqualify them as "returns." *In re Coyle*, 524 B.R. 863 (Bankr. S.D. Fla. 2015) (In declining to follow *McCoy* and *Mallo*, the Court rejected a narrow reading of the Hanging Paragraph under which the only late filed returns eligible for discharge pursuant to § 523(a)(1)(B)(ii) are returns filed under § 6020(a)). *In re*

Biggers, 2015 WL 1652342 (Bankr. M.D. Tenn 2015) (The Court agrees with the IRS and those decisions that define "applicable nonbankruptcy law" as the pre-BAPCPA *Beard* test.)

VI BAD FAITH IN INDIVIDUAL BANKRUPTCY CASES

Does Bad Faith Constitute Cause For Dismissal Under 11 U.S.C. §707(a)?

Courts have taken varying approaches on the issue of whether "bad faith" constitutes "cause" for dismissal of a bankruptcy case under Section 707(a). Section 707(a) provides that:

> (a) The court may dismiss a case under this chapter only after notice and a hearing and only for cause, including—
>
> (1) unreasonable delay by the debtor that is prejudicial to creditors;
>
> (2) nonpayment of any fees or charges required under chapter 123 of title 28; and
>
> (3) failure of the debtor in a voluntary case to file, within fifteen days or such additional time as the court may allow after the filing of the petition commencing such case, the information required by paragraph (1) of section 521(a), but only on a motion by the United States trustee.

11 U.S.C. § 707(a).

On one end of the spectrum, the District Court of Colorado found § 707(a) does not include an implicit good faith requirement in the context of the dismissal of Chapter 7 bankruptcy liquidation proceedings. *In re Etcheverry*, 242 B.R. 503 (D. Colo 1999). The *Etcheverry* Court found that the exclusion of good faith provision in §707(a), which is included in Chapter 11, 12 and 13, meant that Congress did not mean to incorporate a good faith requirement when a bankruptcy court rules on motions to dismiss under §707(a).

Other Courts have held that a debtor's bad faith in filing a Chapter 7 case ***may*** be cause for dismissal of the case. The United States Court of Appeals for the Eighth Circuit has held that a debtor's bad faith in filing a Chapter 7 case may be cause for dismissal of the case, but that "bad faith under § 707(a) [must] be limited to extreme misconduct falling outside the purview of more specific Code provisions, such as using bankruptcy as a 'scorched-earth' tactic against a diligent creditor, or using bankruptcy as a refuge from another court's jurisdiction." *In re*

Huckfeldt, 39 F.3d 829, 832 (8th Cir.1994) (citing *In re Khan,* 172 B.R. 613, 624–26 (Bankr.D.Minn.1994). In *Huckfeldt*, the debtor sought Chapter 7 relief to avoid obligations incurred as part of a divorce decree, and in order to make his ex-wife file her own petition for bankruptcy relief.

The United States Court of Appeals for the Ninth Circuit reached a similar conclusion in *In re Padilla,* 222 F.3d 1184 (9th Cir. 2000). In *Padilla,* the debtor filed a Chapter 7 petition listing monthly income of $1,950, monthly expenses of $1,830, and credit card debt of almost $100,000. Most of the credit card debt was incurred in the year prior to the filing of the bankruptcy. The UST filed a motion to dismiss the case under § 707(a), alleging that the incurring of large amounts of credit card debt in anticipation of filing bankruptcy (a tactic described as "credit card bust-out") demonstrated a lack of good faith on the part of the debtor, and was cause for dismissal of the case under § 707(a). The bankruptcy court agreed, and dismissed the case. The Bankruptcy Appellate Panel of the Ninth Circuit reversed. On further appeal, the Ninth Circuit affirmed the decision of the Bankruptcy Appellate Panel. In doing so, the Ninth Circuit expressly followed *Huckfeldt* and declined to equate the term "for cause" found in § 707(a) with a requirement that a Chapter 7 petition be filed in good faith. The Ninth Circuit also noted that, while bad faith may be grounds for dismissal of a case filed under Chapter 11 or Chapter 13 because of "the protracted relationship between reorganization debtors and their creditors" contemplated under those chapters, there was no such ongoing relationship between a Chapter 7 debtor and her creditors, and therefore, no good faith prerequisite to the filing of a Chapter 7 case.

The Ninth Circuit also expressly ruled that engaging in "credit card bust-out" was not cause for dismissal under § 707(a). The Ninth Circuit noted that the credit card debt at issue was by its very nature consumer debt, and that Congress, in response to concerns raised by the consumer credit industry, enacted § 707(b) of the Bankruptcy Code to deal with abusive tactics by consumer debtors, including "avoiding bothersome unsecured debts which they could easily repay." The Ninth Circuit held that any action based upon "credit card bust-out" must be based upon § 707(b), not § 707(a).

Other courts have held that "bad faith" **does** fall within the purview of cause under §707(a). In *In re Baird*, 456 B.R. 112 (Bankr. M.D. Fla. 2010), the court held that good faith is

an inherent requirement of §707(a). The *Baird* Court outlined 15 factors it deemed relevant to the issue of whether a case should be dismissed under §707(a).

In *In re Piazza*, 719 F.3d 1253 (11th Cir. 2013), the Eleventh Circuit affirmed the principle that a finding of "bad faith" was sufficient to support a motion to dismiss under § 707(a). However, the *Piazza* court refused to endorse the 15 factor test used in *Baird*. Instead, the Eleventh Circuit found that "[b]ad faith does not lend itself to a strict formula," *Id*. at 1271 and ruled that "[i]t is instead a fact-intensive judgment that is 'subject to judicial discretion under the circumstances of each case.' "*Id*.

In *In re Bushyhead*, 525 B.R. 136 (Bankr. N.D. Okla. 2015), the Court concluded that a bankruptcy case should be dismissed "for cause" under § 707(a) only under one of the enumerated subsections or "where the debtor has taken advantage of the court's jurisdiction in a manner abhorrent to the purposes of Chapter 7." The *Bushyhead* Court held that the ability to pay is not cause for dismissal under § 707(a). *Id*.

After a detailed analysis of the case law on §707(a), the *Bushyhead* Court aptly asked "What are we to draw from all this? *Bushyhead* at 148. In response to its own question, the *Bushyhead* court stated: "One thing seems certain: the ability to repay pre-petition debt, standing alone, does not constitute cause to dismiss a case under § 707(a). The legislative history says so. The cases that say a debtor must file his or her Chapter 7 case in good faith say so. When it comes to § 707(a), this is one of the few areas of consensus among the courts." *Id.*

VII CHAPTER 13 CONSUMER UPDATES

Who gets the undistributed funds collected by the Chapter 13 upon conversion to a Chapter 7?

The U.S. Supreme Court recently issued its opinion in the case of *Harris v. Viegelahn*, 135 S.Ct. 1829 (2015). The issue was whether the undistributed funds collected pursuant to a confirmed Chapter 13 Plan which is later converted to a Chapter 7 goes to the creditors or the debtor. There was a split of authority on the issue.

The issue stems from the language in Section 348(f) of the Bankruptcy Code. Clearly, property acquired after the filing of a Chapter 13 petition, including wages, does not become part of the Chapter 7 estate upon conversion (absent bad faith). Specifically, this means that any funds paid by the debtor to the trustee pursuant to the Chapter 13 plan that have not been

distributed at the time of conversion are not transferred to the Chapter 7 estate. However, no statute explicitly states what should happen to the funds left undistributed by the Chapter 13 trustee.

The United States Supreme Court held that the undistributed funds must be returned to the Debtor. Absent bad faith, property of the Chapter 7 estate is limited to those assets belonging to the debtor as of the date the original Chapter 13 petition was filed. Since, post-petition earnings are not property of a Chapter 7 estate, the funds must be returned to the Debtor.

Can a reverse mortgage on residential real property be bifurcated with the secured portion of the claim being paid over the life of the plan where the mortgage was accelerated prepetition?

A debtor whose residence is subject to a reverse mortgage which was accelerated prepetition following her mother's death could modify reverse mortgage debt by stripping down mortgagee's secured claim and paying it over life of plan, and has standing to bifurcate the claim and provide for the claim in her Chapter 13 plan, even though debtor had no personal liability to mortgagee. *In re Gray*, No. 14-31097-RAM, 2015 WL 1956802 (Bankr. S.D.Fla. Apr. 10, 2015).

In striping off a wholly unsecured loan on a primary residence, what is the proper valuation date

In re Cahill, No. 12-11666-BAH, 2013 WL 6229144, at *5 (Bankr. D.N.H. Dec. 2, 2013), the court addressed the issue of what date the court should use to fix the value of the residential real property. The court stated that Section 506(a) does not direct a court to make the value determination at a fixed or predetermined time. *Id*. The open-ended language has resulted in a "plethora of case law on the issue" generating "a wide variety of divergent decisions." *Id*. (citing *In re Hales,* 493 B.R. 861, 864 (Bankr.D.Utah 2013)). The decisions fall into two general catagories. Some courts set bright line rules for valuations in specific circumstances. *Id*. (citations omitted). These cases hold that the valuation is determined as of the date of the petition. Other courts support a flexible approach. *Id*. (citations omitted). In *In Re Cahill*, the court adopted the flexible approach and determined based upon the facts in that case that the proper valuation date would be near to the confirmation date.

In *TD Bank, N.A. v. Landry*, 479 B.R. 1 (D. Mass. 2012), the court concluded that the proper valuation date was the petition date rather than the date of plan confirmation.

Is property that is inherited more than 180 days after the filing of a Chapter 13 bankruptcy property of the bankruptcy estate?

There is a divergent of thought on the issue of whether property that is inherited more than 180 days after the filing of a Chapter 13 bankruptcy is property of the bankruptcy estate.

Two circuit courts have determined that when a chapter 13 debtor receives an inheritance more than 180 days after the petition date, the inheritance is property of the bankruptcy estate. *In re Dale*, 505 B.R. 8, 10 (B.A.P. 9th Cir. 2014) and *Carroll v. Logan*, 735 F.3d 147 (4th Cir. 2013) came to the same conclusion.

However, other courts have reached the opposite conclusion. For instance, in *In re Key*, 465 B.R. 709, 712 (Bankr. S.D. Ga. 2012), the court stated that in enacting the provisions of § 1306(a)(2) which pulls post-petition wages into the chapter 13 estate, Congress specifically addressed the express exclusion in § 541(a)(6) of post-petition earnings from property of the estate. Congress did not take such steps to include the property excluded in § 541(a)(5). For these reasons, the court stated that applying the time limitation of § 541(a)(5) to chapter 13 cases does not render § 1306 superfluous. *Id*. Therefore, the court held that an inheritance which the debtor becomes entitled to more than 180 days after the filing of the bankruptcy is not included in the Chapter 13 estate.

Does the deadline contained in Rule 3002(c) apply to secured creditors?

In *In re Pajian*, No. 14-2052, 2015 WL 2182951, at *1 (7th Cir. May 11, 2015), a bank, as a secured lender, filed its proof of claim several months after the deadline set by the court in accordance with Federal Rule of Bankruptcy Procedure 3002(c), which requires creditors to file proofs of claim within 90 days of the date set for the meeting of creditors. The bank argued that Rule 3002(c) applies only to unsecured creditors; as a secured creditor, it asserted, it was entitled to file a proof of claim at any time, at least until plan confirmation. The Seventh Circuit held that the requirement to file a proof of claim applied equally to secured and unsecured creditors. The court recognized a split in authority with *In re Mehl,* No. 04–85570, 2005 WL 2806676, at *2–3 (Bankr.C.D.Ill. Oct.25, 2005) (secured creditors need not comply with the deadline, although

there may be some point after which they cannot file a proof of claim), and *Strong,* 203 B.R. 105, 112–13 (Rule 3002(c) deadline does not apply to secured creditors).

Are Florida debtors precluded from claiming Florida's "wildcard" exemption when they file a Chapter 13 and their residence is protected by the automatic stay?

In the case of In Re Valone, 2015 WL 1918138 (11th Cir. 2015), the debtors filed a Chapter 13 bankruptcy. They owned a residence in which they resided. The debtors did not claim the residence exempt under Florida's Homestead laws and elected to claim Florida's "wildcard" exemption which is only available if the debtors are not claiming or receiving the benefit of Florida's Homestead laws. The Chapter 13 trustee objected to their claiming of the "wildcard" exemption arguing that by choosing to file a Chapter 13 bankruptcy the automatic stay impeded the Chapter 13 trustee's ability to administer the residence, therefore the debtors received the benefit of Florida's Homestead protections. The Eleventh Circuit disagreed and held that the protection afforded by the automatic stay was not enough to make the debtors ineligible to claim the wildcard exemption.

What is the correct test to determine whether modification of a confirmed Chapter 13 plan will be approved and what is the date for determining the "best interest of the creditors" test?)

In In re Nachon-Torres, B.R. 306 (Bankr. S.D. Fla. 2014), the bankruptcy court consolidated four cases where there were motions seeking to modify confirmed Chapter 13 Plans. The court addressed the test for a request for modification and the time to determine the best interests of creditors test.

The bankruptcy court has discretion to allow or not allow a modification of a Chapter 13 plan. There is a split of authority on whether a court should use its discretion when considering a modification. The court held that to modify a Chapter 13 plan, the court must determine whether the statutory requirements for modification are met. Also, the court must determine whether the circumstances that give rise to the proposed modification were neither known nor virtually certain at the time of confirmation. Finally, the court must determine whether there are other circumstances that would otherwise warrant modification.

The court also recognized a split of authority as to whether the date for determining the best interests of the creditors test under section 1325(a)(4) is on the original petition date or on the modification date. The court adhered to the majority position and held that the correct date for the determination is on the date of the modification.

VIII EXEMPTIONS

Recent Cases on Exemptions

1. **Purchase of LLC in an IRA is not prohibited transaction**

In re Nolte, 2015 WL 2128670 (Bankr. E.D.Va. May 15, 2015)

The debtor purchased a 5% interest in an LLC using IRA funds, and a creditor subsequently objected to the exemption, on the grounds that said purchase was a "prohibited transaction" under 26 U.S.C. § 4975, and therefore the IRA lost its status as exempt funds. The court, however, held that the debtor properly claimed the exemption since the debtor's investment of account funds in a limited liability company was not a "prohibited transaction for the debtor's personal benefit" under the Internal Revenue Code, and thus the account was immune from taxation and properly treated as exempt.

2. **Debtor's Bad Faith can preclude an Exemption**

In re Lua, 2015 WL 1969903 (Baknkr. C.D. Cal. May 1, 2015)

The Chapter 7 trustee objected to the amended homestead exemption claimed by debtor, and asserted that the bankruptcy court should use the equitable power that it possessed to enter "necessary or appropriate" orders in order to deny the exemption, when schedules were amended 3 years after petition date and the trustee was close to selling the homestead. The court could deny the debtor's request to amend her schedules to claim a homestead exemption under state law. Although the court was precluded by the U.S. Supreme Court's decision in *Law v. Siegel* from using its powers under 11 U.S.C. § 105 to deny a debtor's request to amend her schedules to claim that property was exempt from creditors' claims, even in cases where a debtor acted in bad faith, the Supreme Court's decision in *Siegel* did not prohibit the court from denying a debtor's request to amend her schedules to claim an exemption to the extent the exemption was based on state law.

3. **522 (f) can only avoid a judgment lien on property actually owned by a debtor.**

In re Weilert, 2015 WL 1815646 (Bankr. E.D. Cal. April 16, 2015)

The Debtors could not avoid a judgment lien on their primary residence for which title was held by a revocable trust at the time the lien was recorded.

At the time that the lien was recorded, the legal title to the property was vested in a revocable trust that was created by the debtor's wife, and she was the sole beneficiary of that trust. Because the trust owned the property, then § 522(f)(1) had no application, as the debtors could not utilize that provision to avoid a judicial lien that encumbered property owned by another.

4. **Strong Presumption of Tenants by Entirety in Account under State Law**
5.

In re Haines, 528 B.R. 912 (Bankr. W.D. Mo. 2015)

Exemption was allowed for brokerage account held by debtor and non-debtor spouse as tenants by the entirety, when the couple had the choice of checking the "tenants by the entirety" box on an account application, but failed to do so. The court held that where the debtor and her non-debtor husband opened a brokerage account together, the account was exempt as tenants by the entirety (TBE) property under 11 U.S.C. § 522(b)(3)(B) because Missouri common law applied, which strongly presumed that all property owned by a husband and wife was TBE property, and the trustee's evidence was insufficient to rebut the presumption. The court also held that where the debtor and her husband testified that their intent was to open a TBE account, despite the fact that they checked the box on the application marked "joint tenants with rights of survivorship," the trustee did not have the right to invoke the parol evidence rule because, as a nonparty to the contract, the trustee fell within the "stranger exception".

6. **A reasonable explanation for purchase of homestead is defense to 522 (o) objection**

In re Van Erem, 2015 WL 1293525 (Bankr. S.D. Tex. March 18, 2015

Debtors were entitled to the homestead exemption as to the equity in their home absent proof of intent to defraud in purchasing the home. Debtors may plan their investments in exempt property to maximize allowed exemptions, even in the face of insolvency, as long as there is no intent to hinder, delay, or defraud a creditor.

A bankruptcy trustee did not show that a husband and wife (joint debtors) who declared chapter 7 bankruptcy were prohibited under 11 U.S.C. § 522(o) from claiming that all of the equity they had in a home in Texas was exempt from creditors' claims because they purchased

the home to shield nonexempt property by converting it into property that was exempt under with the intent to defraud creditors. Although an arbitrator had ordered the husband to repay a large bonus he received from a former employer because he left that job to take another job in Texas, and there was some evidence that the debtors concealed their assets from the husband's former employer, the debtors moved to Texas so the husband could take a new job and they had a reasonable explanation for making a $112,589 down payment when they bought their Texas home.

7. **A debtor cannot have the intent to make a home his homestead when he did not think he owned the property.**

In re Charania, 2015 WL 1208616, (Bankr. S.D. Fla. March 11, 2015)

A debtor in a reopened case could not claim a homestead exemption in property he did not believe he owned at the time of his original bankruptcy filing.

A debtor who reopened his chapter 7 bankruptcy case seven years after it was closed was not allowed to claim that a lien a judgment creditor had placed on a home he owned could be avoided pursuant to 11 U.S.C. § 522(f) because it impaired his homestead exemption. The debtor did not claim a homestead exemption in his home when he declared bankruptcy because he thought he had sold the home to his son and daughter-in-law, and he was not allowed to return to court seven years later and claim that the home was his homestead at the time he declared bankruptcy because he resided in the home and had the intent to permanently live there. In order to qualify for the homestead protection in Florida, an individual must (1) occupy the property and (2) have the actual intent to permanently live in the property. Here, the debtor could not have had the actual intent to permanently live at the property because at the time of filing, the debtor thought he did not own the property.

8. **522 (o) reduction of homestead ordered because of liquidation and concealment of assets into the homestead**

In re Roberts 527 B.R. 461 (Bankr. N.D. Fla. 2015)

The chapter 7 debtors' homestead exemption was reduced pursuant to 11 U.S.C. § 522(o) because the debtors' actions and testimony combined to show that they liquidated their non-exempt assets in order to acquire a valuable exempt homestead that they did not have before, with the purpose of hindering, delaying or defrauding their creditors. Here, the debtors liquidated substantial non-exempt assets to fund the construction of new home, did not disclose those

transfers or value of and equity in new home to mortgagee of former home when they continued with the short sale of their former home and received forgiveness of about $250,000 in debt. In addition, the debtors misled the mortgagee by failing to disclose that their inability to pay the mortgage for former home was caused entirely by the liquidation of their assets for construction of new home and that they defaulted on the mortgage on their former home while in the process of transferring assets and building new home, and as a result of debtors' transfers, their balance sheet went from several hundred thousand dollars' worth of nonexempt assets to $0.

9. **Exempt assets cannot be used to pay administrative expenses even if caused by debtor's fraud**

Law v. Seigel, 134 S.Ct. 1188 (2014)

The Supreme Court held that neither § 105(a) nor the inherent authority of the bankruptcy court could contravene a specific provision of the Code, such as § 522(k), which expressly prohibited the application of a debtor's exemption to the payment of any administrative expenses. The bankruptcy court always has the ability to sanction the debtor's misconduct by denying the debtor's discharge and imposing sanctions under Rule 9011 and imposing other appropriate sanctions under § 105, and the bankruptcy court's inherent authority, but that authority could not contravene an express provision of the Code.

10. **Debtor cannot use Federal Exemptions on law outside of the filing state where the filing state's law could be applied to out of state property**

In re Wilson, 2015 WL 1850919 (Bankr. D. Idaho January 13, 2015)

Debtors could not claim federal exemptions in property located outside of filing state where the exemptions available under the law of the filing state could be applied to out-of-state property.

A husband and wife were not allowed to claim the federal exemptions that were available under 11 U.S.C. § 522(d)(1) on property that they owned in Idaho because they were Colorado residents for purposes of the Bankruptcy Code at the time they declared chapter 7 bankruptcy and were required to use the exemptions that were available under Colorado law. In addition, the key to interpreting the hanging paragraph that followed the other provisions of 11 U.S.C.S. § 522(b)(3) was concluding that a debtor was ineligible to claim any exemptions under state law due to the domiciliary requirements of § 522(b)(3)(A), and because Colorado law did

not prohibit debtors from using Colorado law to claim exemptions on property that was located outside of Colorado, the debtors were required to use Colorado law.

11. **Strong Presumption in Favor of Homestead Exemption**

In re Edwards, 2015 WL 179073 (Bankr. N.D. Tex. January 13, 2015)

Objections by the trustee and the creditors' committee to the debtor's state homestead exemption were overruled, because the chapter 7 debtor met his burden of proof that the real property he owned (the "Dallas Property") was his homestead. The debtor resided at the Dallas Property when he was not living at his girlfriend's house, kept his personal property at the Dallas Property, and intended to claim the Dallas Property as his homestead under Texas law. Although the bankruptcy trustee and the Creditors' Committee filed objections to the debtor's claim, the evidence they offered which showed that the debtor received his mail at his girlfriend's address, used his girlfriend's address when he obtained a driver's license, did not file documents with Dallas County, Texas, prepetition claiming that the property in question was his homestead, and failed to list the property as exempt on the first Schedule C, was not sufficient to overcome the debtor's proof that the Dallas Property was the debtor's homestead for exemption purposes.

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Recent Case Developments
Business Cases
20th Annual Southeast Bankruptcy Workshop

Professor Michelle M. Harner
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Although quarterly business filings are generally down,[2] the courts and parties in pending Chapter 7 and Chapter 11 business cases have been very active. In many instances, the courts have addressed issues that continue to divide the circuits in the business bankruptcy context. These issues include the calculation of interest under section 1129(b) of the Bankruptcy Code, the treatment of trademark licenses under section 365 of the Bankruptcy Code, and a court's ability to deviate from the Bankruptcy Code's priority scheme in the context of a settlement.

The following overview summarizes some recent key decisions in Chapter 7 and Chapter 11 business cases. This overview is not an exhaustive list. Rather, it attempts to identify cases that represent the kinds of issues being litigated in business bankruptcy cases and how courts are resolving those disputes. It also focuses on circuit level decisions, with a few lower court decisions on particularly timely or interesting issues. The overview is organized by general topic area.

Appealable Final Orders

- **Pinpoint IT Servs., LLC v. Rivera, No. 14-418 (R46-007), 135 S.Ct. 1758 (U.S. Apr. 17, 2015) (case below 761 F.3d 177).**

  The Supreme Court dismissed the petition for *writ of certiorari* pursuant to Sup. Ct. R. 46.1.

  The issue in *Pinpoint*, in the United States Court of Appeals for the First Circuit, was whether orders denying relief from the automatic stay are final and appealable as a matter of right. The First Circuit held that such orders are not final unless they have definitively decided a discrete, fully developed issue that is unreviewable in another forum. *The circuits are split on this particular issue.*

Attorney's Fees

- **Rose Hill Bank v. Mark J. Lazzo, P.A. (*In re* Schupbach Invs., LLC), 521 B.R. 449, 2014 WL 6680122 (B.A.P. 10th Cir. Nov. 25, 2014).**

  Bankruptcy attorney, Mark Lazzo, performed work on behalf of debtor Schupbach Investments, LLC ("SILLC") prior to, and after, SILLC filed for bankruptcy.

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[1] Professor Harner would like to thank Robbie Walker, UM Carey Law J.D. Candidate 2016, for his assistance in researching and drafting these materials. The materials draw upon and summarize the key aspects of each bulleted case; the facts and issues are taken directly from the cases.

[2] See generally http://www.uscourts.gov/news/2015/04/27/march-2015-bankruptcy-filings-down-12-percent (reporting 26,130 business bankruptcy filings for the year ending March 31, 2015, compared to 31,671 business bankruptcy filings for the year ending March 31, 2014).

When SILLC commenced its Chapter 11 case, it did not file an application to employ Lazzo. In fact, an application was not filed until one month after the petition date. The initial application failed to address the services performed in that one-month gap ("Gap Period"). The primary issues addressed by the court were whether the Bankruptcy Court erred by: "(i) granting employment of counsel *post facto* under 11 U.S.C. § 327; and allowing fees for services rendered prior to filing of the employment application; (ii) allowing fees for services that did not benefit the estate; and (iii) allowing fees for services rendered postconfirmation."

The Ninth Circuit BAP (i) reversed the Bankruptcy Court's approval of Lazzo's employment *post facto* and its allowance of fees incurred during the Gap Period; (ii) affirmed the Bankruptcy Court's allowance of fees disputed as not benefitting the estate; and (iii) reversed the Bankruptcy Court's allowance of postconfirmation fees, holding that "Lazzo was not entitled to compensation for services rendered after confirmation because SILLC no longer had the ability to employ, and the Bankruptcy Court no longer had the ability to award compensation to, professional persons under §§ 327 and 330."

- **Barron & Newburger, P.C. v. Tex. Skyline, Ltd. (*In re* Woerner), 783 F.3d 266 (5th Cir. 2015).**

The attorney for the debtor applied for fees relating to work performed in connection with the debtor's Chapter 11 case before the case was converted to one under Chapter 7. The Bankruptcy Court awarded the attorney only 15% of the fees requested and explained that for a service to be compensable under § 330, fee applicants must prove that the service resulted in an "identifiable, tangible, and material benefit to the bankruptcy estate." *In re Pro-Snax Distribs., Inc.*, 157 F.3d 414 (5th Cir. 1998). The Bankruptcy Court found much of the attorney's billed time "was not of identifiable benefit to the estate." On appeal, "the District Court found no error in the Bankruptcy Court's application of *Pro-Snax* to the fee application."

The issue on appeal to the Fifth Circuit was whether the "hindsight" or "material benefit" standard enunciated in *Pro-Snax* conflicts with the text and legislative history of § 330 and is at odds with other circuits. The Fifth Circuit overruled *Pro-Snax*, and held that § 330 "embraces the 'reasonable at the time' standard for attorney compensation" (endorsed by the Second, Third, and Ninth Circuits). The Court explained that § 330 "contemplates a prospective standard for the award of attorney's fees relating to bankruptcy proceedings—one that looks to the necessity or reasonableness of legal services at the time they were rendered," and not on their success in hindsight. Under this framework, if a fee applicant establishes that its services were "necessary to the administration" of a bankruptcy case or "reasonably likely to benefit" the bankruptcy estate "at the time at which [they were] rendered," see 11 U.S.C. § 330(a)(3)(C), (4)(A), then the services are compensable. *This decision appears to resolve an open circuit split on the issue.*

Recent Case Developments
Business Cases

Chapter 15 – Cross-Border Insolvencies

- ***In re* Rede Energia S.A., 515 B.R. 69 (Bankr. S.D.N.Y. 2014).**
  The foreign representative of a Brazilian debtor sought enforcement of a reorganization plan that was confirmed under Brazilian bankruptcy law. The Bankruptcy Court found that "the requested plan enforcement relief was proper under both §§ 1521 and 1507 of the Bankruptcy Code and should not be denied pursuant to the public policy exception in § 1506."

Contents of Plan

- **SCH Corp. v. CFI Class Action Claimants, No. 14-28888, 2015 WL 756552 (3d Cir. Feb. 24, 2015).**
  CFI Claimants appealed a District Court order affirming a Bankruptcy Court order granting a motion filed by the Chapter 11 debtors, SCH, to approve the settlement reached with the plan funder, National Corrective Group, Inc. ("NCG"). The issue was whether the Bankruptcy Court properly applied the factors laid out in *In re Martin*, 91 F.3d 389 (3d Cir. 1999), to determine that the settlement at issue was fair and equitable and adequately addressed the CFI Claimants' allegations of collusion.
  The Third Circuit found that the Bankruptcy Court abused its discretion by failing to consider the purported settlement as a modification of a confirmed plan governed by § 1127. The Circuit Court vacated the District Court's order and remanded with instructions for the District Court to vacate the Bankruptcy Court's order and direct the Bankruptcy Court to consider the purported settlement as a request for a plan modification pursuant to § 1127. *This case cites to unpublished cases in other circuits arguably taking a different approach to plan modifications. In addition, the settlement approval standard set forth in In re Martin is also discussed by the Third Circuit in its decision in In re Jevic Holding Corp., summarized below.*

- **Marlow Manor Downtown, LLC v. Wells Fargo Bank (*In re* Marlow Manor Downtown LLC), 2015 WL 667543 (B.A.P. 9th Cir. Feb. 6, 2015).**
  Chapter 11 debtor, Marlow Manor Downtown, LLC ("Marlow"), filed a third amended plan (TAP) that classified two unsecured deficiency claims of its lender, the Alaska Housing Financing Corporation (AHFC), in class 3 and 4 as secured and unimpaired and placed them in different classes from the general unsecured creditors. Prior to confirmation, Wells Fargo Bank, as servicing agent for AHFC, made a motion seeking an order that the debtor's classification of AHFC's deficiency claims was improper because (i) the claims were unsecured and impaired and substantially similar to the claims of the general unsecured creditors and (ii) the debtor failed to provide a business justification or economic reason for the separate classification. The Bankruptcy Court granted Wells Fargo's motion, and Marlow appealed.
  The Ninth Circuit BAP found no error in the Bankruptcy Court's judgment and affirmed the granting of the motion. The BAP found, among other things, that: (i) Marlow had conceded in its opening brief that AHFC's deficiency claims were unsecured under § 506(a); (ii) Marlow failed to distinguish AHFC's deficiency claims

from garden variety unsecured claims; and (iii) Marlow failed to point to any legitimate business or economic reason for the separate classification of AHFC's deficiency claims.

- ***In re* MPM Silicones, LLC, 14-22503-rdd, 2014 WL 4436335 (Bankr. S.D.N.Y. Sept. 9, 2014), *aff'd* 2015 WL 2330761 (S.D.N.Y. May 4, 2015).**

  The lead debtor in these Chapter 11 cases, d/b/a Momentive Performance Materials, sought and obtained confirmation of its plan of reorganization after a four-day contested confirmation hearing. The two primary issues resolved by the Bankruptcy Court were (i) the appropriate calculation of interest in the cramdown context under § 1129(b) and (ii) the enforceability of a make-whole premium provision in the indenture agreement of certain senior noteholders. The Bankruptcy Court rejected a market-based approach to cramdown interest in favor of the formula approach articulated by the U.S. Supreme Court in *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004). The Bankruptcy Court also determined that the make-whole premium provision was not applicable because it was triggered only by a prepayment of the notes subject to the indenture agreement and not the acceleration of the notes in a bankruptcy case. The District Court affirmed the Bankruptcy Court's decision in all key aspects. The Bankruptcy Court's holding on the make-whole premium was followed by the Bankruptcy Court in *In re Energy Future Holdings Corp.*, *et al*., 527 B.R. 178 (Bankr. D. Del. Mar. 26, 2015). *The Bankruptcy Court's holding on the cramdown interest rate represents a circuit split.*

- **BOKF, N.A. v. JPMorgan Chase Bank, N.A. (*In re* MPM Silicones, LLC), 518 B.R. 740 (Bankr. S.D.N.Y. 2014).**

  First and second lien creditors entered into an intercreditor agreement (ICA) that, among other things, specified that second lien creditors agreed not to contest or support any other party in contesting first lien creditors' attempts to enforce their claims. Second lien creditors supported the debtor in objecting to some of the first lien creditors' claims and in proposing a cramdown plan against the first lien creditors. The first lien creditors claimed that the ICA had been violated. The Bankruptcy Court held that the second lien creditors' actions did not violate the ICA because an unsecured claimholder may support the debtor in objecting to claims or proposing a cramdown plan against a senior lienholder.

  Further, under the ICA, second lien creditors had agreed not to receive any proceeds of common collateral or rights arising out common collateral until the first lien creditors' lien claims were paid. Under the plan of reorganization, the second lien creditors were to receive all of the reorganized debtor's stock. The first lien creditors claimed that the ICA had been violated for this reason as well. The Bankruptcy Court held that the ICA allowed the second lien creditors to take any action available to them as holders of unsecured claims, and given that the stock was available to them because of their claims and not because of the common collateral held with the first lien creditors, the plan did not violate the ICA.

Recent Case Developments
Business Cases

Employee Agreement with Debtor

- **Schuller v. Naylor, No. 14-945, 135 S.Ct. 1715 (U.S. 2015) (case below 584 Fed.Appx. 307).**

  The Supreme Court denied the petition for *writ of certiorari*.

  Dr. Robert H. Schuller (the Crystal Cathedral's founding pastor) entered into a Transition Agreement to address his transition from his position as Senior Pastor and define his future relationship with the church, prior to the church entering bankruptcy. The Bankruptcy Court found that Dr. Schuller's relationship to the church under the Transition Agreement was that of an employee and thus his claim under the agreement was limited by § 502(b)(7). The District Court and the Ninth Circuit affirmed the Bankruptcy Court's ruling that the claim of the former pastor of the debtor church was a claim for damages resulting from termination of an employment agreement and thus limited in amount by § 502(b)(7). The case and decisions of the lower courts discuss interesting issues in characterizing an agreement as one for employment that is subject to the § 502(b)(7) cap rather than a retirement agreement that would not be so limited.

- **Commercial Law Corp. PC v. FDIC, 777 F.3d 324 (6th Cir. Jan. 27, 2015).**

  Commercial Law Corporation, P.C. ("CLC") sued the FDIC in its capacity as receiver for a bank, claiming $176,750 in unpaid attorneys' fees for legal services rendered to the bank in 2008 and 2009. The District Court granted the FDIC's motion for summary judgment, holding that 12 U.S.C. §§ 1821(d)(9)(A) and 1823(e)(1) precluded enforcement of CLC's unrecorded fee agreement with the bank. These statutes codify the common law *D'Oench* doctrine, which is an estoppel rule similar to the statute of frauds that shields the FDIC from claims and defenses based on unwritten agreements that reduce bank assets. *See D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 455-62 (1942); *First State Bank of Wayne Cnty. v. City & Cnty. Bank of Knox Cnty.*, 872 F.2d 707, 715-16 (6th Cir. 1989).

  CLC appealed and argued that *D'Oench* and its statutory progeny do not apply to its legal services arrangement with the bank. The Sixth Circuit agreed with CLC and reversed the District Court's order. The Circuit Court noted that *D'Oench* has been found to apply to a bank's lending activities but does not compel application of *D'Oench* to non-banking services purchased by the bank.

Equitable Title Primacy over Tax Liens

- **Susquehanna Bank v. United States, IRS (*In re* Restive Auto Body, Inc.), 772 F.3d 168 (4th Cir. Md. 2014).**

  Restive Auto Body, Inc. ("Restive") borrowed $1 million from Susquehanna Bank and secured repayment of the loan by executing and delivering to the Bank a deed of trust with respect to two parcels of real property. Six days later, the IRS filed notice of a federal tax lien against Restive for unpaid employment taxes. Susquehanna Bank recorded the deed of trust it had received.

  Susquehanna Bank commenced this adversary proceeding in Restive Auto Body's Chapter 11 bankruptcy case, seeking a judgment declaring that the security interest it

acquired had priority over the IRS's tax lien. The District Court granted Susquehanna Bank priority, ruling (i) that Md. Code Ann., Real Prop. § 3-201, related back Susquehanna Bank's subsequent recordation of its deed of trust to the date the deed of trust was executed and delivered, thus giving Susquehanna Bank a security interest effective before the IRS recorded its tax lien; and alternatively (ii) that Maryland common law, under the doctrine of equitable conversion, gave Susquehanna Bank a protected equitable security interest in Restive's property, regardless of recordation, when Restive executed the deed of trust in exchange for the $1 million loan before the IRS recorded its tax lien.

The Fourth Circuit rejected the District Court's holding that Md. Code Ann., Real Prop. § 3-201 gave Susquehanna Bank retroactive priority over the IRS, concluding that 26 U.S.C. § 6323(h)(1)(A)'s use of the present perfect tense precludes giving effect to Real Prop. § 3-201's relation-back provision. The Circuit Court nonetheless affirmed the judgment of the District Court on the ground that under Maryland common law, Susquehanna Bank acquired an equitable security interest in the two parcels of real property on the date it received the deed of trust, regardless of recordation, because its interest became "protected . . . against a subsequent lien arising out of an unsecured obligation" on that date and that therefore its security interest had priority over the IRS's tax lien under 26 U.S.C. § 6323(a) and § 6323(h)(1).

<u>*Evidentiary Claims*</u>

- **Curtis v. Perkins (*In re* International Management Associates, LLC), 781 F.3d 1262, 2015 WL 1245503 (11th Cir. Mar. 19, 2015).**

  The defendants in this case appealed the Bankruptcy Court's decision that allowed the bankruptcy trustee of International Management Associates ("IMA") to avoid a $200,000 transfer from the debtor, IMA, to the defendants. IMA was an alleged "hedge fund" that was investigated in connection with a suspected Ponzi scheme. The defendants invested $500,000 with IMA. The Bankruptcy Court found that IMA was a Ponzi scheme and the defendants and the trustee stipulated to the fact that IMA's last disbursement to the defendants was a $200,000 transfer made 65 days before IMA's bankruptcy petition was filed. The Bankruptcy Court entered judgment allowing the trustee to avoid the $200,000 transfer from IMA to the defendants.

  The defendants appealed the judgment challenging the admissibility of evidence entered by the trustee. The Eleventh Circuit found that the summaries used by the trustee, which were based on underlying documents and used to prove the truth of the information contained in those documents, were properly admitted into evidence since the underlying documents would have been admissible as business records and the Bankruptcy Court did not abuse its discretion by admitting the summaries into evidence. The court held that the Bankruptcy Court's finding that IMA was a Ponzi scheme was not clearly erroneous.

Recent Case Developments
Business Cases

Fiduciary Duties of Insolvent Debtor

- ***In re* Lemington Home for the Aged, 777 F.3d 620 (3d Cir. Jan. 26, 2015).**

  The plaintiffs alleged breach of fiduciary duty and deepening insolvency claims against certain of the debtor's officers and directors for, among other things, mismanagement of the debtor, which operated a nursing home, prior to the Chapter 11 case. On the third appeal to the Third Circuit in this particular case, the Circuit Court affirmed the jury's liability findings against the defendants on the breach of fiduciary duty and deepening insolvency claims. With respect to the latter, the Circuit Court cited its holding in *Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co.* that predicted Pennsylvania would recognize a cause of action for deepening insolvency. *See Lafferty*, 267 F.3d 340, 349 (3d Cir. 2001) ("Even when a corporation is insolvent, its corporate property may have value," which can be damaged by "[t]he fraudulent and concealed incurrence of debt . . . ."). The Circuit Court reversed and remanded part of the punitive damages award granted in connection with the jury verdict. *This issue represents a case law split, as some jurisdictions have not recognized deepening insolvency as a viable, separate cause of action.*

- **Lightsway Litig. Servs., LLC v. Yung (*In re* Tropicana Entm't, LLC), 520 B.R. 455, (Bankr. D. Del. 2014).**

  The Chapter 11 debtors were hotels and casinos that were owned and controlled by William Yung, III, through a holding company structure. Two other entities controlled by Yung filed motions for allowance and payment of administrative expense claims against the debtors, and the unsecured creditors' committee objected to those claims. The postconfirmation litigation trustee then filed a complaint against Yung (and the two related entities) asserting claims for breach of fiduciary duties, breach of contract, breach of the implied covenant of fair dealing, and equitable subordination. The defendants filed a motion to dismiss the complaint and, after a hearing, the court entered an order denying the motions to dismiss, but directing the trustee to file an amended complaint. The trustee filed an amended complaint, and the defendants again moved to dismiss.

  The primary issue in the case involved whether Yung had breached a fiduciary duty. The court cited *North American Catholic Educ. Programming Found, Inc. v. Gheewalla*, 930 A.2d 92, 101-102 (Del. 2007) for the proposition that "the creditors of an insolvent corporation have standing to maintain derivative claims against the directors on behalf of the corporation for breaches of fiduciary duties" in recognizing that the confirmed plans transferred to the litigation trustee any right of the debtors to pursue claims against insiders. Still the court found that Yung was obligated to manage the solvent debtor subsidiaries in the best interests of the parent corporation, and—ultimately—himself, as the sole shareholder of the parent. The Bankruptcy Court granted the defendant's motion in part and dismissed the claim.

Recent Case Developments
Business Cases

Involuntary Cases

- **DVI Receivables XIV, LLC v. Rosenberg (*In re* Rosenberg), 779 F.3d 1254 (11th Cir. Feb. 27, 2015).**

  DVI Receivables, among other entities ("DVI Entities"), filed an involuntary Chapter 7 petition against Rosenberg in connection with a limited guaranty that Rosenberg had made in connection with some medical equipment leases. The evidence before the court suggested that Lyon Financial Services, Inc. ("Lyon"), a successor servicer of the DVI Entities, had actually filed the petition on behalf of each DVI Entity. Lyon was not, however, named as a petitioning creditor. In fact, no evidence showed that the DVI Entities were aware of the filing. The Bankruptcy Court dismissed the petition finding that the DVI Entities were not the real parties in interest and did not have standing to file an involuntary petition against Rosenberg. The Bankruptcy Court awarded attorney's fees and costs to Rosenberg.

  Rosenberg filed a 11 U.S.C. § 303(i) adversary proceeding against the DVI Entities and Jane Fox (who signed for Lyon). One issue on appeal was whether Lyon was an actual petitioner that could be held liable under § 303(i)(1), and the Eleventh Circuit did not overturn the Bankruptcy Court's order imposing liability. Another issue involved the categories of fees covered by § 303(i)(1). The Eleventh Circuit reasoned that when the preconditions of § 303(i)(1) are met, a Bankruptcy Court is not limited to granting only those attorney's fees incurred in the Bankruptcy Court and nothing "precludes appellate fees or limits fees to only those incurred before the date of dismissal." *(The court noted that its ruling was opposite of that of the only other circuit to rule on the issue which interpreted § 303(i)(1) to preclude the Bankruptcy Court from awarding any appellate fees. See Higgins v. Vortex Fishing Sys., Inc., 379 F.3d 701, 708-09 (9th Cir. 2004)).*

Jurisdiction / Standing to Appeal

- **O&S Trucking, Inc. v. Mercedes Benz Financial Services USA (*In re* O&S Trucking, Inc.), 2015 WL 1528302 (B.A.P. 8th Cir. 2015).**

  O&S Trucking, a Chapter 11 debtor, appealed the Bankruptcy Court's order confirming the debtor's third amended plan and two separate orders determining the secured status of claims asserted by creditor, Mercedes Benz. The BAP observed that the two claims-related orders were interlocutory and not final orders subject to appeal. Turning to the only final order—the confirmation order—the BAP noted that despite appealing the confirmation order, the debtor did not allege any error in that order. Rather, the debtor sought review of the Bankruptcy Court's valuation and adequate protection determinations that were indirectly related to the plan. Since O&S Trucking's proposed plan was confirmed, the BAP held, among other things, that O&S Trucking did not have standing to appeal the confirmation order because the debtor was not an aggrieved party. The BAP dismissed O&S Trucking's appeal for lack of jurisdiction.

Recent Case Developments
Business Cases

- ***In re* Fisher Island Inv.'s, 2015 WL 729689 (11th Cir. Feb. 20, 2015).**

  Creditors commenced these cases by filing involuntary Chapter 11 petitions against the alleged debtors. Two competing ownership groups attempted to represent the alleged debtors in responding to the involuntary petitions—the Redmond group and the Zelster group. The Bankruptcy Court ultimately identified the Redmond group as the authorized representatives of the alleged debtors, and the Zelster group appealed. Among the issues on appeal was whether the Bankruptcy Court had authority to resolve the ownership issues. Specifically, Zelster relied on the Supreme Court's decision in *Stern v. Marshall* to argue that the Bankruptcy Court lacked authority to enter final orders on the various ownership issues in the cases.

  The Eleventh Circuit affirmed the lower courts' decisions, including the extent of the Bankruptcy Court's authority to determine by final order the ownership issues. The Eleventh Circuit methodically walked through Zelster's comparison of the tortious interference claim in *Stern* and the ownership issues involved in the case before it. It observed that "[t]he ownership issue does not simply have 'some bearing' on the bankruptcy proceedings…. Rather, for the reasons explained above, the bankruptcy court could not undertake the bankruptcy proceedings without first determining who owned the Alleged Debtors, and thus who represented them, and ultimately whether the bankruptcy was contested or uncontested. *See* Katchen, 382 U.S. at 329-30, 86 S. Ct. at 472-73 (affirming the bankruptcy court's authority because the referee could not rule on the creditor's proof of claim without first resolving the voidable preference issue)."

- **Wellness International Network, Ltd. v. Sharif, 135 S. Ct. 1932 (May 26, 2015).**

  In *Wellness*, the eventual debtor Sharif had been subject to a judgment as a sanction for failure to engage in discovery in an unrelated civil suit. Sharif then filed for Chapter 7 bankruptcy. His judgment creditors filed an adversary complaint seeking to prevent discharge of Sharif's debts based on § 727 and also sought a declaratory judgment that a nonparty trust (for which Sharif was allegedly the trustee) was actually the debtor's alter ego in order to establish grounds for denying discharge. Debtor again failed to adequately comply with court ordered discovery and the Bankruptcy Court entered a default judgment in the creditors' favor, also awarding attorney's fees. After the Bankruptcy Court order, but before the briefing on appeal in the District Court, the Supreme Court decided *Stern v. Marshall*, 131 S. Ct. 2594 (2011). The debtor did not challenge the Bankruptcy Court's authority to enter final judgment on the alter ego claim in his opening brief to the District Court, although debtor did later file a motion for supplemental briefing in the District Court so he could advance a *Stern* argument in regard to the alter ego claim. The District Court held that the motion was untimely, that the debtor's *Stern* objection was waivable, and that the debtor's failure to raise it earlier constituted waiver, ultimately affirming the Bankruptcy Court's decision. The Circuit Court reversed in part, holding that (1) a constitutional objection based on *Stern* is not waivable and (2) that the Bankruptcy Court lacked constitutional authority to enter a final judgment on the state law based alter-ego claim.

  The U.S. Supreme Court granted *certiorari* in regard to these two issues. The Supreme Court ultimately held that "Article III permits Bankruptcy Courts to decide Stern claims submitted to them by consent." Slip op. at 20. In addition, the Supreme

Court determined that consent "need not be express" but may be based on "actions rather than words." Slip op. at 18-19. The Court reversed and remanded the case.

Parol Evidence Rule

- **State Bank of Toulon v. Covey (*In re* Duckworth), 776 F.3d 453 (7th Cir. 2014).**

  The issue in this case involved whether a secured lender can use parol evidence against a bankruptcy trustee to save a security agreement from a mistaken description of the debt to be secured. The security agreement stated that the collateral secured a promissory note made on a given date, but the date was a mistake. The borrower had executed a promissory note but two days after the stated date.

  The Seventh Circuit ruled that the lender in this case was not entitled to use parol evidence and reformation against the bankruptcy trustee to correct the mistaken description of the debt to be secured. The Circuit Court held that the security agreement did not give the lender a security interest in the specified collateral that could be enforced against the trustee, and that the trustee could avoid the security interest. The Circuit Court reversed the judgment of the District Court and remanded for further proceedings in the Bankruptcy Court.

Preferences & Fraudulent Transfers

- **Pyfer v. American Management Services, Inc. (*In re* National Pool Construction, Inc.), No 14-1257, 598 F. App'x. 841 (3d Cir. Apr. 2, 2015).**

  Pyfer, liquidating trustee under National Pool Constructions confirmed plan of reorganization, appealed from a District Court order affirming the Bankruptcy Court's grant of summary judgment in favor of American Management Services, Inc. ("AMS"), a former management consultant to the company. Pyfer had filed an adversary proceeding against AMS seeking to avoid and recover allegedly fraudulent transfers under the Bankruptcy Code and New Jersey's Uniform Fraudulent Transfer Act ("NJUFTA").

  Pyfer and AMS's counsel had agreed that no motion for summary judgment would be made, but after AMS made a counsel switch, the subsequent AMS counsel moved for summary judgment. The only issue Pyfer raised in response to the motion was that there had been an agreement to not make such a motion, but AMS's new counsel denied knowledge of such an agreement. The Bankruptcy Court granted summary judgment in favor of the defendant, finding that Pyfer had not contested AMS's showing that it provided reasonably equivalent value for the transfers made to AMS, and the District Court affirmed. The Third Circuit likewise affirmed, upholding the grant of summary judgment in favor of AMS.

- **Williams v. FDIC (*In re* Positive Health Mgmt.), 769 F.3d 899 (5th Cir. 2014).**

  The Bankruptcy Court concluded that debtor Positive Health Management made transfers to First National Bank that amounted to actual fraud under 11 U.S.C. § 548(a)(1)(A). The Bankruptcy Court allowed the recipient of the fraudulent transfers to retain all of the funds it received under the affirmative defense that it took the payments

in good faith and gave value in return. *See* 11 U.S.C. § 548(c). Williams, the trustee of the bankruptcy estate, appealed the decision. (Constructive fraud was eliminated as a viable claim since First National Bank returned "reasonably equivalent value" in the form of delaying foreclosure on a building allowing Positive Health Management to carry on its business there.)

The issue in this case was whether netting is required when a transferee gave less value to the debtor than it received. The Fifth Circuit discussed the arguable difference between a strict netting approach of the actual value exchanged and the "reasonably equivalent" value approach applied by the lower courts. The Fifth Circuit was persuaded by courts and commentators that treat the two standards as different and determined that the statute required a strict netting (or analysis of the actual value exchanged). Accordingly, the Circuit Court held that Williams, as trustee of the bankruptcy estate, was entitled to recover the difference between the payments First National Bank received and the value it gave in return. *The case law is split on this particular issue.*

- **Picard v. Ida Fishman Revocable Trust (*In re* Bernard L. Madoff Inv. Secs. LLC), 773 F.3d 411 (2d Cir. 2014).**

  This case involved the trustee for, and customers of, Bernard Madoff's Ponzi scheme that operated under the entity name Bernard L. Madoff Investment Securities LLC ("BLMIS"). Picard, the trustee for debtor BLMIS, invoked his "clawback" power and sued BLMIS customers who withdrew more from their accounts than they had invested and thus profited from Madoff's scheme.

  The issue in this appeal was whether the payments that BLMIS made to its customers are the type of securities-related payments that are shielded by § 546(e) from clawback. The District Court held that the payments were shielded, and dismissed the claims under Fed. R. Civ. P. 12(b)(6). The Second Circuit agreed and affirmed.

- **Rund v. Bank of America Corp. (*In re* EPD Inv. Co., LLC), 523 B.R. 680 (B.A.P. 9th Cir. Jan. 7, 2015).**

  Chapter 7 trustee, Rund, appealed orders granting the motions of Bank of America ("BOA") to dismiss trustee's claims of certain fraudulent transfers. The trustee sought to avoid certain transfers to BOA that occurred up to seven years prior to the debtors' petition date under § 544(b) and Cal. Civ. Code §§ 3439-3439.12. The trustee filed his complaints against BOA within the two years prescribed in § 546(a)(1)(A).

  The Bankruptcy Court found that the California fraudulent transfer statute, Cal. Civ. Code § 3439.09(c), is a statute of repose and ruled that the trustee could reach back only to those transfers occurring up to seven years prior to the filing of his complaint, not the petition date. In short, the Bankruptcy Court determined that § 546(a) has no effect on the seven-year limitations period set forth in Cal. Civ. Code § 3439.09(c); it runs concurrently with the two year statute of limitations set forth in § 546(a). The specific issue on appeal was whether 11 U.S.C.S. § 546(a) preempts a state-law fraudulent transfer statute of repose such as Cal. Civ. Code § 3439.09(c). The Ninth Circuit BAP reversed the Bankruptcy Court decision and held that so long as a state-law fraudulent transfer claim exists on the petition date, the trustee may bring the avoidance action under § 544(b), provided it is filed within the limitations period in § 546(a). The "reach back"

period is established on the petition date and encompasses all transfers within the relevant period provided by state law. *There is a split in the case law on this issue.*

- **LandAmerica Fin. Group, Inc. v. Southern Cal. Edison Co., 525 B.R. 308 (E.D. Va. 2015).**

  LandAmerica Financial Group, Inc. ("LFG") was a holding company that operated a title insurance business and other real estate transaction services, all through its operating subsidiaries. LFG held a concentration account into which the subsidiaries would deposit their cash, and in exchange LFG would cover all of the subsidiaries' expenses. After LFG filed bankruptcy, the liquidating trustee filed a complaint against Southern California Edison, Company ("SCE"), one of the subsidiary's utility providers, seeking to avoid and recover transfers from the concentration account pursuant to 11 U.S.C. §§ 544, 547, 548 and 550 and to disallow claim(s) pursuant to 11 U.S.C. § 502(d). The Bankruptcy Court granted partial summary judgment in favor of SCE.

  The primary issue on appeal was whether the Bankruptcy Court erred in determining that LFG received reasonably equivalent value in exchange for its transfers to SCE by LFG's receipt through the operation of its centralized cash management system of funds generated by its subsidiaries. The District Court noted that "the Fourth Circuit has stated that the proper focus in determining reasonably equivalent value 'is whether the *net effect* of the transaction has depleted the bankruptcy estate.'" (Citing *In re Jeffrey Bigelow Design Group, Inc.,* 956 F.2d at 485 (citations omitted)). The court thus affirmed the Bankruptcy Court's opinion and dismissed the appeal, ruling that LFG received reasonably equivalent value for the transfers and thus the trustee may not avoid the transfers.

- **Hosking v. TPC Cap. Mgmt., L.P. (*In re* Hellas Telecomm'ns (Luxembourg) II SCA), 526 B.R. 499 (Bankr. S.D.N.Y. 2015).**

  Foreign liquidators brought an unjust enrichment claim in the Bankruptcy Court to recover transfers from the debtor to its shareholders. The issue was whether § 546(e)'s safe harbor exception applies where the unjust enrichment claims are similar to the allegations of an actual fraudulent transfer, as opposed to a claim for constructive fraudulent transfer claim. The Bankruptcy Court held that the unjust enrichment claim was more like an actual fraudulent conveyance claim and thus was excepted from § 546(e)'s safe harbor.

- **Wolff v. United States, IRS (*In re* FirstPay, Inc.), 773 F.3d 583 (4th Cir. 2014).**

  This decision involved an adversary proceeding, wherein the bankruptcy trustee of a payroll-processing firm sought a judgment against the United States for payroll tax payments the firm made on behalf of its employer-clients to the Internal Revenue Service. The debtor misappropriated money from the account designated for withholding tax funds to its own use and the trustee sought to recover other payments made from the account.

  The one issue on appeal was whether the trustee in bankruptcy may reclaim as property of the debtor the approximately $28 million transferred by the debtor to the IRS during the 90 days preceding the filing of the bankruptcy petition. The Fourth Circuit

agreed with the Bankruptcy Court and the District Court that, as a matter of law, the debtor lacked an equitable interest in the funds paid over to the IRS.

- **Dietz v. Calandrillo (*In re* Genmar Holdings), 776 F.3d 961 (8th Cir. 2015).**

  Prior to Genmar filing for bankruptcy, a customer of the debtor initiated a claim for a defective boat that he had purchased from Genmar. Genmar ended up paying the customer $65,000 to satisfy a bank lien on the boat after title to the boat was transferred back to Genmar. The bankruptcy trustee brought this suit seeking recovery of the $65,000 payment from the customer as a preferential transfer.

  The issue was whether this transfer was an avoidable preference or a "contemporaneous exchange" excepted by § 547(c)(1). The Eight Circuit BAP affirmed the Bankruptcy Court's determination that the customer presented no evidence permitting a reasonable fact-finder to conclude that the parties to the settlement agreement intended a contemporaneous exchange for new value. The Eighth Circuit affirmed and noted that, without more, a debtor's repayment of a loan within 90 days of bankruptcy is an avoidable preference.

Proof of Claims

- **Pensco Trust Co. v. Tristar Esperanza Prop. (*In re* Tristar Esperanza Prop., LLC), 782 F.3d 492 (9th Cir. April 2, 2015).**

  Jane O'Donnell challenged the decisions of the Bankruptcy Court and the BAP (which affirmed) that her claim based on a minority interest in the debtor, Tristar Esperanza Properties, LLC (Tristar), was subject to mandatory subordination under the Bankruptcy Code. Before Tristar filed its petition, Tristar failed to pay O'Donnell the amount an arbitrator awarded her for the repurchase of her membership interest, and O'Donnell sought and received a money judgment for that amount in state court.

  The court said the question for purposes of § 510(b) was not whether the claim is debt or equity at the time of the petition, but rather whether the claim *arises from* the purchase or sale of a security. The court said it is clear that O'Donnell's claim arises from the sale of a security of the debtor, and therefore the Bankruptcy Court properly subordinated it. *There is a split in the case law on this issue.*

Recovery

- **Mano-Y&M Ltd. v. Field (*In re* Mortgage Store, Inc.), 773 F.3d 990 (9th Cir. 2014).**

  Mano-Y&M, Ltd. ("Mano") appealed from the judgment of the District Court holding that under 11 U.S.C. § 550 Mano was the initial transferee of $311,065.25 paid by the debtor, The Mortgage Store, Inc., in connection with the sale of a shopping plaza. Mano sold property to George Lindell, and payment for the property was wired by The Mortgage Store, Inc., which was formerly operated by Lindell and then by Lindell's daughter. The Mortgage Store subsequently filed bankruptcy and was discovered to be a Ponzi scheme. The bankruptcy trustee commenced this action, alleging that The Mortgage Store's transfer in connection with the plaza transaction was fraudulent under

11 U.S.C. §§ 544(b), 548(a)(1), and Haw. Rev. Stat. § 651C-4(a), and seeking to avoid the transfer and recoup the funds from Mano.

The Bankruptcy Court granted the trustee's motion for summary judgment, and held that the transfer was fraudulent. The Bankruptcy Court later determined that Mano was the initial transferee, rather than a subsequent transferee. Mano appealed to the U.S. District Court for the District of Hawaii, which (i) affirmed that Mano was an initial transferee, and (ii) refused to consider Mano's alternative argument that it should not be held responsible for the entire $311,065.25 amount because Mano waived the argument by not raising it in the Bankruptcy Court. Mano appealed and the Ninth Circuit affirmed, holding that the District Court did not err in determining that Mano was the initial transferee of the disputed funds and in declining to address Mano's alternative argument because it was waived.

The Ninth Circuit ruled that, in the absence of a statutory definition of "initial transferee," the court should apply the "dominion test" to determine whether a party is the initial transferee. *Universal Serv. Admin. Co. v. Post-Confirmation Comm. of Unsecured Creditors of Incomnet Commc'n Corp. (In re Incomnet)*, 463 F.3d 1064, 1071 (9th Cir. 2006). "Under the dominion test, a transferee is one who . . . has dominion over the money or other asset, the right to put the money to one's own purposes." *Id*. at 1070 (9th Cir. 2006) (quoting *Abele v. Modern Fin. Plans Servs., Inc. (In re Cohen)*, 300 F.3d 1097, 1102 (9th Cir. 2002)) (internal quotation marks omitted). Key in the dominion test is "whether the recipient of funds has legal title to them" and whether the recipient has "the ability to use [the funds] as he sees fit." *Id*. at 1071.

Structured Dismissals

- ***In re* Jevic Holding Corp., 787 F.3d 173, 2015 WL 2403443 (3d Cir. May 21, 2015).**

The debtor's trucking company declined significantly and essentially ceased operations prior to the Chapter 11 case. The debtor sold substantially all of its assets under § 363(b) of the Bankruptcy Code. The Chapter 11 case was litigious, but eventually the secured creditor and unsecured creditors' committee reached a settlement that, among other things, provided for the payment of certain administrative claims, a small payment to unsecured creditors, releases of certain claims among the parties, and the dismissal of the Chapter 11 case. The Bankruptcy Court approved the settlement, and creditors holding WARN claims against the estate and the U.S. Trustee appealed. The Third Circuit affirmed the Bankruptcy Court's approval of the settlement. In reaching its holding, the Circuit Court noted that "bankruptcy courts may deviate from the priority scheme of § 507 of the Bankruptcy Code only if they have 'specific and credible grounds to justify [the] deviation.'" (Citing *In re Iridium Operating LLC*, 478 F.3d 452, 466 (2007).) *So-called structured dismissal orders raise a number of issues, including the standard for approving settlements, the propriety of gifting and deviations from bankruptcy priorities, and the permissibility of third-party releases; courts are divided on several of these issues.*

Recent Case Developments
Business Cases

Trademark Licenses

- ***In re* Trump Entertainment Resorts, Inc., 526 B.R. 116 (Bankr. D. Del. Feb. 20, 2015).**

  In the most recent Chapter 11 case filed by Trump Entertainment Resorts, Inc., Trump AC Casino Marks, LLC (the "Licensor") moved for relief from the automatic stay under § 362(d) to terminate its trademark license agreement with the debtor/licensee. The Licensor argued that the trademark license was not assignable under §§ 365(c)(1) and (f)(1) because applicable law deemed the agreement nonassignable without the licensor's consent. The Licensor argued, in turn, that under the Third Circuit's holding in *In re West Elecs. Inc.,* 852 F.2d 79 (3d Cir. 1988), this nonassignability was "cause" to lift the automatic stay under § 362(d). The primary issue addressed by the Bankruptcy Court was whether a trademark license agreement could be deemed nonassignable within the meanings of §§ 365(c)(1) and (f)(1). The Bankruptcy Court answered this question in the affirmative, holding that applicable law (federal trademark law) makes a trademark license agreement nonassignable without the licensor's consent. *The use of the "hypothetical test" (as articulated in West Electronics) rather than the "actual test" to analyze contracts under § 365(c)(1) represents a circuit split. In addition, courts tend to take different approaches to the treatment of trademark license agreements under the Bankruptcy Code.*

Trustee Compensation

- **Tamm v. United States Trustee (*In re* Hokulani Square, Inc.), 776 F.3d 1083 (9th Cir. 2015).**

  Bradley Tamm, the Chapter 7 trustee for the estate of Hokulani Square, Inc., negotiated the sale of a set of debtor's condominiums to two of the debtor's secured creditors. The secured creditors paid for the property through a credit bid (and the estate's debt was reduced by the amount of the bid). The issue in this case involved whether the trustee has any claim to compensation for his services in arranging the sale since the buyers paid through a credit bid.

  The Ninth Circuit held that, "section 326(a) does not permit a trustee to collect fees on a credit bid transaction in which the trustee disburses only property, not 'moneys,' to the creditor. *Other courts of appeal have reached the same conclusion and we find no basis for creating a circuit conflict*." (Emphasis added.)

Tender Offers

- **Del. Trust Co. v. Energy Future Intermediate Holdings, LLC (*In re* Energy Future Holding Corp.), 527 B.R. 157 (D. Del. 2015).**

  Debtors settled with its first lien noteholders ("First Lien Settlement") through a tender offer to all first lien noteholders. The tender offer proposed to exchange the existing notes for new debt obligations to be issued under a $5.4 billion DIP Financing Facility. The tender offer compensated the noteholders with new value of 105% of their

outstanding principal and 101% of the accrued interest. Under the terms of the agreement, the noteholders agreed to release certain disputed make-whole claims.

The Bankruptcy Court approved the First Lien Settlement under Federal Rule of Bankruptcy Procedure 9019, and the Delaware Trust Company appealed the approval arguing that the settlement provided a disparate effective recovery on the make-whole claims of different classes (i.e., 6 7/8% and 10%) of noteholders.

The District Court affirmed the Bankruptcy Court, holding that: (i) the Bankruptcy Court did not commit legal error by approving the First Lien Settlement; (ii) debtors' use of the tender offer to propose the First Lien Settlement was not improper; (iii) the First Lien Settlement's disparate treatment of the disputed make-whole claims of the 6 7/8% noteholders and the 10% noteholders did not violate 11 U.S.C. § 1123(a)(4); and (iv) the First Lien Settlement did not constitute a *sub rosa* plan.

Third Party Releases/Valuation

- **Iberiabank v. Geisen (*In re* FFS Data, Inc.), 776 F.3d 1299 (11th Cir. 2015).**

  Iberiabank's predecessor made a $10.6 million loan to Siena Real Estate Associates, LLC ("Siena") for a build out of a building that FFS leased from Siena. Giesen and FFS each guaranteed the loan. Giesen was the 100% shareholder of FFS and owned a 48% interest in Siena. Siena was in default under the loan when FFS filed for Chapter 11 bankruptcy protection in December 2009. Iberiabank became a general unsecured creditor in FFS's bankruptcy, based on FFS's guaranty, and Iberiabank filed a claim in the bankruptcy case for the full amount of the loan. To resolve the claim, FFS and Iberiabank entered into a settlement agreement, under which the creditors agreed to a "general release" of Giesen. The Bankruptcy Court approved the plan, and Iberiabank moved for a determination of its claims against Giesen. The Bankruptcy Court held that every creditor of FFS had given a general release to Giesen. Iberiabank appealed the District Court's decision affirming the Bankruptcy Court's order that Iberiabank's claims against Giesen were released, arguing that the personal guaranty was not released.

  The Eleventh Circuit held that the release of Giesen's guaranty was an integral part of the bankruptcy order and the plan because Giesen received the release as consideration for his release of over $1 million in claims held against the debtor and his personal contribution of $750,000 to the bankruptcy estate. To reach its holding, the Circuit Court examined the doctrine of res judicata in the plan confirmation context, noting that "[a] bankruptcy court's confirmation order that is final and no longer subject to appeal becomes 'res judicata to the parties and those in privity with them.'" (Citing *Travelers Indemnity Co. v. Bailey,* 557 U.S. 137, 152, 129 S.Ct. 2195, 174 L.Ed.2d 99 (2009) (quotations omitted)). *It also declined to follow a more exacting test for res judicata articulated by the Fifth Circuit.*

- **SE Property Holdings, Inc. v. Seaside Engineering & Surveying, Inc. (*In re* Seaside Engineering & Surveying, Inc.), 780 F.3d 1070 (11th Cir. Mar. 12, 2015).**

  The debtor Seaside filed for Chapter 11 protection and, under its Chapter 11 plan, reorganized into a new entity called Gulf Atlantic. A lender of the wholly owned subsidiaries of Seaside purchased an equity interest in Seaside through a Chapter 7 case

of one of the guarantors. That lender appealed the confirmation of the debtor's plan because the lender was not made an equity holder in the reorganized debtor.

The ultimate issue was whether the Bankruptcy Court was correct to confirm (and the District Court to affirm) the Second Amended Plan of Reorganization valuing Seaside at $200,000. The key sub-issue was whether the Bankruptcy Court improperly valued Seaside under a forced-sale analysis as opposed to a going-concern analysis.

The court held that the Bankruptcy Court was correct to confirm the reorganization plan, which included releases of claims against non-debtor parties (commonly called "third-party releases" or "bar orders"). *See In re Munford*, 97 F.3d 449 (11th Cir. 1996) (holding that § 105(a) provided authority for the Bankruptcy Court to enter a bar order where the settling defendant provided funds for the bankruptcy estate, and where the Bankruptcy Court found that the bar order was fair and equitable). The court also held that the Bankruptcy Court was correct to value Seaside using a going-concern analysis. *Circuit courts are split on the permissibility of, and standard for reviewing, third-party releases.*

Termination Statement

- **Official Comm. of Unsecured Creditors of Motors Liquidation Co. v. JPMorgan Chase Bank, N.A. (*In re* Motors Liquidation Co.), 777 F.3d 100 (2d Cir. 2015).**

The debtor, General Motors, entered into a synthetic lease financing transaction ("Synthetic Lease"), and later, a separate term loan facility ("Term Loan") with JPMorgan serving as the administrative agent for each. JPMorgan filed UCC-1 financing statements to perfect the lenders' security interests in the collateral. "One such financing statement, the 'Main Term Loan UCC-1,' was filed with the Delaware Secretary of State and bore file number '6416808 4. It 'covered, among other things, all of the debtors' equipment and fixtures at 42 manufacturing facilities'" and was considered the most important of the financing statements filed in connection with the Term Loan. The debtor subsequently asked its counsel to prepare documents to facilitate the repayment of the Synthetic Lease and release the related security interests. When counsel prepared a closing checklist of the actions required to unwind the Synthetic Lease, "it identified the Main Term Loan UCC-1 for termination alongside the security interests that actually did need to be terminated. When debtor's counsel prepared draft UCC-3 statements to terminate the three security interests identified in the Closing Checklist, it prepared a UCC-3 statement to terminate the Main Term Loan UCC-1 as well as those related to the Synthetic Lease."

The mistake went undetected. General Motors paid off the Synthetic Lease. "All three UCC-3s were filed with the Delaware Secretary of State, including the UCC-3 that erroneously identified for termination the Main Term Loan UCC-1, which was entirely unrelated to the Synthetic Lease." The Circuit Court found that even though the bank never intended to terminate the Main Term Loan UCC-1, the bank authorized the filing of a UCC-3 termination statement that had that effect. The authorization, and not the intent to authorize, was all that was needed to terminate the Main Term Loan UCC-1.

Recent Case Developments
Business Cases

TIA Violations

- **Meehancombs Global Credit Opportunities Funds, LP v. Caesars Entm't Corp., 2015 WL 221055 (S.D.N.Y. Jan. 15, 2015).**

  The plaintiffs, holders of certain notes issued by Caesars Entertainment Operating Company, Inc. ("CEOC") pursuant to indentures, alleged that the issuance of supplemental indentures in August 2014 (the "August 2014 Transaction")—guaranteed by Caesars Entertainment Corporation ("CEC"; together with CEOC, "Caesars")—violated the Trust Indenture Act of 1939 ("TIA") and breached the governing indentures as well as the implied covenant of good faith and fair dealing. Plaintiffs contended that the August 2014 Transaction removed the guarantees given by the asset-rich parent company, CEC, leaving plaintiffs and the other bondholders with a worthless right to collect principal and interest from the issuer, CEOC, a company divesting itself of assets and holding approximately $17 billion of senior secured debt. The crux of plaintiffs' allegations was that the release of the guarantees effected a non-consensual change to plaintiffs' payment rights and affected plaintiffs' practical ability to recover payment in violation of § 316 of the TIA and the governing indentures.

  The court held that the plaintiffs had stated a claim under § 316(b) of the TIA sufficient to survive the defendants' motion to dismiss. In so holding, the court rejected the argument that the TIA "protects only a noteholder's *legal* right to receive payment when due." The court in *Marblegate Asset Management et al. v. Education Management Corp*., 2014 WL 7399041 (S.D.N.Y. Dec. 30, 2014), reached a similar result.