AMERICAN BANKRUPTCY INSTITUTE

Consumer Practice Extravaganza

SCOTUS Update

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U.S. Supreme Court Update

Recent Decisions

- *Bartenwerfer v. Buckley.*
- *MOAC Mall Holdings v. Transform Holdco LLC.*
- *Lac du Flambeau Band of Lake Superior Chippewa Indians v. Coughlin.*
- *Tyler v. Hennepin County.*

Is the Debt or the Debtor's intent determinative?

- *Bartenwerfer v. Buckley*, 143 S.Ct. 665 (February 22, 2023).
- The innocent spouse rule works in tax law; does it work in bankruptcy?

Bad Debt or Bad Debtor?

- Husband and Wife (originally girlfriend) engaged in renovating and reselling real estate.
- Husband undertook the work and supervised the project.
- Wife was not involved in the work but did sign the seller disclosure forms.
- Purchaser sued both Husband and Wife for non-disclosure of defects in real estate and state court entered judgment against both. **Leaky Roof, Defective Windows, Missing Fire Escape and No Permits.**
- Husband and Wife filed Chapter 7 bankruptcy case and Purchaser filed an Adversary Proceeding against both seeking an exception to discharge under 11 U.S.C. §523(a)(2)(A).

Procedural History:

- Bankruptcy Court: Husband committed fraud; his intent is imputed to Wife based on a finding that the couple entered into a legal partnership to renovate and sell property.
- BAP: reversed and remanded non-dischargeability finding as to Wife. Bankruptcy Court must determine if Wife had the requisite intent. On remand, Bankruptcy Court entered Order denying discharge only as to Husband.
- 9th Circuit reversed, holding both parties had non-dischargeable debts.
- Purchaser appealed to SCOTUS.

Split in Circuits

Walker v. Citizens Bank Co . 726 F.2d 452 (8th Cir. 1984): proof must demonstrate or justify an inference that Debtor "knew or should have known" of fraud.

Deodati v. MM Winkler & Assoc. 239 F.3d 746, 751 (5th Cir. 2001): leading case applying the *per se*/strict liability rule:

- "[W]e hold that § 523(a)(2)(A) prevents an innocent debtor from discharging liability for the fraud of his partners, regardless whether he receives a monetary benefit."

Issue on Appeal:

- Can the intent requirement in 11 U.S.C. §523(a)(2)(A) be imputed to a co-debtor or must the Court find individual intent before excepting a debt from discharge?

Case History

- BAP relied on caselaw under which §523(a)(2)(A) barred a co-debtor from discharging debt only if he/she knew or had reason to know of the other party's fraud. *Sachan v. Huh*, 506 B.R. 257 (9th Cir. BAP 2014).
- 9th Circuit broke from the prior caselaw, relying instead on *Strang v. Bradner*, 114 U.S. 555, 5 S. Ct. 1038 (1885), which held that a debtor who is liable for her partner's fraud cannot discharge the debt in bankruptcy regardless of her own culpability.

Holding

- Language of §523(a)(2)(A) does not include an *individual* finding of intent, unlike (a)(2)(B) or (a)(2)(C).
- Per *Strang*, the fraud of one partner is imputed to all.
- Bankruptcy Court found that Wife and Husband were acting as partners in the renovation and sale of the property. Wife did not dispute that she and Husband acted as partners.
- In a unanimous opinion, Supreme Court upheld 9th Circuit, finding Wife liable because of Husband's fraud based on partnership relationship.

Take Aways

What mattered to the Court?

- The use of passive voice (remember your fourth-grade grammar class!).
- Old SCOTUS case law.
- Old Acts (e.g., Bankruptcy Act of 1867).
- Other provisions in the same section.

This decision could affect Sub V cases involving non-consensual plans. Do we need legislative reform?

Cases since *Bartenwerfer*

***In re Rassbach*, 650 B.R. 568 (Bankr. W.D. Wis. 2023)**

- Husband and Wife owned a concrete business.
- Customer sued Husband and business in state court for violation of the Wisconsin Home Improvement Trade Practices Act; customer won judgment.
- Husband and Wife filed for Chapter 7.
- Customer filed AP alleging non-dischargeability under §§523(a)(2) and (a)(6).
- Debtors filed Motion to Dismiss.

Court denied motion with respect to the 523(a)(2)(A) claim against both Husband and Wife because they both owned the company; Husband's intent could be imputed to Wife even if she lacked knowledge and involvement in Husband's business dealings.

In re Beach, 2023 WL 2780880 (Bankr. E.D. Wis. April 3, 2023)

- Husband, the sole member of an LLC, owned and operated a restaurant business.
- LLC borrowed substantial funds from a lender; Husband was guarantor.
- Wife managed the restaurant but had no ownership interest in LLC and did not sign any of the loan paperwork.
- Restaurant defaulted; Lender sued both LLC and Husband; a stipulated judgment was entered in state court against Husband and LLC.

Court found that Wife had no liability for the debt since under Wisconsin law debts of an LLC are solely owed by the LLC. No evidence Wife had any ownership of the business nor signed any loan documents; therefore, no need to determine whether an exception to discharge existed under 523(a)(2)(A) as to Wife.

Is 11 U.S.C. 363(m) Jurisdictional)?

- *MOAC Mall Holdings v. Transform, LLC.,* 143 S.Ct. 927 (April 19, 2023).
- Subject Matter Jurisdiction; or Statutory Authority?

History

- Sears Holding files for Chapter 11 relief.
- In March 2019, it sells certain assets to Transform Holdings, an entity controlled by Sears' former insider Eddie Lampert. Among the assets sold were designation rights for all of Sears' leases. Transform designated the Sears lease at Mall of America for assumption and assignment (under §365) to Transform's wholly-owned subsidiary. The base rent on this triple net lease was $10.00 per year. The wholly-owned subsidiary would ultimately find one or more subtenants or assignees. MOAC objected to the assumption and assignment, but the bankruptcy court approved it anyways.
- MOAC then asked for a stay pending appeal, but Transform argued that it was not necessary because §363(m) did not apply and Transcom would not assert its applicability. MOAC won the appeal in the U.S. District Court, but Transcom asked for a rehearing on the grounds that the Court lacked subject matter jurisdiction under 11 U.S.C. §363(m). The District Court angerly agreed. The Court of Appeals affirmed and the U.S. Supreme Court granted Cert.

Circuit Split

- Jurisdictional.
- *In re Pursuit Holdings (NY) LLC 847 F.App'x 60 (2nd Cir. 2021).*
- *In re Gilchrist* 891 F.2d 559 (5th Cir. 1990).
- Statutory or applying equitable mootness.
- *Reynolds v. Servisfirst Bank* 17 F.4th 116 (11 Cir. 2021).
- *In re Energy Future Holds Corp*. 949 (F.3d 806 (3rd Cir. 2020).
- *Trinity 83 Dev. LLC v. COLFin Midwest Funding, LLC* 917 F.3d 599 (7th Cir. 2019).
- *In re Spanish Peaks Holdings II* , LLC 872 F3d 892 (9th Cir. 2017).
- In re Brown 851 F 3 619 (6th Cir. 2017).
- *COP Coal Dev. Co. v. C.W. Mining Co*. 641 F3d 1285 (10th Cir. 2011).

Issue:

- Does 11 U.S.C. 363(m) deprive the reviewing court of subject matter jurisdiction if the appellant has failed to produce a stay pending appeal?

Controlling Law

- 11 U.S.C. 363(m) states: The reversal or modification on appeal of an authorization under subsection (b) or (c) of this section of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal.

Holding: Reversed

11 U.S.C. 363(m) does not impair the subject matter jurisdiction of the court. It only impacts the personal (and thus waivable) rights of the parties.

By contrast, subject matter jurisdiction deals with the power of the court.

11 U.S.C. 363(m) only deals with the remedies of parties.

A section is only jurisdictional if Congress explicitly says so.

What kind of relief can the Court of Appeals or District Court provide?

The Aftermath.

Open Issues

- Does 363(m) even apply to an order under 365?
- Could the court have decided this matter by holding that the appellee did not act in good faith?
  - See *EDC Holding Co.* 676 F.2d 945 (7th Cir. 1982).
- If a party puts in a requirement in an agreement that the debtor's or trustee's execution, delivery or performance is subject to a final order, is there even a need for a stay pending appeal?
  - After all, what is a "final order"? Ever heard of Rule 60(b) (Bankr. R. 9024)?
- Is putting a list of leases in a pleading in miniature type good faith?

Tribal Sovereign Immunity

- *Lac du Flambeau Band of Lake Superior Chippewa Indians v. Coughlin,* 143 S. Ct. 1689 (U.S. Supreme Court, June 15, 2023).

Facts

- A wholly owned subsidiary of recognized Indian Tribe made a pay day loan to the Debtor.
- The Debtor filed Chapter 13.
- The Tribe's lender hired a collection agency who aggressively pursued collection including chasing the Debtor into a hospital after the Debtor had a nervous breakdown.
- The Debtor sought an injunction and punitive damages against the Tribe.
- The Tribe asserted immunity.

Circuit Split

- Congress abrogated sovereign immunity.
  - *Coughlin v. Lac Du Flambeau Band of Lake Superior Chippewa Indians et. al,* 33 F.4th 600 (1st Cir. 2022).
  - *Krystal Energy Co. v. Navajo Nation* 357 F. 3d 1055 (9th Cir. 2004).
- Congress did not unequivocally express intent to abrogate sovereign immunity.
  - *In re Greektown Holdings LLC* 917 F. 3d 451 (6th Cir. 2019).
  - *Meyers v. Oneida Tribe of Indians of Wisconsin* 836 F.3d 818 (7th Cir. 2016).

Holding:

- Bankruptcy Code unequivocally abrogates the sovereign immunity of all governments, including Indian Tribes.
- 11 U.S.C. 106(a) abrogates sovereign immunity for governmental units.
- 11 U.S.C. 101(27) defines governmental unit as "the United States; State; Commonwealth; District; Territory; Municipality; Foreign State; department, agency, or instrumentality of the United States… or other foreign or domestic government."
- Does this definition include Recognized Indian Tribes?

- Justice Gorsuch dissents adopting the magic words position
- JusticeThomas concurs but states that other than the tribe, moneyed businesses owned by the tribe should not have sovereign immunity.

CONSUMER PRACTICE EXTRAVAGANZA

***Tyler v. Hennepin Cnty., Minnesota*,**

598 U.S. 631, 143 S. Ct. 1369, 215 L. Ed. 2d 564 (2023)

- 94-year old owns condominium encumbered by a $15,000 delinquent property tax bill. Country uses tax foreclosure sale to take property.
  - Minnesota process is to foreclose after a year of nonpayment, followed by a three-year period of redemption. If tax not paid, title automatically transfers to county.
- County takes title under this procedure and then sells the property for $40,000. It then asserts state law permits it to retain all $40,000, including the $25,000 excess proceeds from the sale of her condominium.
- Taxpayer alleges this was a taking of property without just compensation, in violation of the Fifth Amendment.
- Taxpayer wins. Court rebuffs arguments that she had no financial interest in the property (given other liens), and that she had "constructively" abandoned the property by not paying her taxes
- Concurrence speaks about errant discussion below of the 8th Amendment excessive fines clause.

CONSUMER PRACTICE EXTRAVAGANZA

Impact

- Constitutional Takings Clause used as tool to avoid tax sale foreclosure.
- Concurring Opinion would also include the 8th amendment prohibition on excessive fines.

Faculty

Prof. Laura N. Coordes is professor of law at Arizona State University's Sandra Day O'Connor College of Law in Phoenix. Her research focuses on bankruptcy and financial distress and includes commercial law, large corporate reorganizations, and local government finance and policy. She teaches chapter 11 bankruptcy, advanced bankruptcy, secured transactions (in person and online) and contracts. Prof. Coordes is an active ABI member and was a 202 honoree of ABI's "40 Under 40" program. She served on the board of the *American Bankruptcy Law Journal* from 2019-22 and is an Honorary Master of the Arizona Bankruptcy American Inn of Court. She also serves on the Education Committee for Credit Abuse Resistance Education (CARE). Prof. Coordes is currently serving as the Reporter for the Uniform Law Commission's Drafting Committee on Assignments for the Benefit of Creditors. She co-authored *The Law of Bankruptcy* (6th ed.). She also is a contributor to the SLoGLaw Blog and a contributing editor for *Bankruptcy Law Letter*. Before coming to the College of Law, Prof. Coordes practiced in the Business, Finance and Restructuring Department at Weil, Gotshal & Manges in New York. She received her J.D. with honors from The University of Chicago Law School, where she was a Bradley Fellow and served on *The University of Chicago Law Review*, after which she completed a legal fellowship at the Student Press Law Center.

Hon. Bruce A. Markell is the Professor of Bankruptcy Law and Practice and the Edward Avery Harriman Lecturer in Law at Northwestern University's Pritzker School of Law in Chicago. From 2013-15, he was the Jeffrey A. Stoops Professor of Law at Florida State University School of Law, and before that he was a U.S. Bankruptcy Judge for the District of Nevada, a position he had held since 2004. After law school, he clerked for then-judge Anthony M. Kennedy on the U.S. Court of Appeals for the Ninth Circuit. Before taking the bench, he practiced bankruptcy and business law in Los Angeles for 10 years (where he was a partner at Sidley & Austin) and was a law professor for 14. He is the author of numerous articles on bankruptcy and commercial law, and a co-author of four law school casebooks. Prof. Markell has been a visiting professor at, among other schools, Peking University School of Law in Beijing and Harvard Law School. He contributes to *Collier on Bankruptcy*, and is a member of *Collier*'s editorial advisory board. He also is a conferee of the National Bankruptcy Conference, a Fellow of the American College of Bankruptcy, a founding member of the International Insolvency Institute, and a life member of the American Law Institute. Prof. Markell served as a commissioner for ABI's Commission on Consumer Bankruptcy, where he served as the chair of its Case Administration and the Estate Committee. He received the Commercial Law League of America's Lawrence King Award in 2022, and in 2016, he completed a project redrafting Kosovo's bankruptcy law. He has consulted with the International Monetary Fund on insolvency-related issues (having been part of the IMF's missions to Ireland, Bosnia, Montenegro, Serbia, Belarus, Georgia and Greece). Prof. Markell received his J.D. in 1980 from the University of California at Davis, where he was editor-in-chief of its law review and a recipient of the School of Law Medal.

Ronald R. Peterson is a Of Counsel in the law firm of Jenner & Block in Chicago, where he counsels debtors, trustees, creditors, committees, landlords and secured lenders in chapter 11 cases. He also advises clients on transactional issues such as corporate restructurings. Mr. Peterson's distinguished career has been highlighted by presiding over high-stakes complex commercial cases, including that of the country's 10th largest commodities house and a $1.7 billion Ponzi scheme. A Fellow of the

American College of Bankruptcy, Mr. Peterson is a prolific lecturer and writer on bankruptcy and commercial law issues. He served on the panel of the chapter 7 trustees for the Northern District of Illinois, Eastern Division, from 1989-2021. He also served on ABI's Commission to Study the reform of Chapter 11, which submitted its report to Congress in 2014, for which he co-chaired its Avoidance Action Committee. Mr. Peterson is a member of INSOL (International Association of Restructuring, Insolvency & Bankruptcy Professionals) and, in the past, served on the board of the National Association of Bankruptcy Trustees. He recently completed his term as governor of the Commercial Law League of America. Mr. Peterson received his A.B. *cum laude* in speech and political science from Ripon College in 1970 and his J.D. in 1973 from the University of Chicago Law School.