The First Annual Connecticut Bankruptcy Conference

October 4, 2018

8:30 a.m. – 6:30 p.m.

Water's Edge Resort

Westbrook, CT

CT Bar Institute, Inc.

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NY: 7.5 CLE Credits (6.5 AOP / 1.0 Ethics)

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Lawyers' Principles of Professionalism

As a lawyer I must strive to make our system of justice work fairly and efficiently. In order to carry out that responsibility, not only will I comply with the letter and spirit of the disciplinary standards applicable to all lawyers, but I will also conduct myself in accordance with the following Principles of Professionalism when dealing with my client, opposing parties, their counsel, the courts and the general public.

Civility and courtesy are the hallmarks of professionalism and should not be equated with weakness;

I will endeavor to be courteous and civil, both in oral and in written communications;

I will not knowingly make statements of fact or of law that are untrue;

I will agree to reasonable requests for extensions of time or for waiver of procedural formalities when the legitimate interests of my client will not be adversely affected;

I will refrain from causing unreasonable delays;

I will endeavor to consult with opposing counsel before scheduling depositions and meetings and before rescheduling hearings, and I will cooperate with opposing counsel when scheduling changes are requested;

When scheduled hearings or depositions have to be canceled, I will notify opposing counsel, and if appropriate, the court (or other tribunal) as early as possible;

Before dates for hearings or trials are set, or if that is not feasible, immediately after such dates have been set, I will attempt to verify the availability of key participants and witnesses so that I can promptly notify the court (or other tribunal) and opposing counsel of any likely problem in that regard;

I will refrain from utilizing litigation or any other course of conduct to harass the opposing party;

I will refrain from engaging in excessive and abusive discovery, and I will comply with all reasonable discovery requests;

In depositions and other proceedings, and in negotiations, I will conduct myself with dignity, avoid making groundless objections and refrain from engaging I acts of rudeness or disrespect;

I will not serve motions and pleadings on the other party or counsel at such time or in such manner as will unfairly limit the other party's opportunity to respond;

In business transactions I will not quarrel over matters of form or style, but will concentrate on matters of substance and content;

I will be a vigorous and zealous advocate on behalf of my client, while recognizing, as an officer of the court, that excessive zeal may be detrimental to my client's interests as well as to the proper functioning of our system of justice;

While I must consider my client's decision concerning the objectives of the representation, I nevertheless will counsel my client that a willingness to initiate or engage in settlement discussions is consistent with zealous and effective representation;

Where consistent with my client's interests, I will communicate with opposing counsel in an effort to avoid litigation and to resolve litigation that has actually commenced;

I will withdraw voluntarily claims or defense when it becomes apparent that they do not have merit or are superfluous;

I will not file frivolous motions;

I will make every effort to agree with other counsel, as early as possible, on a voluntary exchange of information and on a plan for discovery;

I will attempt to resolve, by agreement, my objections to matters contained in my opponent's pleadings and discovery requests;

In civil matters, I will stipulate to facts as to which there is no genuine dispute;

I will endeavor to be punctual in attending court hearings, conferences, meetings and depositions;

I will at all times be candid with the court and its personnel;

I will remember that, in addition to commitment to my client's cause, my responsibilities as a lawyer include a devotion to the public good;

I will endeavor to keep myself current in the areas in which I practice and when necessary, will associate with, or refer my client to, counsel knowledgeable in another field of practice;

I will be mindful of the fact that, as a member of a self-regulating profession, it is incumbent on me to report violations by fellow lawyers as required by the Rules of Professional Conduct;

I will be mindful of the need to protect the image of the legal profession in the eyes of the public and will be so guided when considering methods and content of advertising;

I will be mindful that the law is a learned profession and that among its desirable goals are devotion to public service, improvement of administration of justice, and the contribution of uncompensated time and civic influence on behalf of those persons who cannot afford adequate legal assistance;

I will endeavor to ensure that all persons, regardless of race, age, gender, disability, national origin, religion, sexual orientation, color, or creed receive fair and equal treatment under the law, and will always conduct myself in such a way as to promote equality and justice for all.

It is understood that nothing in these Principles shall be deemed to supersede, supplement or in any way amend the Rules of Professional Conduct, alter existing standards of conduct against which lawyer conduct might be judged or become a basis for the imposition of civil liability of any kind.

--Adopted by the Connecticut Bar Association House of Delegates on June 6, 1994

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Be a Part of the First Annual Connecticut Bankruptcy Conference

Get a critical overview of changes in the **Local Bankruptcy Rules** from **Connecticut's Bankruptcy Court judges**.

Learn about **best practices** and **ethical considerations** in both **commercial** and **consumer bankruptcy** from top practitioners.

You Will Learn

- About the new Local Bankruptcy Rules
- The latest on consumer bankruptcy
- About the risks, benefits, and strategic considerations in Article 9 sales
- Chapter 13 updates
- About third-party releases and exculpation provisions in Chapter 11 reorganization plans
- About the issues faced by debtors, creditors, counsel, and the court in individual Chapter 11 bankruptcies, including the absolute priority rule, fiduciary duty obligations, and the role of non-debtor family members
- About not-for-profit insolvencies
- Ethical considerations for bankruptcy lawyers

Cost

(Includes electronic materials, a light breakfast, lunch, and a cocktail reception)
Commercial Law and Bankruptcy Section Member $169
CBA Member $199
Non-Member $329
Student Member $99

CLE Credit

CT: 6.5 CLE Credits (5.5 General; 1.0 Ethics)
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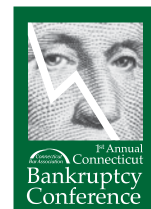
The Connecticut Bar Association/CT Bar Institute is an accredited provider of New York State CLE. This program qualifies for transitional and non-transitional credits. Financial hardship information available upon request.

Schedule

8:30 a.m. – 9:00 a.m.	**Registration**
9:00 a.m. – 9:10 a.m.	**Welcome Remarks**
9:10 a.m. – 10:10 a.m.	**The New Local Bankruptcy Rules** Hon. Julie A. Manning, Hon. Ann M. Nevins, Hon. James J. Tancredi
10:10 a.m. – 10:25 a.m.	**Break**
10:25 a.m. – 11:10 a.m.	**Consumer Bankruptcy Program** Professor Deborah Thorne
11:15 a.m. – 12:15 p.m.	**Article 9 Sales** Elizabeth J. Austin, William S. Fish, Jr., Eric A. Henzy, Scott D. Rosen
12:35 p.m. – 1:20 p.m.	**Luncheon** *Sponsored by* *Keynote Speaker: Bill Rochelle, American Bankruptcy Institute*
1:30 p.m. – 2:45 p.m.	**Concurrent: Chapter 13 Updates** Carl T. Gulliver, Charles A. Maglieri, Eugene S. Melchionne, Roberta Napolitano **Concurrent: Third-Party Releases** Hon. Robert E. Gerber, US Trustee William K. Harrington, Irve J. Goldman
2:50 p.m. – 3:50 p.m.	**Concurrent: Individual Chapter 11 Bankruptcy** Hon. Ann M. Nevins, Scott M. Charmoy, Douglas S. Skalka **Concurrent: Not-for-Profit Insolvencies** Hon. James J. Tancredi, Craig I. Lifland, Robert A. White
3:50 p.m. – 4:05 p.m.	**Break**
4:05 p.m.– 5:05 p.m.	**Ethics Presentation** Hon. Julie A. Manning, Jeffrey R. Hellman, Thomas J. Sansone, Suzanne B. Sutton
5:05 p.m. – 5:10 p.m.	**Closing Remarks**
5:10 p.m. – 6:30 p.m.	**Cocktail Reception**



Faculty Biographies

Elizabeth J. Austin is a member and chair of the Bankruptcy Section of Pullman & Comley's Litigation Department. Her practice consists of the representation of financial institutions, creditors'committees, debtors and trustees in both reorganizations and liquidations and related bankruptcy court litigation.

Prior to rejoining Pullman & Comley in 2006, she was the Assistant United States Trustee for the Southern District of New York, where she oversaw all Chapter 11 proceedings filed in the district including such major cases as Refco, Delta Airlines, Northwest Airlines, Delphi, Calpine and Dana Automotive. She argued crucial motions in major cases including the U.S. Trustee's motions for examiners and trustees in the Refco, Delta and Adelphia cases. She also oversaw the appointment of creditors' committees, including equity committees, in all major cases.

Prior to joining the Office of the United States Trustee, Liz was a member and chair of Pullman & Comley's Bankruptcy Section.

In her bankruptcy litigation practice, she represented major creditors in the Chapter 11 cases of three airlines; debtors and creditors' committees; official committees of working interest and royalty owners in numerous oil company bankruptcies; and debtors and creditors in real estate cases involving shopping centers, apartment complexes and office buildings.

In addition to her bankruptcy experience, Liz has considerable trial experience in federal court.

Liz has written on many aspects of bankruptcy law. Most recently she was a contributing author and editor to *Examiners in Bankruptcy Cases: A Guide for Examiners, Courts and Practitioners, 2013-2014 Edition,* published by Thomson Reuters Westlaw. Liz also wrote a case study titled "Alternatives to Bankruptcy for Insolvent Nursing Homes," published by the *American Bankruptcy Institute Law Review*, and on matters related to bankruptcy fraudulent transfer avoidance, the bankruptcy collection process, bankruptcy ethics and the Bankruptcy Reform Act of 1994. She has lectured on bankruptcy law before numerous professional groups.

Scott M. Charmoy is a partner at Charmoy & Charmoy with offices in Fairfield and Stamford. His practice focuses on debtor and creditor representation in consumer and business bankruptcy cases and on commercial, business, and civil litigation, including foreclosure defense.

Scott is an active member of the Connecticut and Greater Bridgeport Bar Associations. He has lectured numerous times for the Connecticut Bar Association on bankruptcy matters and has written numerous articles for the Greater Bridgeport Bar Association newsletter. He has testified as an expert on bankruptcy matters. Scott is the current Connecticut State Chair for the National Association of Consumer Bankruptcy Attorneys (NACBA). He has also served on the Town of Trumbull Board of Assessment appeals from 2004 to 2016 and is currently an alternate on the Town of Easton Board of Assessment Appeals and Zoning Board of Appeals. He is a James W. Cooper Fellow.

Scott graduated from Duke University in 1992 and from Washington University School of Law in 1995.

William S. Fish is a partner at Hinckley Allen. Bill's practice spans across a broad range of legal disciplines including business services, complex commercial litigation, bankruptcy and creditors' rights, real estate, and the First Amendment. He has tried numerous complex matters in state and federal court and regularly represents clients in complex bankruptcy proceedings, acquisitions, real estate transactions, loan transactions, and other

business matters throughout the country. Bill also represents clients in cross-border and other international transactions. He acts as general counsel to a broad range of clients, providing legal advice on a variety of business topics. He also counsels clients on how best to structure joint ventures and other related matters. He also regularly represents clients regarding the acquisition, re-development, financing, sale, and operation of all types of senior housing facilities.

He was selected by Best Lawyers as the Lawyer of the Year (Hartford region) in 2018 for Bet-the-Company Litigation, Lawyer of the Year (Hartford region) in 2015-2017 for Litigation – Bankruptcy and Lawyer of the Year (Hartford region) in 2011 for Bankruptcy and Creditor Debtor Rights. He also is a Fellow in The Trial Lawyer Honorary Society of the Litigation Counsel of America.

Robert E. Gerber retired from the federal bench in January 2016, having served, for 15 years, as a United States Bankruptcy Judge in the Southern District of New York. During his tenure as a federal bankruptcy judge, he presided over a wide variety of chapter 11, chapter 7, chapter 15, section 304 and SIPA cases—including *Ames Department Stores, PSINet*, *Global Crossing, Adelphia, ABIZ, Basis Yield Alpha Fund, Lyondell Chemical, BearingPoint, DBSD North America, Chemtura, Pinnacle Airlines, Houghton-Mifflin Harcourt* and *General Motors*. Of these cases, more than 20 had over $100 million in debt, including 10 with over $1 billion in debt. He was named as one of the nation's outstanding bankruptcy judges six times.

In February 2016, he became Of Counsel to the law firm of Joseph Hage Aaronson, where he now offers services in consulting, bankruptcy and commercial expert testimony, arbitration, mediation, and as a fiduciary. He is also an Adjunct Professor of Law at Columbia Law School (where he teaches Columbia's Advanced Bankruptcy Seminar); a contributing author to *Collier on Bankruptcy*; and a Fellow (and former director) of the American College of Bankruptcy.

Irve J. Goldman has practiced in the areas of bankruptcy law and commercial litigation for more than 25 years. In 1993, Irve became one of the first attorneys in Connecticut to become a certified specialist in business bankruptcy by the American Board of Certification. He is a past chairman of the Commercial Law and Bankruptcy section of the Connecticut Bar Association, from whom he received the Service to the Profession award in 2018, a member of the Committee on revisions to the Local Bankruptcy Rules of the U.S. Bankruptcy Court for the District of Connecticut, and a 25-year member of the American Bankruptcy Institute.

Irve has represented a diversity of interests in bankruptcy proceedings, including companies reorganizing under Chapter 11, secured creditors, equipment lessors, franchisees, landlords, other creditors, and asset purchasers in section 363 sales. He has published numerous articles in the *American Bankruptcy Institute Law Journal* covering topics such as executory contracts in bankruptcy, the effect of bankruptcy on a pre-judgment attachment lien, asset-freeze injunctions, and trustee standing to assert non-bankruptcy causes of action. In 1985, he also published one of the earliest articles in Connecticut on the status of lien stripping in bankruptcy in the *Connecticut Bar Journal,* and has been a frequent contributor to the *Quinnipiac Law Review's* annual summary of decisions from the Second Circuit.

Carl T. Gulliver is a member of the New Haven-based law firm of Coan Lewendon Gulliver & Miltenberger LLC, where his practice areas include bankruptcy and personal and business reorganization. He joined the firm in 1994 having practiced in the bankruptcy area in Connecticut with DiPietro Kantrovitz & Brownstein and Andrew M. DiPietro, Jr. between 1986 and his joining Coan Lewendon. Prior to 1986 he worked with the bankruptcy boutique firm of Doctor Doctor & Salus in Washington, DC, after receiving his J.D. degree from

The George Washington University National Law Center in 1980. He graduated Ohio Wesleyan University with a B.A. in 1973.

Board-certified in business bankruptcy law by the American Board of Certification, Mr. Gulliver is also AV® Preeminent Peer Review Rated by Martindale-Hubbell®, and has been selected as a Super Lawyer by the Super Lawyer rating service each year since 2007.

He was Chairperson of the Connecticut Bar Association's Commercial Law and Bankruptcy Section from June 2012 through June 2014, and served as the Senior Topical Editor for Bankruptcy on the Association's Connecticut Bar Journal from 1998 through 2017.

William K. Harrington is the United States Trustee for Region 1 and Region 2. Mr. Harrington was appointed as the United States Trustee for Region 1 on November 8, 2010 and as the United States Trustee for Region 2 on November 26, 2013. Prior to his appointment as the United States Trustee for Region 1, Mr. Harrington was the Assistant United States Trustee for the District of Delaware. Prior to joining the Office of the United States Trustee, he practiced bankruptcy and reorganization law at Duane Morris LLP. Mr. Harrington is a member of the Boston Bar Association, the Delaware State Bar Association, the American Bar Association, the American Bankruptcy Institute, and the Delaware Bankruptcy American Inn of Court. He received his undergraduate degree from the University of Pennsylvania and his J.D. from Villanova University School of Law.

Jeffrey R. Hellman's practice is focused on the representation of individuals and businesses in complex commercial litigation. Mr. Hellman's practice regularly includes contract disputes, prosecution and defense of preference and fraudulent transfer litigation, partnership and inter-company disputes, and various types of debtor and creditor disputes. Mr. Hellman's practice also includes various types of real estate litigation including title disputes, lease disputes, and trespass actions. Mr. Hellman regularly appears in the Connecticut Superior Court, the United States District Court for the District of Connecticut, and the United States Bankruptcy Court for the District of Connecticut. Mr. Hellman has lectured to the Connecticut Bar Association and the Norton Bankruptcy Litigation Institute. Mr. Hellman has been a member of the Executive Committee of the Federal Practice Section of the Connecticut Bar Association from 1996 to the present and a member of the Section since 1989. Mr. Hellman is also a member of the Commercial Law and Bankruptcy Section of the Connecticut Bar Association.

Mr. Hellman was an Assistant District Attorney in Philadelphia, P A from 1986 to 1989.

Eric A. Henzy is a partner at Zeisler & Zeisler PC. He has extensive experience representing debtors, creditors' committees, secured and unsecured creditors, and other parties in bankruptcy cases and out-of-court workouts.

Eric has appeared in bankruptcy courts around the country and has represented parties in a number of the first hedge fund insolvencies in the country. He has first-chair tried more than thirty contested matters and adversary proceedings to judgment. Prior to joining Z&Z, Eric practiced in the bankruptcy group at Reid and Riege PC in Hartford; and previously, at the New York firm Milbank Tweed Hadley and McCloy. He also served as law clerk to the Honorable Alan H. W. Shiff, United States Bankruptcy Judge for the District of Connecticut.

Craig I. Lifland focuses on matters related to business reorganization, insolvency, workouts, creditors' rights, and general business. For more than thirty-five years, Craig has been involved in many of the largest and most complex Chapter 11 filings in the State of Connecticut. He has handled matters in numerous industries including transportation, manufacturing, retail, wholesale and distributors, construction, publishing, telecom, healthcare, medical devices, real estate development, and professional services. In connection with these industries, Craig has represented borrowers, lenders, creditors' committees, Plan Custodians / Plan Administrators, landlords, stalking horse purchasers, litigants, and virtually every conceivable constituency in bankruptcy and out-of-court restructurings.

Craig's deep and varied experience provides an acute understanding of the various leverage points of all parties to an insolvency matter and how to best take advantage of that insight. He also applies this experience to deliver valuable insight and advice to businesses and individuals in a broad range of transactions beyond insolvency matters. Craig strives to understand his clients' goals and effectively communicate options and solutions to the problem at hand. He prides himself on being responsive and efficiently handling both straight-forward and complex matters.

Craig has been a speaker and panelist on bankruptcy topics for numerous Bar Associations and professional associations.

As a result of all this, Craig has received numerous honors for his work in bankruptcy matters. He has been rated AV by the peer-reviewed legal directory, *Martindale-Hubbell* since he was rated over 25 years ago. He has been listed in *The Best Lawyers in America®* since 2006 in the area of Bankruptcy and Creditor Debtor Rights / Insolvency and Reorganization Law, Litigation - Bankruptcy. Craig was named Lawyer of the Year by Best Lawyers in 2011, 2012 and 2018 for Litigation-Bankruptcy and Bankruptcy and Creditor Debtor Rights / Insolvency and Reorganization Law. He has also been selected by *Super Lawyers®* in the areas of Creditor Debtor Rights: Business since 2007 and in 2013 and 2015 was recognized as one of Connecticut's Top Fifty Lawyers.

Attorney Charles A. Maglieri is a sole practitioner who concentrates his areas of practice in Consumer Bankruptcy Law cases and Bankruptcy related cases, loan workouts, common law compositions and arrangements and business organizations. Since 2001 Attorney Maglieri has operated his law practice under the trade name of "Advanced Bankruptcy Legal Services" maintaining two full time law office locations in Bloomfield and Brooklyn, CT. Mr. Maglieri has represented both creditors and debtors in all Chapters of Bankruptcy Law; however, since 1986, has limited his practice to representing debtors in both consumer and commercial cases.

Education: He received his B.A. Degree from Central Connecticut State University in 1977, Magna Cum Laude, having a double major in Psychology and Criminal Justice with a minor in Philosophy; he received the Department of Psychology award for Superior Academic Achievement earning him a personal referral for admission to Harvard University as a Ph.D. Candidate for Clinical Psychology. Thereafter Mr. Maglieri was awarded his Juris Doctor Degree from Western New England University, School of Law in 1981 together with the completion and approval of a Juris Doctoral Thesis on "The Nature of Legal Discourse: A Philosophical investigation into the Function and Structure of Legal Discourse". While a law student pursuing his legal studies he was a Student Instructor for Legal Writing and Research for two years, a National Moot Court Coach, Intramural Moot Court Champion and worked as a legal intern for law firms in the Hartford, Ct areas for the summer months following first and second year legal studies. Just prior to graduation from Law School Mr. Maglieri received his second personal referral for one of two open positions for a candidate to earn a Doctor of Juris Science Degree at Yale University for advanced studies in Jurisprudence.

Professional Organization Memberships, Teaching Positions and Bar Admissions: Mr. Maglieri is a member of: the Connecticut Bar Association, Commercial Law and Bankruptcy Section and serves as the current Chairperson of the Consumer Bankruptcy Law Committee; Hartford County Bar Association, Commercial Law and Bankruptcy Section; the American Bankruptcy Institute and sits on the National Advisory Board for Consumer Bankruptcy Law; National Association of Chapter 13 Trustees (NACTT), National Association Consumer Bankruptcy Attorneys (NACBA), serves as a volunteer Mediator for the Bankruptcy Court Mediation Program at Hartford and is Senior Moderator for the Consumer Bankruptcy Round Table Discussions since 1996. He has held prior teaching positions at Western New England College School of Law where he taught Law Students the Code of Professional Responsibility and an instructor at Tunxis Community College from 1982 to 1991 where he taught Criminal law, Constitutional law, and Evidence and Court Procedure.

Since 1981 Mr. Maglieri has been admitted to practice law in the State of Connecticut, Trial and Appellate Courts and the United States District Court for the District of Connecticut. In 1985 he was admitted to practice in the United State Court of Appeals, Second Circuit and later in 1986 he was admitted to practice in the Supreme Court of the United States of America, Washington D.C. In addition to the foregoing Mr. Maglieri has been a member of the Connecticut Bar Association Rules Drafting Committee and a judicially appointed member of three committees tasked with drafting the new District of Connecticut Chapter 13 Plan, Local Rules of Chapter 13 Procedure, and Local Rules of Chapter 12.

Julie A. Manning was sworn in as a United States Bankruptcy Judge for the District of Connecticut on September 9, 2013. Judge Manning became the Chief Judge of the United States Bankruptcy Court for the District of Connecticut on September 9, 2014. She maintains chambers at and presides over the Bridgeport Division of the Court.

Prior to her appointment, she was in private practice for twenty-five years, representing corporations, partnerships, financial institutions, and insurance companies in bankruptcy and commercial litigation cases throughout the United States. From 1999 until her appointment, she was a partner with the law firm of Shipman & Goodwin, LLP, where she served as Chair of the firm's Bankruptcy and Creditor Rights Group, Co-Chair of the firm's Finance and Investment Practice Group, and was a member of the firm's Partnership Review Committee and Compensation Committee. As a practicing attorney, Judge Manning was an active member of the Commercial Law and Bankruptcy Section of the Connecticut Bar Association and served on its Executive Committee. Judge Manning was also listed in the Bar Register of Preeminent Women Lawyers, was repeatedly named a "Connecticut Super Lawyer", a "New England Super Lawyer" and one of the "Best Lawyers in America" in the area of Bankruptcy and Creditor/Debtor Rights.

Judge Manning is a member of the Connecticut Bar Association, the American Bankruptcy Institute and the National Conference of Bankruptcy Judges. She serves on the Public Outreach Committee and Endowment for Education Board of the National Conference of Bankruptcy Judges.

Eugene S. Melchionne is a native of Waterbury, Connecticut and currently resides and practices there. He is an avid boater, amateur musician, and Mac User, spending every weekend on his boat with his guitar and iPad. He is a member of the Board of Directors for National Association of Consumer Bankruptcy Attorneys (NACBA). He graduated from Drake University School of Law in 1980 where he received the American Jurisprudence Award for academic excellence. In 2007, he was appointed to the Connecticut Supreme Court's Commission on Foreclosures, a role he continues in to this day. Formerly, Melchionne was Vice President of the Waterbury Credit Bureau and a member of the Northwestern Regional Council of the American Institute of Banking and

the only attorney to receive its prestigious Ken Kovel Award. He has also been repeatedly recognized by the U.S. Bankruptcy Court for Pro Bono service to indigent consumers. Gene is a long-time member of NACBA and a national speaker on bankruptcy law, consumer representation, and use of technology in the law office. He has been featured on the PBS show *NOW*, appeared on a segment of "Your Money" on CNN, and on the CBS Evening News. He has been interviewed by the *New York Times*, *Business Week*, the *Connecticut Law Tribune,* and numerous Connecticut newspapers. He has testified before the Connecticut legislature and in court as an expert in bankruptcy law issues.

Roberta Napolitano was a member of the panel of Chapter 7 Trustees for the District of Connecticut from May 1997 through September 1, 2017, when she became the acting Chapter 13 Trustee for the District of Connecticut. She was a partner and associate at Ignal Napolitano and Shapiro from October 1983 to September 1, 2018. Roberta is Vice President of the Commercial Law and Bankruptcy Section of the Connecticut Bar Association, and Treasurer of the Connecticut Chapter of the International Women's Insolvency and Reorganization Confederation. She received her J.D. from the University of Connecticut School of Law in 1982, and her A.B. in 1979 from Bryn Mawr College. Her reported cases are *Fichera v. Mine Hill Corporation*, 207 Conn. 204 (1988); *In re McNamara*, 310 B.R. 664, 666 (Bankr. D. Conn. 2004); and *In re Kujan*, 286 B.R. 216, 217 (Bankr. D. Conn. 2002).

The United States Court of Appeals for the Second Circuit appointed **Ann M. Nevins** as a United States Bankruptcy Judge on April 15, 2015. Judge Nevins graduated from the University of Michigan, Ann Arbor in 1986, and from Boston University School of Law in 1989.

After graduating from law school, Judge Nevins joined a Connecticut law firm and became an equity partner in the firm. During her time in private practice, Judge Nevins's practice included representation of – or litigation against – every type of party to a bankruptcy case, including bankruptcy debtors, creditors, corporations, lenders, and investors including hedge funds and private equity firms, banks, pension funds, unions, trade creditors, government creditors and regulatory agencies, insurance companies, and bankruptcy trustees. Judge Nevins also represented clients in complex corporate and real estate transactions, including large commercial financings, acquisitions, dispositions and development, commercial leasing, and business restructurings.

From 1999 through her appointment to the Bankruptcy Court, Judge Nevins served as an Assistant United States Attorney with the United States Attorney's Office in the District of Connecticut. She principally represented the United States in civil bankruptcy cases, but also prosecuted bankruptcy-related crimes, including bankruptcy fraud, bank fraud, and wire fraud. From 2005 to 2007, Judge Nevins served as a Senior Litigation Counsel for the United States Attorney's Office. In 2011, Judge Nevins was named the Assistant-in-Charge of the United States Attorney's Office's Bridgeport, Connecticut office.

Bill Rochelle joined the American Bankruptcy Institute in 2015 as its Editor-at-Large, writing every day on developments in consumer and reorganization law. For the prior nine years, he was the bankruptcy columnist for Bloomberg News.

Bill got his undergraduate and law degrees from Columbia University, where he received Harlan Fiske Stone Scholar awards from the law school. Before turning to journalism, he practiced bankruptcy law for 35 years, including 17 years as a partner in the New York office of Fulbright & Jaworski LLP.

In addition to writing, Bill travels the country for ABI, speaking to bar groups and professional organizations on hot topics in the turnaround community and trends in consumer bankruptcies.

Scott D. Rosen is a principal of Cohn Birnbaum & Shea PC and a member of the Bankruptcy & Creditors Rights Group and the Litigation Group. He represents secured lenders and other creditors in the resolution of troubled business credits, distressed real estate, and reorganization and liquidation proceedings under the Bankruptcy Code. In addition, Scott has represented all parties in interest in business reorganization proceedings, including trustees, creditors, committees, examiners, and debtors in possession.

Mr. Rosen represents financial institutions, private lenders, holders of commercial mortgage backed securities (CMBS), and private lenders in commercial real estate loan foreclosures and workouts, including multi-family, office, retail, residential projects, construction loans, affordable housing projects, and subdivision and condominium developments.

Of particular note, he served as lead litigation counsel in connection with the largest mortgage foreclosure action in the City of Hartford ($140,000,000), and through the innovative use of Connecticut's legal process, successfully concluded the foreclosure and obtained title for the lender three business days after commencing the action. He represented the debtor in Connecticut´s only successful prepackaged Chapter 11 reorganization.

Thomas J. Sansone is a partner in Carmody Torrance Sandak & Hennessey, where he has practiced in the civil litigation arena in Connecticut for more than 32 years, representing individuals and companies in a wide variety of business-related and personal disputes. He practices in various fields, including commercial, construction, and insolvency litigation. He has tried more than 90 cases to conclusion in Connecticut Superior Court, the United States District Court and the United States Bankruptcy Court, and has argued before both the Connecticut Supreme and Appellate Courts. Much of his trial work involves complex banking issues, including lender liability cases, contested foreclosure/collection matters, and representation of creditors in adversary bankruptcy proceedings.

From 2012 – 2018, Tom served as one of the 14 lawyers appointed by the judges of the Superior Court as a member of the Statewide Grievance Committee. During that time, he presided over dozens of hearings involving allegations of attorneys' professional misconduct.

Tom has also served the bar for many years as a member of the Executive Committee of the Commercial Law & Bankruptcy Section of the Connecticut Bar Association. From 2014 – 2016, he acted as the Secretary/Treasurer of that Section, and from 2016 – 2018, served as its Vice-Chair. On July 1st of this year, he assumed the chairmanship of the Section.

Tom is a published author, having twice written the annual review of commercial litigation cases for *The Connecticut Bar Journal* (2009, 2010), as well as co-authoring the Thomson Reuters book, *Inside the Minds: Banking & Finance Litigation Strategies* (2009). Tom is a frequent lecturer on commercial law topics and has, on three occasions, co-presented the annual update of Commercial Law & Bankruptcy at the Connecticut Bar Association's annual Connecticut Legal Conference.

Tom obtained both his undergraduate and law degrees from Boston University. He is active in a number of civic and community organizations including Clifford W. Beers Guidance Clinic, where he serves as president of its board of directors, the United Way of Greater New Haven (past Chair) and Vice-President of WIKS-USA, a charitable organization that supports a residential school in rural Western Kenya for children orphaned by the AIDS/HIV Pandemic.

Douglas S. Skalka is an experienced bankruptcy and commercial finance practitioner representing businesses, lenders, trade auditors, and investors in many bankruptcy and business reorganization matters over the past thirty years. Doug's clients include secured and unsecured creditors, debtors, commercial lenders, trustees, and creditors' committees. Cases are located in Connecticut and though out the country. His services include serving as counsel for asset-based lending transactions, avoidance actions, and the acquisition of troubled companies and their assets.

Attorney Skalka holds a certification in business bankruptcy from the American Board of Certification. He was recently named a Senior Specialist by the Board as he has held a certification in business bankruptcy for more than twenty years. The American Board of Certification is the nation's premier legal specialty certification organization, certifying attorneys as specialist in business bankruptcy, consumer bankruptcy, and creditors' rights law.

Attorney Skalka served as the President of the Connecticut chapter of the Turnaround Management Association (1999-2000) and served as a Contributing Editor to the 1998-1999 treatise on bankruptcy law published by Wiley Publications. He has lectured extensively on commercial finance, business reorganizations, and insolvency issues.

Suzanne B. Sutton serves as Of Counsel to Cohen and Wolf, LLC and is a resident of the firm's Orange office. Ms. Sutton has extensive experience in attorney discipline defense and in bankruptcy. She is a member of the firm's Ethics Group, Litigation Group and Bankruptcy Group.

Prior to joining Cohen and Wolf, Ms. Sutton spent approximately nine years at the Office of Chief Disciplinary Counsel and was appointed First Assistant Chief Disciplinary Counsel. As a disciplinary counsel she investigated, negotiated and prosecuted all matters of grievance complaints and unauthorized practice of law issues. Her accomplishments in the attorney discipline are seen in a vast number of grievance panel, Superior Court, Appellate Court and Supreme Court decisions. She now focusses on defending attorneys in the area of attorney discipline and professional mal practice. She also serves as an expert witness in the area of attorney responsibility.

Ms. Sutton has an abundance of experience in commercial law and bankruptcy. In her earlier career she represented individuals and businesses in Chapter 7, 13 and 11 cases. She also served as a Chapter 7 Panel Trustee for the District of Connecticut for several years. She continues to represent Debtors and creditors in bankruptcy and serves as a mentor to new or struggling bankruptcy attorneys.

Ms. Sutton is a member of the Connecticut Bar Association and chairs the Professional Responsibility Section. She is also a member of the Commercial Law and bankruptcy Section of the Connecticut Bar Association. She often participates in legal ethics seminars for the Connecticut Bar Association and for individual County Bar Associations. Ms. Sutton is an adjunct legal ethics professor at the University of Hartford.

James J. Tancredi was appointed to the United States Bankruptcy Court for the District of Connecticut by the U.S. Court of Appeals for the Second Circuit, and took the oath of office on September 1, 2016. Prior to his appointment he was a partner at the law firm of Day Pitney LLP (f/ka Day Berry & Howard) where, as a business litigator and commercial restructuring lawyer, he co-founded the firm's regional and national bankruptcy practice. During his 37 years in private practice, he represented financial institutions and other major constituents in a broad range of prominent insolvency related proceedings pending in courts on the Amtrak corridor.

Judge Tancredi has a Bachelor of Arts degree in Urban Studies and Political Science from the College of the Holy Cross in Worcester, Massachusetts, and received his law degree from the University of Connecticut School of Law. Each degree was awarded magna cum laude.

During his career, Judge Tancredi frequently lectured at the University of Connecticut School of Law and at bar association Continuing Legal Education programs on a broad range of commercial, real estate and restructuring issues and strategies. His professional and bar association activities included service as president and director of the Hartford County Bar Association and the Connecticut Turnaround Management Association. He has been an active member of the Connecticut Bar Association, American Bar Association, American Trial Lawyers Association, and was a director of the Hartford County Bar Foundation and Connecticut Mental Health Association. He is also a Connecticut Bar Foundation James W. Cooper fellow. These platforms provided invaluable opportunities for enhanced legal education and service to the bench and bar and served to drive local community pro bono initiatives.

While in practice, he wrote widely about business restructuring issues and co-authored the Connecticut chapter in "Strategic Alternatives for and Against Distressed Businesses, 2016 Edition", published by *Thomson Reuters West*.

Deborah Thorne is associate professor of sociology at the University of Idaho and a principle investigator on the nationally-recognized Consumer Bankruptcy Project. For the past two decades, economic inequality generally and debt and consumer bankruptcy specifically, have been at the core of her research agenda. As such, she has authored articles and book chapters on a range of issues associated with debt and consumer bankruptcy such as stigma, reasons for elder debtors' bankruptcy, medical debt and bankruptcy, effects of severe debt on couples' relationships, financial health following bankruptcy, social mobility, gender, and financial education. As a recognized expert on the subject of consumer bankruptcy, she has been interviewed by numerous media outlets such as *The New York Times*, *The Wall Street Journal*, *Salon Magazine*, *USA Today*, *National Public Radio*, *CNN*, and *ABC World News*.

Robert A. White is a Distinguished Practitioner in Residence at the Quinnipiac University School of Law where he teaches the basic course in bankruptcy and creditors' rights. Bob also developed a bankruptcy lab where students practice writing, counseling, and negotiation skills in simulated bankruptcy settings. With two other instructors, he teaches a commercial transactions workshop where students draft a simple contract, review basic commercial documents, and engage in other negotiating and writing exercises. He previously served as an adjunct processor and currently serves as faculty advisor for law students participating in the American Bankruptcy Institute Duberstein moot court competition. Bob has been active in bringing practitioners into the classroom and is grateful for the participation of the bench and bar in this effort.

Bob is Of Counsel with Murtha Cullina LLP having retired as a partner in 2015. He serves as chair of the firm's professional development committee. He previously served as a loss prevention and ethics counsel for the firm.

He has over 30 years of experience in bankruptcy, commercial litigation and workouts. His experience includes the representation of troubled companies and purchasers of distressed assets both in and out of bankruptcy. In the bankruptcy process he has assisted creditors' committees, secured and unsecured creditors, and trustees, and has served as a fiduciary in a confirmed plan of liquidation. He has served clients in many industries, including health care, construction, retail, real estate, manufacturing, energy, fuel oil distribution, and not-for-profit. He actively litigates claims in the bankruptcy court including preferences, fraudulent transfers, and director and officer claims.

Bob has represented clients in arbitration and mediation and served as an expert witness and mediator in a range of insolvency and commercial disputes. He serves on the pro bono bankruptcy mediation panel in Hartford.

He serves on several committees of the Hartford Foundation for Public Giving and is a James W. Cooper Life Fellow of the Connecticut Bar Foundation.

Prior to joining Murtha Cullina, Bob served as an assistant district attorney with the Manhattan District Attorney's Office.

The New Local Bankruptcy Rules

Hon. Julie A. Manning
Hon. Ann M. Nevins
Hon. James J. Tancredi

Part I – Commencement of Case; Proceedings Relating to Petition and Order for Relief

Rule 1001-1. Scope, Incorporation of District Court Rules, and Short Title.
The Local Rules supplement, but do not replace, the FRCP, FRE and FRCP, or the US. District Court's Local Rules ("Local District Rules"). Appendices can be modified without formal amendment. Amended rules effective as of September 4, 2018.

Rule 1001-2. Definitions.
Contains definitions for "Bankruptcy Rule(s)," "Bankruptcy Court" or "Court," "Certificate of Service" or "Proof of Service," "Clerk" or "Clerk of Court," "Debtor," "District Court Clerk," "District Court Local Civil Rules," "Local Bankruptcy Rules," "EFC No.," "FRBP" or "Fed. R. Bankr. P.," "FRCP" or "Fed. R. Civ. Proc.," "Pro Se Filer/Litigant," "Chapter 12 Trustee," and "Chapter 13 Trustee."

Rules 1002-1. Commencement or Continuation of Case Without Counsel.
Only self-represented individuals may file voluntary bankruptcy petition or appear in Court without being represented by an attorney. Pro Se Filers/Litigants must read and follow Local Rules, Bankruptcy Code, FRCP, FRBP and Local District Rules. Any agent of an individual (i.e. conservator, guardian, power of attorney) must attach evidence of such authority to any filings. All other entities must be represented by counsel. Court can dismiss a case for failure to comply with this Rule.

Rule 1002-2. Notice to Office of United States Trustee Regarding Filing of a Chapter 11 Petition.
Absent exigent circumstances, Debtors counsel is urged to contact US Trustee's Office and Clerk two business days before filing voluntary Chapter 11 petition to advise of anticipated filing date and matters requiring immediate relief.

Rule 1004-1. Business Entity Petition.
Along with petition or within five business days of filing of the petition, Debtor must provide documentation demonstrating requisite authority or consent for the bankruptcy filing by the business entity. Prior rule was fifteen days.

Rule 1006-1 Filing Fees. Application to Pay Filing Fee in Installments.
Filing fees prescribed by the Judicial Conference (see 28 U.S.C. § 1930). Applications to pay in installments must use Official Form 103(a) and be paid within four months of filing. Cash, certified check, money order, check drawn on an attorney's account, or an approved credit card are accepted.

Rule 1007-1. Lists, Schedules, and Statements.
Creditor List identifying name and address of each individual or entity included on Schedules D, E, F, G and H must be filed with petition or within 14 days of order for relief in involuntary case. Replaces the creditor matrix from prior rules. Must also include agencies and U.S. offices

required to receive notice under FRBP 2002(j). Creditor List must be filed in accordance with Court's Administrative Procedures for Electronic Filing, see Appendix A.

Filers must redact certain privacy information/ personal identifiers from documents and pleadings filed with court, including exhibits. This includes Social Security Numbers (use only last four if an individual SSN needs to be included), Names of Minor Children (use initials only if necessary), Dates of Birth (use birth year only) and Financial Account Numbers (use last four digits if necessary).

Schedules and Statements must be filed within time limits in FRBP 1007(c). Good cause required for any extension of time. Failure to timely file may result in dismissal after notice and failure to cure, without further notice or hearing.

Rule 1009-1. Amendments to Creditor Lists, Schedules, and Statements.
Within seven days of filing any amendment, Debtor shall file, along with the amended document and a Certificate of Service, the following:

> If adding parties, an amendment to the Creditor List, Schedules and/or Statements including the names, addresses and amount of such claims.
>
> If removing parties, a list clearly identifying the creditors being removed.

Rule 1015-1. Joint Administration.
Order for joint administration may enter without notice/hearing upon filing of motion in accordance with FRBP 1015 and supported by affidavit/declaration. The order may be reconsidered upon motion of any party in interest.

Debtor to serve joint administration order on all creditors and parties in interest. Judge shall be the judge assigned to first filed lead case.

Caption to include "Jointly Administered" and filed in lead case only, except (1) proofs of claim to be filed in claims register of specific debtor and (2) each debtor to file own Schedules, unless substantive consolidation ordered.

Joint administration order is for procedural purposes only; not cause for substantive consolidation.

Rule 1017-1. Contemporaneous Petitions.
No debtor may maintain more than one petition under any chapter of Bankruptcy Code at the same time. Second petition may be dismissed sua sponte or pursuant to motion.

Rule 1019-1. Conversion of Case; Documents Required to Be Filed.
Debtor must file schedule of assets, list of abandoned property, list of property against which relief from the automatic stay was granted, a schedule of assets and a schedule of unpaid post-petition obligations or expenses and, if an individual, a statement of current monthly income and a means test calculation within 14 days of the order converting case to Chapter 7.

If converted to Chapter 13, Debtor must file and serve on Chapter 13 Trustee a statement of currently monthly income and a calculation of commitment period and disposable income.

Rule 1073-1. Assignment and Reassignment of Cases within the District.
No change from prior rules. Fairfield and Litchfield Counties to Bridgeport, Middlesex and New Haven Counties to New Haven, and Hartford, New London, Tolland and Windham Counties to Hartford.

Part II - Officers and Administration; Notices, Meetings, Examinations, Elections; Attorneys and Accountants

Rule 2002-1. Notice and Service to Creditors and Other Interested Parties.
A copy of all motions, pleadings, applications, petition and other papers shall be served on any party in interest who filed written demand for service and on any ECF filer through CM/ECF system, and a Certificate of Service shall be filed.

The Creditor List shall include an attention line to an Officer, President, Director, Manager or General Agent of a business entity (though not necessarily by individual name).

If Creditor List has not been filed, and notice is required to be served by Clerk or party other than the Debtor, the Debtor shall serve the notice and file a Certificate of Service.

Rule 2002-2. Omnibus Hearing Calendar.
In Chapter 9, 11 and 12 cases, Court may establish omnibus hearing calendar with pre-set dates for any and all matters.

Rule 2004-1.Rule 2004 Examinations.
FRBP 7026 and Local District Rules 26 (a) – (e) (definitions, rules of construction, and privilege log) and 37 (discovery disputes) apply to 2004 Examinations and requests for documentation. However, FRCP 26 (a) (Initial Disclosures) (b) (Discovery Scope and Limits), (d) (Timing and Sequence of Discovery), (f) (Conference of the Parties; Planning for Discovery) and (g) (Signing Disclosures and Discovery Requests, Responses and Objections) do not. Proportionality considerations apply to a request for the production of documents or electronically stored information in connection with a FRBP 2004 examination.

The new rule authorizes parties to enter into "2004 Agreements." A party seeking an examination and the party to be examined may agree on date, time and place of examination and production of documents, without needing motion or subpoena. Notice of the agreement is to be filed with Court and served on the Debtor, any trustee, the US Trustee, the official committee, any party who filed appearance in case, and the proposed witness. Notice must include individual/entity to be examined, date/time/place of examination and list of documents to be produced. A party has seven days to file objection, which must be served on the above-mentioned parties. Objection limited to five pages and must state specific legal and factual basis for objection. If no objection is filed, the 2004 Agreement is deemed ordered by the Court. If an objection is filed, a notice of hearing is issued by clerk and objecting party must serve notice and

file Certificate of Service. Failure to comply with Local District Rule 37 (discovery disputes) is grounds for overruling the objection.

A written 2004 Agreement is enforceable by motion to compel or for sanctions without court order or service of subpoena.

If unable to enter into a 2004 Agreement and a party proceeds with a motion under FRBP 2004(a), the moving party must serve the motion accompanied by a proposed order, notice and a copy of the subpoena for production of documents under FRBP 2004(c) and 9016. Notice must provide an objection deadline of seven days from filing with Court, and the statement that proposed order may enter if no objection filed. Any objection is limited to five pages, must state legal and factual bases for objection, timely filed, and be served. Court will then schedule hearing. Failure to comply with Local District Rule 37 is grounds for overruling objection.

Failure to respond or object shall not prejudice proposed examinee from filing motion for protective order, quash the subpoena, or vacate order.

Rule 2014-1. Employment of Professionals.
Counsel for Debtor. Form B2020 must accompany any motion for employment of debtor's counsel/substitute counsel.

If application filed within thirty days of commencement of services, application is contemporaneously filed. If filed more than thirty days after commencement of services and seeking retroactive/nunc pro tunc relief, application must include affidavit relating to late filing of application and legal authority as to how retroactive/nunc pro tunc relief is appropriate.

If seeking contingent fees, applicant must annex engagement agreement to application and must provide sufficient information to confirm its enforceability.

In Chapter 9, 11, 12 or 13, professionals must deposit funds, regardless of source, in in a trust account, clients' funds account, escrow account, or IOLTA account consistent with Rule 1.15 of the Connecticut Rules of Professional Conduct. Counsel cannot apply the retainer to fees earned or expenses incurred after petition date absent court order.

Rule 2014-2. Retention of Ordinary Course Professionals.
Nothing changed from prior version. Debtor in 11, 12 or 13 or trustee in 7, 11, 12 or 13 may upon motion and notice, for good cause, hire professionals and advisors in ordinary course of business.

Rule 2015-1. Post-Confirmation Reports.
Nothing changed from prior version. Every forty-five days after order confirming Chapter 11 plan and every day thereafter until final decree, post-confirmation reports must be filed.

Rule 2016-1. Compensation of Professionals.
Applications must include Fee Application Cover Sheet and comply with Guidelines for Allowance of Compensation and Expense Reimbursement of Professionals (Appendices C and D, respectively) and comply with other guidelines.

Appendix D provides that every fee application should include:

- date petition filed, date or order approving employment, identify of party represented, date services commenced and whether seeking compensation under authority besides 11 U.S.C. § 330;
- terms and conditions of employment and compensation, source of compensation, existence and terms for retainer, and any budgetary or limitation on fees;
- names and hourly rates of professionals and paraprofessionals, any changes in hourly rates, and statement on whether compensation is based on customary compensation charged by comparably skilled practitioners in cases other than bankruptcy cases;
- whether interim or final, dates of prior orders, amounts requested and amount allowed/disallowed, amounts of prior payments and any amount remaining unpaid;
- whether party has had opportunity to review and whether said party approves the requested amount;
- if application filed more than once every 120 days, the date and terms of order authorizing shortened intervals;
- time period of services covered by application;
- to the extent known, the application should provide information related to case status:
    - Chapter 7-status of administration of case and if seeking interim award, whether feasible without prejudicing rights of creditor holding equal or higher priority claims.
    - Chapter 11- whether plan and disclosure statement field (and if not, anticipated filing date), whether quarterly fees paid and monthly operating reports filed.
    - Chapter 12 or 13-if debtor's attorney, whether application complies with §330(a)(4)(B) and in accordance with 20166(f) statement filed at beginning of case, and whether approval has effect on Debtor's plan.
- in all cases: cash on hand, accrued unpaid administrative expenses and amount of unencumbered funds.
- Material changes in status of case should be raised, orally or in writing, prior to hearing or objection deadline if hearing not required.

For the reimbursement of actual and necessary expenses, relevant factors include whether expense reasonable and economical, whether customarily charged to non-bankruptcy clients, whether applicant provided detailed itemization of all expenses, whether applicant has prorated.

If applicant desires to omit any information or as privileged or confidential, it must get prior approval from Court.

Any voluntary reduction of fees must be identified in the application.

Disbursements can't be enhanced – must be at rates and in practice with customs of applicant and generally accepted by applicant's clients.

Rule 2016-2. Compensation of Debtor's Counsel in Chapter 13 Cases.
Must disclose amount received by Debtor's counsel within one year of filing in Disclosure of Compensation of Attorney for Debtor, Form B2030.

If total amount of fees prior to confirmation is $4,000 or less, Form B2030 is sufficient and the filing of an itemized application for compensation is not necessary. Court still has authority to review and enter appropriate orders.

Rule 2017-1. Committees in Chapter 9, 11, and 12 Cases.
US Trustee to file with Court list of names of any committee, or statement that no committee constituted. US Trustee to facilitate the initial organizational meeting of any committee and appropriately advise it of its authority, duties and responsibilities.

Part III – Claims and Distribution to Creditors and Equity Interest Holders; Plans

Rule 3001-1. Proofs of Claim: Secured Claims in Individual Debtor Case.
Rule 3001-1 is new. In addition to the requirements of FRBP 3001, 3002, and 3002.1, this Rule requires that proofs of claim for secured claims against a debtor's residence (1) be filed in accordance with the instructions for Official Form B410 (Proof of Claim); and (2) include Official Forms B410-A (for mortgages), B410S-1 (mortgage payment change), and B410S-2 (postpetition mortgage fees, expenses, and charges), as applicable.

Rule 3003-1. Filing Proofs of Claim or Interest in a Chapter 9 or 11 Case, Notice to Disputed, Contingent, Unliquidated Creditors.
Rule 3003-1 is new. It provides the notice requirements to disputed, contingent, or unliquidated claimants in Chapter 11 cases. **Appendix K** contains the required order and notice.

Rule 3007-1. Claim Objections.
Rule 3007-1 is new. It contains the requirements for the content and service of claims objections. It also requires that Local Form 420B (Notice of Objection to Claim) be attached to every objection to a claim.

Rule 3007-2. Omnibus Claim Objection.
Rule 3007-2 is new. It provides the procedure for filing omnibus objections to up to 100 claims.

Rule 3007-3. Estimation of Claims.
Rule 3007-3 is new. It provides a procedure to implement 11 U.S.C. § 502(c), allowing a contested matter to be commenced to estimate unliquidated claims and claims to which there are objections.

Rule 3015-1. Chapter 12 Confirmation.
Rule 3015-1 modifies former Rule 3015-1. It provides that objections to Chapter 12 plans are to be filed at least seven days prior to the confirmation hearing.

Rule 3015-2. Chapter 13 – Confirmation.
Rule 3015-2 modifies former Rule 3015-1. It provides that objections to Chapter 13 plans are to be filed at least seven days prior to the confirmation hearing and that said hearing will be held after the claims bar date, unless otherwise ordered.

Rule 3016-1. Chapter 11 – Plan.
Rule 3016-1 is new. It provides the procedure and requirements for filing motions to extend the exclusivity period and the time for confirming a plan in small business cases. Note that motions to extend the time to confirm a plan in small business cases must be filed in time to give fourteen-days' notice of the hearing prior to the expiration of the deadline.

Rule 3017-1. Transmission and Notice of Plan and Disclosure Statement.
Rule 3017-1 modifies former Rule 3017-1. It provides the requirements for notice of the plan and disclosure statement and the disclaimer that must accompany the disclosure statement in cases other than small business cases.

Rule 3017-1.1. Consideration of Disclosure Statement in a Small Business Case.
Rule 3017-1.1 modifies former Rule 3017-1. It provides the required disclaimer that must be served with conditionally approved disclosure statements in small business cases.

Rule 3017-2. Approval of Disclosure Statement in Small Business Case.
Rule 3017-2 is new. It provides a procedure for the conditional approval of disclosure statements in small business cases pursuant to FRBP 3017.1. It also provides a procedure to seek a waiver of the requirement of a disclosure statement in small business cases.

Rule 3018-1. Certification of Acceptances and Rejections of Chapter 11 Plans.
Rule 3018-1 modifies former Rule 3018-2 to require that certifications of the number of claimants accepting and rejecting the plan be filed at least two business days prior to the confirmation hearing.

Rule 3020-1. Chapter 11 – Confirmation.
Rule 3020-1 is new. It requires that objections to confirmation of Chapter 11 plans be filed at least four days prior to the confirmation hearing.

Rule 3022-1. Application for Final Decree.
Rule 3022-1 is a minor modification to former Rule 3022-1 providing the requirements for seeking a final decree in a Chapter 11 case.

Part IV – The Debtor: Duties and Benefits

Rule 4001-1. Automatic Stay; Relief from Stay Worksheet.
Rule 4001-1 provides a new requirement that any party filing a motion for relief from stay concerning real property must file a Motion for Relief from Stay Worksheet. The Worksheet is found in **Appendix B** to the Local Rules. To complete the Worksheet, the movant will need to include detailed information concerning the debt (both pre-petition and post-petition), payments received and estimated value of the subject property. The movant is additionally required to attach all documents evidencing the movant's debt and perfected security interest. Finally, the worksheet must be signed as a declaration under penalties of perjury.

Rule 4001-2. Continuation or Imposition of Automatic Stay.
Rule 4001-2 governs motions for continuation or imposition of the automatic stay under 11 U.S.C. §§ 362(c)(3)(B) or (c)(4)(B). The movant must file a sworn declaration detailing the Debtor's past bankruptcy filings and alleging specific facts supporting the motion.

Rule 4001-3. Use of Cash Collateral and Debtor in Possession Financing.
Rule 4001-3 provides a detailed list of information that now must be included with any motion to use cash collateral or motion to approve debtor in possession financing. First, the debtor must file a Checklist accompanying any such motion, the form of which is found in **Appendix H**. The Checklist is designed to ensure the movant complies with the new detailed requirements of Local Rule 4001-3.

Any cash collateral motion must include the proposed order's effect on existing liens, the nature of any adequate protection payments and any conditions that may terminate the use of cash collateral. If the Debtor seeks to stipulate to the validity of any pre-petition liens in conjunction with use of cash collateral, the motion must either provide a minimum 60 day period for other parties in interest to investigate and challenge the liens or provide cause why the motion does not include such a provision.

Any movant seeking debtor in possession financing must provide the Court with details concerning the proposed terms of any proposed financing, the investigation undertaken by the Debtor to determine that the proposed financing is on the best terms available and an explanation of how any default may modify or terminate the automatic stay.

Movants seeking interim cash collateral or financing orders must describe the proposed use of funds and explain facts demonstrating that immediate or irreparable harm would befall the estate if immediate relief is denied.

The movant must submit a proposed order including proposed findings of fact, conclusions of law and citations to specific statutory provisions relied upon in support of the motion.

Rule 4002-1. Documents to Be Delivered to Trustee Prior to Section 341 Creditors' Meeting.
Rule 4002-1 specifies the documents that must be provided to a Chapter 7 Trustee, Chapter 12 Trustee, or Chapter 13 Trustee prior to a § 341 meeting of creditors. The Debtor must provide documents to the Trustee seven (7) days prior to the § 341 meeting.

The documents that must be provided to a Chapter 7 Trustee are listed in **Appendix I** to the Local Rules. In addition to documents such as identification, pay stubs, tax returns and bank statements, the Debtor must provide certain documents concerning any real estate or mobile home the Debtor owns, including an appraisal or comparative market analysis less than one (1) year old (Zillow type estimates will not suffice) and a title search or copy of all recorded mortgages. The Debtor must also provide documents stating the value of any interest the Debtor owns in a business entity or venture.

The documents that must be provided to a Chapter 13 Trustee are listed in **Appendix J** to the Local Rules. Aside from requiring the Debtor to produce many similar documents to what is required in a Chapter 7, the Debtor must provide financial information from his or her spouse and an affidavit and supporting financial information from any non-filing party contributing money to the Debtor's income.

In a Chapter 7, 12 or 13 case, the Debtor must provide the Trustee with evidence of payments received by the Debtor within the sooner or 60 days from the petition date or seven (7) days prior to the initially scheduled § 341 meeting of creditors.

Rule 4004-1. Entry of Discharge in Individual Chapter 11, Chapter 12 and Chapter 13 Cases.
Any individual seeking a discharge in a Chapter 11, Chapter 12 or Chapter 13 case must file a Certification and Application for Entry of Discharge on Court-approved forms. There are separate forms for each chapter and for discharged requested before completion or a plan versus after completion of a plan.

Part V - Courts and Clerks

Rule. 5003-1. Clerk of Court– General Authority:
This Rule permits the Clerk to change the form of the Creditor List (required by Local Rule 1007-1(a)) as required by the Clerk's automated case management system. It also provides for the Clerk to require alternative forms of payment from attorneys and firms that have previously had their checks or credit/debit cards dishonored.

Rule 5005-1. Filing Papers – Requirements:
This Rule governs the form of pleadings (*e.g.*, font size, margin, signature block, etc.) and dispenses with certain of the requirements of the prior Local Rule 9004-1. The new Rule 5005-1

incorporates the requirements from the Local District Rule 10. Note that this Local District Rule was amended as of November 7, 2016.

Rule 5010-1. Reopening Cases:
Concerns motions to reopen a case under § 350(b) of the Code if applicant desires to omit any information or as privileged or confidential FRBP 5010. Requires that such a motion state with specificity the reason for reopening, and provides that the Court may grant such a motion upon a finding of cause. Further requires a filing fee for the reopening of such a case, unless the case is reopened to correct administrative error or for reasons relating to the debtor's discharge.

Rule 5011-1. Withdrawal of the Reference:
Concerns the procedure for moving for withdrawal of the reference under 28 U.S.C. §§ 1334 and 157 and for notice with respect to same. Replaces (and is substantively identical to) the prior Local Rule 5011-1.

Rule 5073-1. Photography, Broadcasting, Recording, and Televising:

Prohibits photographing, recording or broadcasting judicial proceedings, absent an Order of the Court.

Part VI – Collection and Liquidation of the Estate

Scope: Part VI primarily concerns the sale of property of the estate, with requirements relating to sale and sale procedures motions, employment and compensation of auctioneers and appraisers, and the conduct of bankruptcy sales. The final Rule in this Part authorizes chapter 12 and chapter 13 trustees to deposit debtors' income tax refunds.

Rule 6004-1. Sale of Estate Property - General
Concerns motions to sell property of the estate. Subsection (a) concerns notice generally; and subsection (b) provides further requirements where the motion seeks to sell property free and clear of liens with liens attaching to the proceeds (under § 363(f) of the Code) – *i.e.*, that such a motion, *inter alia*, name all parties asserting liens/interests in the property as respondents, describe the liens/interests (including perfection and whether the lien/interest is disputed), and discuss what will be paid upon consummation of the sale and what will be paid pursuant to further order of the Court. Subsection (c) prohibits certain interested persons (*e.g.*, appraisers, auctioneers, officers, directors, stockholders, agents, employees, or related persons of the foregoing) from purchasing property of the estate as to which they are engaged. Subsections (d), (e), (f) and (g) provide certain notice and procedural requirements for bankruptcy sales and subsection (h) provides that the sanctions for violating this Rule include, without limitation, disgorgement, fines and disqualification from future employment by a bankruptcy estate. Subsections (i), (j) and (k) provide that the Court may approve sale by automated Internet auction listing or brokerage, require that a motion seeking such approval contain certain specific information, and contain requirements governing internet auction mechanisms. The new Local Rules 6004-1 and 6004-2 replace the prior Local Rule 6004-1, with the new rules containing (a) substantially more detailed requirements for the form and content of motions and proposed

orders relating to sales/sale procedures and (b) new and expanded requirements applicable to the conduct of bankruptcy sales.

Rule 6004-2. Sales and Sale Procedures Motions
Concerns motions to sell property of the estate under § 363(b) of the Code and motions seeking approval of sale/bid/auction procedures. Subsection (b) of this Rule requires that such motions include a proposed purchase agreement or form of same (if applicable) and a proposed form of sale order, and require that certain information be included/highlighted. Subsection (c) provides that a motion seeking approval of sale procedures may be filed either as part of the sale motion under § 363(b) of the Code or by separate motion filed in anticipation of an auction and proposed sale and requires that a sale procedures motion highlight certain provisions. Subsection (d) requires, absent an order otherwise, that a sale procedures order specify certain information/requirements with respect to the auction. Subsection (e) imposes further requirements for the inclusion of factual information as to a motion for approval of a sale or sale procedures with respect to substantially all assets within sixty days of the petition date.

Rule 6005-1. Employment of Auctioneers
Sets requirements for the employment of auctioneers and the conduct of auctions, which apply absent an order otherwise by the Court. Subsection (b) requires the inclusion of certain specific information in an application to employ an auctioneer (*e.g.*, the need for the auctioneer, description of the property to be sold, the mechanism to pay the auctioneer, whether or not lienholders have consented to payment of the auctioneer's expenses, and the required bond). The new rule dispenses with the procedure in the prior Rule 6005-1 for the Court's Clerk to maintain a list of qualified auctioneers. Subsections (c) and (d) require the auctioneer to give the estate a bond that meets certain requirements. Subsection (e) provides for payment and reimbursement of expenses of an auctioneer upon proper application and approval by the Court and contains certain requirements and limitations relating to reimbursement of expenses. The new rule eliminates the prior Rule 6005-1's presumptive percentage-based compensation scheme. Subsections (f), (g) and (h) contain further requirements as to the auctioneer's conduct. Subsection (i) provides that the sanctions imposed for violation of this Rule include, without limitation, disqualification from future employment on the behalf of bankruptcy estates.

Rule 6005-2. Employment of Appraisers
Concerns employment and compensation of appraisers. Subsection (a) requires that certain information be contained in an application to employ an appraiser in addition to the requirements in Local Rule 2014-1.1 (*e.g.*, how the appraisal will be paid for, estimation of the appraiser's fee, description of the item(s) to be appraised and the time needed for the appraisal); similar to the requirements in the prior Rule 6005-1(a) except for the elimination of the statement required by the prior Rule 6005-1(a)(3). Subsection (b) requires, in addition to the requirements in the Bankruptcy Code and FRBP 2016(a), that applications for allowance of an appraiser's fees or reimbursement of expenses exceeding $1,000.00 contain certain information. These requirements were also part of the prior Rule 6005-1 but previously the threshold to trigger them was $500.00.

Rule 6070-1. Tax Returns and Tax Refunds in Chapter 12 and 13 Cases

Authorizes chapter 12 or chapter 13 trustees to endorse, on behalf of chapter 12 or 13 debtors, federal/state/local income tax refunds payable to the debtor (with such funds to be deposited into the trustee's trust fund account).

Part VII – Adversary Proceedings

Rule 7001-1. Adversary Proceedings - General.
Rule 7001-1 states that an adversary complaint shall be filed in the division in which the related Debtor case is pending.

Rule 7002-1. Adversary Proceeding Cover Sheet.
Rule 7002-1 requires that every adversary proceeding shall be accompanied by an adversary proceeding cover sheet, Official Form B1040.

Rule 7005-1. Service of Pleadings and Other Papers by Electronic Means.
Rule 7005-1 permits parties to make service through the Bankruptcy Court's CM/ECF system, as permitted by FRCP 5(b)(2)(E) and Local District Rule 5; this rule, however, does not apply to the service of process of a summons and complaint which must be served in accordance with FRBP 7004.

Rule 7007-1. Motion Practice.
Rule 7007-1 indicates that motion practice in adversary proceedings follows the Local Rules to include Local District Rules 7 and 56.

Rule 7007-2. Briefs.
Rule 7007-2 governs the length of briefs; a brief shall not exceed twenty-five pages (excluding the table of contents and table of authorities) and a reply brief shall not exceed ten pages. If a party seeks to submit a brief in excess of the page limit, such a request must be made by motion, only, filed at least seven days before the deadline for the filing, and upon a showing of cause. Amicus briefs may not be filed without permission of the Court. If permission is granted, the brief shall specifically state the interest of the amicus curiae in the outcome of the litigation.

Rule 7012-1. Motions to Dismiss.
Rule 7012-2 renders Local District Rule 12 applicable to motions to dismiss adversary proceedings, to include the requirement that represented parties wishing to dismiss the complaint of a self-represented/Pro Se Filer/Litigant shall also file and serve as a separate document a "Notice to Self-Represented Litigant Concerning Motion to Dismiss."

Rule 7016-1. Pretrial Procedures.
Rule 7016-1 outlines the procedure for the initial pretrial conference, the date for which shall appear in the summons. Unless ordered otherwise, the initial pretrial order shall be filed, jointly, at least seven days before the initial pretrial conference. If no appearance has been filed by the Defendant/s seven days prior to the initial pretrial conference, the plaintiff shall file the initial pretrial order. The pretrial order shall include: a summary of the claims and defenses of each

party, a list of additional matters that might aid in the scheduling or disposition of the case, and the signature of each attorney. If there is a conflict between the pretrial order and the Local Bankruptcy Rules, the provisions of the orders of the Court shall control.

Rule 7026-1. Discovery; Duty of Disclosure, Filing of Discovery.
Rule 7026-1 renders Local District Rule 26 applicable to discovery in adversary proceedings.

Rule 7037-1. Discovery Disputes.
Rule 7037-1 renders Local District Rule 37 applicable to discovery disputes.

Rule 7055-1. Default and Default Judgment
Rule 7055-1 requires a party requesting the entry of a default judgment, to file a written request for the entry of default with the Court, together with a proposed form of entry of default, and other materials required by FRCP 55(a). An affidavit in compliance with 50 U.S.C. §3931 must also be filed with any motion for default judgment against an individual.

A hearing on a Motion for Default Judgment may be scheduled by the Court. The Court may also require the plaintiff to move for an entry of default judgment if the default has lasted for ninety days or longer. If the plaintiff fails to so move, the Court may dismiss the proceedings without prejudice, as to the defendant.

Rule 7056-1. Summary Judgment.
Rule 7056-1 renders Local District Rule 56 applicable to motions for summary judgment, to include the requirement that represented parties moving for summary judgment against a self-represented/Pro Se Filer/Litigant shall also file and serve as a separate document a "Notice to Self-Represented Litigant Concerning Motion for Summary Judgment."

Rule 7067-1. Registry Fund.
Rule 7067-1 sets forth the policies which govern the deposit and withdrawal of monies deposited into the registry of the Court. Monies directed to be deposited, by written order of the Court, shall be deposited and invested by the Clerk of Court in accordance with the terms of the order. All payments shall be made payable to "Clerk, U.S. Bankruptcy Court."

The withdrawal of funds from the registry shall also be governed by the terms of the written order of the Court and shall be withdrawn only if the order so provides. Any order for the distribution of less than all funds and accrued interest shall be denominated "Order for Partial Distribution from the Registry of the Court." Otherwise, the order will be treated as an Order for Final Distribution. Whenever an Order does not specify for the distribution of all funds or interest, the Clerk of Court shall pay such funds into the Treasury of the United States. This Rule applies to both adversary proceedings and bankruptcy case.

All orders authorizing disbursement must include the payee's name, address, tax identification number (redacted to include only the last four digits of the number) as well as the dollar amount to be paid. Prior to the receipt of payment, the payee must submit an executed IRS Form W-9, delivered to the Clerk.

Part IX – General Provisions.

Rule 9010-1. Appearances.
Rule 9010-1 governs the filing of appearances in a case under the Bankruptcy Code, or any matter commenced by a complaint or motion. The new iteration of this rule omits any reference to subsection (a) of the previous rule which stated that the signature of an attorney constitutes a certification that the attorney is authorized to practice law in the United States Bankruptcy Court for the District of Connecticut.

Rule 9013-1. Form of Pleading of Certain Contested Matters.
There is no change to Rule 9013-1.

Rule 9013-2. Motions Filed With Petition in Chapter 11 Case.
Rule 9013-2 is a new Rule which controls any motions or applications in which the Debtor requests a hearing ("First Day Hearing") or the entry of an order with less than seven days' notice and prior to the earlier of the creditors' committee formation or the Section 341 meeting of creditors. Requests under this rule shall be confined to matters required to avoid irreparable harm or to maintain ongoing business operations, and other matters which the Court may deem appropriate. The rule requires that the Debtor serve copies of all motions and applications filed with the Court as to which a First Day Order has entered, on all parties entitled to such notice, within forty-eight hours.

Rule 9014-1. Contested Matters and the Contested Matters Procedure.
Rule 9014-1 outlines the procedure for contested matters, hereinafter the Contested Matter Procedure, which applies to all contested matters (unless noted in Appendix M-N). This Rule requires that a certificate of service shall be filed with all documents referred to in this Contested Matter Procedure.

All contested matters shall contain a proposed order and notice; the notice shall contain a response deadline of fourteen days or twenty-one days, pursuant to FRBP 2002(a) and 9014. The response deadline shall be set from the date the notice was filed with the Court, and shall indicate that in the absence of a timely filed response, the proposed order may enter without further notice or hearing.

All responses to contested matters shall be no more than ten pages in length, shall state the legal and factual bases therefore, shall be filed no later than the response date, and shall be served upon all parties. Upon the filing of a timely response, a notice of hearing shall be sent by the clerk's office. The party who filed the contested matter shall then serve the notice of hearing on all parties. Any reply to the response shall be no more than five pages in length and shall be filed no later then three days before the hearing on the contested matter.

The initial hearing will not be an evidentiary hearing unless the Court provides notice stating otherwise, or unless the initial motion or application requests emergency relief. At the initial

non-evidentiary hearing, the Court will conduct a status/scheduling conference which will address the following: stipulations concerning the admissibility of evidence, stipulations of fact, the filing and/or service of witness and exhibit lists, proposed exhibits, as well as the scheduling of an evidentiary hearing.

Requests for a continuance of the initial hearing shall be made at least seven days before the scheduled hearing. If the request is granted, the Clerk's Office will issue a notice of final hearing to the party who filed the matter, which party shall thereafter make service of the notice on all parties. If the request is not granted, the hearing will be heard as scheduled.

Requests for a continuance of the final hearing shall be made at least three business days before the date of the final hearing, and shall be made by motion, served upon all parties; the motion shall state the factual basis for the continuance and must indicate whether any prior continuance was granted. If the request is granted, the Clerk's Office will issue a notice of continued final hearing to the party who filed the matter, which party shall thereafter make service of the notice on all parties. Unless the request is granted at least one business day before the scheduled hearing, the final hearing will be heard as scheduled.

Unless an order granting the continuance states otherwise, a continuance of the hearing automatically extends the time for filing and serving reply documents.

Motions or applications which do not follow the Contested Matters Procedure are set forth in Appendix M. Exceptions to the Contested Matter Procedure are set forth in Appendix N.

Rule 9019-1. Motions to Compromise.
Rule 9019-1 is a new Rule which provides that a motion to compromise under FRBP 9019 shall be filed in the bankruptcy case; a motion to compromise an adversary proceeding shall be filed in the main bankruptcy case and in the adversary proceeding. Motions to compromise adversary proceedings are governed by Local Rule 9007-1, and must identify the cause of action and any consideration paid or agreed to be paid, and shall be served on all parties. The Clerk shall issue a notice of hearing for any such motion, which notice will be served by movant's counsel, together with the motion and proposed order, on all creditors in the Debtor's case, and shall file the certificate of service in the adversary proceeding.

Rule 9019-2. Alternative Dispute Resolution.
Rule 9019-2 replaces the prior rule, and indicates that the Court, either sua sponte, or upon motion by any party, may order the parties to participate in mediation and non-binding ADR, and may order the parties to share the costs thereof. The Court may stay proceedings and discovery during the ADR process. Upon motion, and by agreement of the parties, the Court may submit a case or proceeding to binding arbitration, early neutral evaluation, or mini-trial.

Rule 9027-1. Removal.
Rule 9027-1 is new and states that a removed claim or cause of action related to a bankruptcy case shall be filed in the Bankruptcy Court as an adversary proceeding. The filing must include a

completed Adversary Proceeding Coversheet, and the filing fee is due upon the filing of the notice of removal; a filing fee may not be required if the Trustee or Debtor in possession files a motion to defer the filing fee, along with a proposed order. The notice of removal must include a copy of the docket sheet, as well as a copy of all pleadings from the Court from which the claim or action was removed. The pleadings must comply with FRBP 7008 and FRBP 7012(b); if the pleadings do not so conform, the filing party shall file amended pleadings which address the entry of final orders within five days of the filing of the notice of removal.

Rule 9036-1. Notice by Electronic Transmission.
Rule 9036-1 is new and states that parties are authorized to serve notices through the Court's CM/ECF system; exceptions include service of a summons and complaint in an adversary proceeding under FRBP 7004, or service of a subpoena under FRBP 9016, for which service may not be electronic.

Rule 9070-1. Exhibits.
Rule 9070-1 is new and states that unless the Court orders otherwise, all parties are required to comply with the procedure for filings proposed exhibits using the CM/ECF system in accordance with Appendix A.

Rule 9077-1. Sealed Documents.
Rule 9077-1 is new and indicates that Local District Rule 5(e) applies to bankruptcy proceedings.

Rule 9083-1. Attorneys - Admission to Practice.
Rule 9083-1 is new and indicates that Local District Rule 83.1 applies to motions for admission of attorneys pro hac vice.

Rule 9083-2. Attorneys – Discipline and Disbarment.
Rule 9083-2 is new and indicates that Local District Rule 83.2 applies to suspension or disbarment of counsel by the Court.

Rule 9083-3. Attorneys – Requirements of Local Counsel.
Rule 9083-3 is new and indicates that Local District Rule 83.1(c) applies to motions for admission of attorneys pro hac vice, and the requirement to maintain a local office.

Rule 9083-4. Attorneys – Withdrawals.
Rule 9083-4 is new and indicates that Local District Rule 7(e) applies to motions for withdrawal of an appearance.

Rule 9083-5. Change of Contact Information or Name.
Rule 9083-5 is new and indicates that an attorney must modify his or her name and/or contact information in CM/ECF within three business days of any change. Any individual filing a proof of claim or participating in a bankruptcy case pro se must file notice of any modification to its mailing address, within seven days of any change.

Appendices

Appendix A-Administrative Procedures for Electronic Case Filing

Appendix B-Relief from Stay Worksheet

Appendix C-Fee Application Cover Sheet

Appendix D-Guidelines for Compensation and Expense Reimbursement of Professionals

Appendix E – Chapter 12 Operating Order

Appendix E sets forth a Local Form Chapter 13 Plan in a fillable PDF document which contains active programming elements. Once the form is completed with all necessary information, it must be converted into PDF format so that it can be filed through CM/ECF. Plans that do not comply with the Local Bankruptcy Rules may not be confirmable. The Local Form Chapter 13 Plan also requires that the Debtor indicate that the Plan contains no non-standard provisions, except those set forth in Section VII of the Local Form Chapter 13 Plan. A non-standard provision is a provision not otherwise included in the Local Form Chapter 13 plan or which deviates therefrom. Of note, the Local Form Chapter 13 Plan requires an attorney seeking compensation or reimbursement in excess of $4,000, to file an application for allowance of compensation and reimbursement of expenses pursuant to 11 U.S.C. §330, before confirmation of the Chapter 13 plan.

Appendix F – Chapter 12 Operating Order

Appendix F sets forth the rules, regulations, and procedures to be followed by the Debtor and Debtor's Counsel in a Chapter 12 proceeding. Specifically, Appendix F sets forth the necessary forms, tax statements, and insurance statements to be submitted, as well as bookkeeping and accounting requirements of the Debtor. Appendix F also outlines the tax documents which the Debtor must bring to the 341 Creditor's Meeting and which the Debtor must file throughout the pendency of the proceeding. Appendix F also references the 90 days in which the Debtor has to file a Chapter 12 plan, and states that the Debtor shall file its objections to claims within 45 days of the confirmation order. Appendix F also outlines the plan confirmation requirements, as well as post-petition tax filing and payment requirements. Failure to comply with the requirements set forth in Appendix F may result in dismissal.

Appendix G provides the guidelines for seeking the sale of substantially all estate assets pursuant to 11 U.S.C. § 363.

Appendix H Checklist for Motions and Orders Pertaining to the Use of Cash Collateral and Post-Petition Financing

Appendix I Documents to Be Produced to Trustee in Chapter 7 Cases Prior to Section 341 Creditor's Meeting

Appendix J Documents to Be Produced to Trustee in Chapter 13 Cases Prior to Section 341 Creditor's Meeting

Appendix K Notice to Disputed, Contingent, and Unliquidated Creditors

Appendix L List of Government Agency Addresses

Appendix M – Motions That Do Not Follow Contested Matter Procedure

Appendix M identifies those motions, referenced in Local Bankr. R. 9014-1(m) which are not governed by the Contested Matter Procedure, and may be scheduled for hearing.

Appendix N – Exceptions to the Contested Matter Procedure

Appendix N identifies those motions, referenced in Local Bankr. R. 9014-1(n) which are excepted from the Contested Matter Procedure, and will be set for hearing.

UNITED STATES BANKRUPTCY COURT
DISTRICT OF CONNECTICUT

LOCAL RULES OF
BANKRUPTCY PROCEDURE

Revised as of April 2018
Effective Date: September 4, 2018

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Part I. Commencement of Case; Proceedings Relating to Petition and Order for Relief

Local Bankr. R. 1001-1 Scope, Incorporation of District Court Rules, and Short Title.

(a) Scope of Rules and Short Title.

(1) These rules shall be known as the Local Rules of Bankruptcy Procedure of the United States Bankruptcy Court for the District of Connecticut. They shall be cited as D. Conn. Bankr. L. R, and referred to as the "Local Bankruptcy Rules", "Local Bankruptcy Rule ____" or "L. Bankr. R. _____," where the meaning is clear. The Local Rules of Bankruptcy Procedure govern the practice and procedure in the United States Bankruptcy Court for the District of Connecticut (the "Bankruptcy Court"), in all cases under Title 11 of the United States Code (the "Bankruptcy Code"). The Local Rules of Bankruptcy Procedure supplement, but do not replace the Federal Rules of Civil Procedure, the Federal Rules of Evidence, the Federal Rules of Bankruptcy Procedure, or the Local Rules of Civil Procedure of the United States District Court for the District of Connecticut.

(2) The Appendices to the Local Rules of Bankruptcy Procedure may be modified by the Bankruptcy Court without the necessity of a formal amendment to the Local Rules of Bankruptcy Procedure.

(3) These Local Rules of Bankruptcy Procedure shall be effective September 4, 2018 (the "Effective Date").

(4) Upon the Effective Date, the Local Rules of Bankruptcy Procedure effective May 15, 1997, the Standing Orders of the Bankruptcy Court (but not Chambers Orders or Procedures) are hereby vacated and superseded.

(b) Incorporation of District Court Rules.

The Local Rules of Civil Procedure of the United States District Court for the District of Connecticut shall apply in all cases or proceedings in the Bankruptcy Court to the extent they are relevant and not inconsistent with the Bankruptcy Code, the Federal Rules of Bankruptcy Procedure, or these Local Rules of Bankruptcy Procedure.

Local Bankr. R. 1001-2 Definitions.

In addition to the definitions found in Fed. R. Bankr. P. 9001, the following definitions apply to these Local Bankruptcy Rules:

(a) "Bankruptcy Rule(s)" means the Federal Rules of Bankruptcy Procedure currently in effect, and as thereafter amended.

(b) "Bankruptcy Court" or "Court" means, in addition to the definition in Bankruptcy Rule 9001(4), the Bankruptcy Judges of the United States Bankruptcy Court for the District of Connecticut, as a collective body.

(c) "Certificate of Service" or "Proof of Service" is a document identifying the pleading/document a party has served, the manner of service, the date of service, and the address where service was made.

(d) "Clerk" or "Clerk of Court" means Clerk of the Bankruptcy Court for the District of Connecticut and any Deputy Clerk acting under the direction of the Clerk of Court.

(e) "Debtor" means debtor or debtors and when referring to an individual or individuals means an individual or individuals who are represented by an attorney or who are proceeding in a case as a *Pro Se* Filer/Litigant.

(f) "District Court Clerk" means Clerk of the United States District Court for the District of Connecticut.

(g) "District Court Local Civil Rule(s)" means the Local Rules of Civil Procedure of the United States District Court for the District of Connecticut.

(h) "Local Bankruptcy Rules" means these Local Rules of Bankruptcy Procedure of the United States Bankruptcy Court for District of Connecticut.

(i) "ECF No.___" means the electronic case filing number for a pleading/document entered on the docket of a case or an adversary proceeding.

(j) "FRBP" or "Fed. R. Bankr .P." means the Federal Rules of Bankruptcy Procedure.

(k) "FRCP" or Fed. R. Civ. P. means the Federal Rules of Civil Procedure.

(l) "*Pro Se* Filer/Litigant" means a self-represented individual.

(m) "Chapter 12 Trustee" means the individual appointed as a standing trustee in Chapter 12 cases filed in this District.

(n) "Chapter 13 Trustee" means the individual appointed as a trustee/standing trustee for all Chapter 13 cases filed in this District.

Local Bankr. R. 1002-1 Commencement or Continuation of Case Without Counsel.

(a) Individual Filers.

Only an individual may file a voluntary bankruptcy petition or appear in Court without being represented by an attorney as a *Pro Se* Filer/Litigant. All other entities, including but not limited to corporations, limited liability companies, partnerships, and trusts, may not appear in Court or sign pleadings, including the petition, without being represented by an attorney. If a Debtor that is not an individual files a petition without an attorney, the Court may dismiss the case without notice, either *sua sponte*, or on motion of a party in interest after notice and an opportunity for a hearing.

If an agent on behalf of an individual, such as a court-appointed conservator, court-appointed guardian or the holder of an unexpired power of attorney or other authority pursuant to non-bankruptcy law files a pleading/document with the Court, the filer shall file evidence of such authority and shall attach such authority simultaneously with the pleading/documents filed

on behalf of the individual. Failure to file such authority may result in a dismissal of the case or the striking of a pleading without notice, either *sua sponte*, or on motion of a party in interest after notice and an opportunity for a hearing.

(b) Responsibility of Individual *Pro Se* Filers/Litigants.

An individual proceeding on his or her own behalf is considered to be proceeding as a *Pro Se* filer or *Pro Se* litigant. Individuals proceeding *pro se* must read and follow these Local Bankruptcy Rules, the Bankruptcy Code, the Federal Rules of Civil Procedure, the Federal Rules of Bankruptcy Procedure, and the Local Rules of the United States District Court for the District of Connecticut. *See* USDC Local Rule and Notice to *Pro Se* Filers/Litigants.

Local Bankr. R. 1002-2 Notice to Office of United States Trustee Regarding Filing of a Chapter 11 Petition.

Unless there are exigent circumstances, counsel for the Debtor are urged to contact the United States Trustee's Office for the District of Connecticut and the Clerk of Court at least two (2) business days prior to filing a voluntary petition for relief under Chapter 11 of the Bankruptcy Code, for the purpose of advising of the anticipated filing of the petition (without disclosing the identity of the Debtor) and the matters on which the Debtor intends to seek immediate relief.

Local Bankr. R. 1004-1 Business Entity Petition.

An authorized officer filing a petition on behalf of a business entity shall file with the petition or within five (5) business days thereafter, documentation evidencing the requisite authority or consent, as applicable, of that business entity to file the petition. Failure to file such documentation may result in a dismissal of the case without notice, either *sua sponte*, or on motion of a party in interest after notice and an opportunity for a hearing.

Local Bankr. R. 1006-1 Filing Fees - Application to Pay Filing Fee in Installments.

(a) Filing fees for cases filed under Chapter 7, 9, 11, 12, and 13 of the Bankruptcy Code are prescribed by the Judicial Conference and may be found in 28 U.S.C. § 1930.

(b) Applications to pay the filing fee in installments shall be filed on Official Form 103 (a) and pursuant to FRBP 1006(b). Such fee shall be paid in full within four (4) months of the filing, unless the Court orders otherwise.

(c) Filing fees may be paid by cash, certified check, money order, check drawn on an attorney's account, or an approved credit card. The Clerk may refuse to accept personal checks, checks from an attorney filing their personal petition, and may also refuse to accept a check from any person who is known by the Clerk to have previously presented a form of payment that was subsequently refused. Checks shall be payable to "Clerk, U.S. Bankruptcy Court." A check is accepted subject to collection.

Local Bankr. R. 1007-1 Lists, Schedules, and Statements.

(a) Creditor List.

A Creditor List containing the name and address of each individual or entity included or to be included on Schedules D, E, F, G, and H shall be filed contemporaneously with every voluntary petition or within fourteen (14) days of the entry of an order for relief in an involuntary case. The Creditor List shall be submitted in accordance with the Court's Administrative Procedures for Electronic Filing, *see* Appendix A, and shall include those agencies and offices of the United States required to receive notice pursuant to FRBP 2002(j). The Creditor List shall be filed by the Debtor or party responsible for filing the documents required by 11 U.S.C. § 521. The failure to file the Creditor List in compliance with this rule may result in dismissal of the case after notice of the deficiency and failure to cure deficiency, without further notice or hearing.

(b) Privacy Information.

(1) Redaction of Personal Identifiers. Unless otherwise ordered by the Court, all individuals and entities shall not include, and shall redact the following personal identifiers from all documents and pleadings filed with the Court, including exhibits thereto, whether filed electronically or in paper:

(A) Social Security Numbers. If an individual's social security number must be included in a pleading or document, only the last four digits of that number should appear.

(B) Names of Minor Children. If a minor child is mentioned, only the initials of that child should appear.

(C) Dates of Birth. If an individual's date of birth is included in a pleading, only the birth year should appear.

(D) Financial Account Numbers. If financial account numbers are used, only the last four digits of these accounts should appear.

(2) Responsible Party. The responsibility for redacting these personal identifiers rests solely with the filer. The Clerk's Office will not review filed documents for compliance with this rule.

(c) Schedules and Statements.

All Schedules and Statements required to be filed pursuant to 11 U.S.C. § 521 shall be filed in accordance with the time limits set forth in FRBP 1007(c). No motion for extension of time to file any or all Schedules and Statements required to be filed by FRBP 1007 shall be granted unless cause is shown for the requested extension of time. Failure to timely file all Schedules and Statements may result in dismissal of the case after notice of the deficiency and a failure to cure the deficiency, without further notice or hearing.

Local Bankr. R. 1009-1 Amendments to Creditor Lists, Schedules, and Statements.

If any Creditor List, Schedule, or Statement is amended to add new parties, to make corrections or changes to mailing addresses, or to remove parties who have not yet filed a proof of claim, the Debtor shall, within seven (7) days of the filing of any amendment, file with the document (i) with respect to adding new creditors, an amendment to the Creditor List, Schedules and/or Statements, as applicable, which shall include as necessary the names, addresses of the parties to be added or corrected, and the amounts of such claims; (ii) with respect to removing parties from the Creditor List, Schedules, and/or Statements, a list clearly and conspicuously identifying the names of the creditor being removed and the fact that such creditor(s) is/are being removed. A Certificate of Service shall also be filed with each amendment, clearly identifying the amendment or correction to be made to the Creditor List.

Local Bankr. R. 1015-1 Joint Administration.

(a) An order of joint administration may be entered, without notice and an opportunity for hearing, upon the filing of a motion for joint administration pursuant to FRBP 1015, supported by an affidavit, declaration, or verification which establishes that the joint administration of two or more cases pending in this Court under the Bankruptcy Code is warranted. An order of joint administration entered in accordance with this Local Rule may be reconsidered for cause upon the motion of any party in interest at any time.

(b) Upon entry of an order directing joint administration of cases, notice thereof shall be served by the Debtor on all creditors and other parties in interest.

(c) Jointly administered cases shall be assigned to the Bankruptcy Judge to whom the first filed lead case was assigned.

(d) All pleadings and other papers filed in jointly administered cases shall bear a combined caption with the legend "Jointly Administered." Except as provided in subsection (e) and (f) of this Rule, pleadings and other papers shall be docketed and placed in the case file of the lead case only.

(e) Any proofs of claim filed in jointly administered cases shall be filed by the claimant in the claims register for the Debtor against which the claim is asserted.

(f) Notwithstanding the joint administration of cases, each Debtor shall file its own Schedule of assets and liabilities in each case, unless an order for substantive consolidation has entered.

(g) An order of joint administration under this Local Rule is for procedural purposes only and shall not be cause for substantive consolidation of the respective Debtors' estates.

Local Bankr. R. 1017-1 Contemporaneous Petitions.

Unless otherwise ordered by the Court, after notice and an opportunity for a hearing, no Debtor as defined by 11 U.S.C. § 109 or § 101(13) may maintain more than one petition under any Chapter or Chapters of the United States Bankruptcy Code at the same time. The second petition filed may be dismissed by the Court *sua sponte* or pursuant to motion upon notice and an opportunity for a hearing.

Local Bankr. R. 1019-1 Conversion of Case; Documents Required to Be Filed.

(a) **Conversion of Case to Chapter 7.** Within fourteen (14) days after the entry of an order converting a case to Chapter 7, the Debtor shall file a schedule of assets remaining in the Debtor's possession as of the date of conversion, a list of abandoned property, a list of property against which relief from the automatic stay was granted, a schedule of assets and a schedule of unpaid post-petition obligations or expenses. If the Debtor is an individual, a statement of current monthly income and a means test calculation shall also be timely filed Official Form 122A. The schedules/statements shall be signed by the Debtor under penalty of perjury certifying that the schedules/statements and any attachments have been read by the Debtor and that they are true and correct to the best of the Debtor's knowledge, information, and belief.

(b) **Conversion of Case to Chapter 13.** If a case is converted to a case under Chapter 13, a Statement of Current Monthly Income and Calculation of Commitment Period and Disposable Income Official Form 122C, shall be filed and served on the Chapter 13 Trustee.

Local Bankr. R. 1073-1 Assignment and Reassignment of Cases within the District.

(a) All cases shall be assigned by the Clerk to a Bankruptcy Judge as follows:

(1) those cases in which the Debtor resides or has its principal place of business in Fairfield or Litchfield Counties shall be assigned to the Bridgeport Division;

(2) those cases in which the Debtor resides or has its principal place of business in Middlesex or New Haven Counties shall be assigned to the New Haven Division; and

(3) those cases in which the Debtor resides or has its principal place of business in Hartford, New London, Tolland or Windham Counties shall be assigned to the Hartford Division.

(b) Upon motion to the judge to whom the case has been assigned, and after notice and an opportunity for a hearing, the Clerk shall reassign the case to another Division as ordered by

that judge upon the findings that such reassignment would be in the best interests of the estate and parties in interest.

PART II. OFFICERS AND ADMINISTRATION; NOTICES; MEETINGS; EXAMINATIONS; ELECTIONS; ATTORNEYS AND ACCOUNTANTS

Local Bankr. R. 2002-1 Notice and Service to Creditors and Other Interested Parties.

(a) Notice and Service to Parties in Interest Who Have Requested Service.

In addition to the requirements of any other applicable rule governing service, unless otherwise ordered by the Court, a copy of all motions, pleadings, applications, petitions, and other papers filed in a case shall be timely served on any party in interest who has filed a written demand for such service and on any ECF filer through the Court's CM/ECF system, and a Certificate of Service shall be filed evidencing that such service has been made. When filing the Creditor List in any case, the address of any business entity such as a corporation, partnership, or bank, shall also include in the full address an attention line to an Officer, President, Director, Manager, or General Agent of the business entity, though not necessarily by individual name.

(b) Debtor to Provide Notice and Service if Creditor List not filed.

If the Creditor List required by 11 U.S.C. § 521(a)(1)(A) and Local Bankr. R. 1007-1(a) has not been filed, and notice is required to be served by the Clerk or a party other than the Debtor, the Debtor shall serve the notice and file a Certificate of Service evidencing that such service has been made.

Local Bankr. R. 2002-2 Omnibus Hearing Calendar.

Upon motion or *sua sponte* order, for cause shown in cases under Chapter 9, 11 and 12, the Court may establish an omnibus hearing calendar with pre-set dates established for any and all matters related to that case in the interests of efficient and cost-effective case management.

Local Bankr. R. 2004-1 Rule 2004 Examinations.

(a) Except for the provisions of FRCP 26 (a), (b), (d), (f) and (g), FRBP 7026 and D. Conn. L. Civ. R. 26(a)-(e) and 37 shall apply to examinations and the production of documents under FRBP 2004. Proportionality considerations apply to a request for the production of documents or electronically stored information in connection with a FRBP 2004 examination.

(b) A party in interest seeking an examination pursuant to FRBP 2004(a) and the party to be examined (the "2004 Parties") may agree orally or in writing (a "2004 Agreement") on an examination taking place, the date, time, and place of such examination, and the production of documents pursuant to FRBP 2004(c) and FRBP 9016, without necessity of a motion or subpoena.

(1) A notice of a 2004 Agreement shall be filed with the Court and served upon the following parties: (i) the Debtor; (ii) the trustee, if any; (iii) the United States Trustee; (iv) any official committee; (v) any party that has filed a notice of appearance in the case; and (vi) the proposed witness, examinee, or party producing documents (the "Notice Parties"). Such notice shall include at a minimum the identity of the individual or entity to be examined, the date, time, and place of the proposed examination, a list of the documents to be produced, and the date for production of documents.

(2) Any party in interest shall file and serve upon the 2004 Parties and the Notice Parties an objection to the proposed examination or production of documents within seven (7) days after the filing of the notice of a 2004 Agreement.

(A) If no objection is filed and served within that time, the 2004 Agreement shall be deemed ordered, without requiring the entry of a 2004 order.

(B) If an objection is filed and served within seven (7) days after the filing of the notice of a 2004 Agreement, then, notwithstanding any requirements of the Contested Matter Procedure, *see* Local Bankr. R. 9014-1, (i) a notice of hearing on the objection shall be issued by the Clerk's Office and (ii) the party in interest who filed the objection shall serve the notice of such hearing upon the 2004 Parties and the Notice Parties and shall file a Certificate of Service.

(C) Any objection to a 2004 Agreement shall be no more than five (5) pages and shall state the specific legal and factual basis for the objection.

(D) Failure to comply with the requirements of D. Conn. L. Civ. R. 37 shall be grounds for overruling any objection to a 2004 Agreement.

(3) A written 2004 Agreement between the 2004 Parties as to the date, time, and place of examination and/or documents to be produced is enforceable by a motion to compel or for sanctions without necessity of a Court order or authorized service of a subpoena.

(c) A party in interest that files a motion under FRBP 2004(a) shall serve such motion upon the Notice Parties. The motion shall be accompanied by a proposed order, a notice, and a copy of any subpoena for the production of documents to be served pursuant to FRBP 2004(c) and FRBP 9016.

(1) The notice shall include: (A) an objection deadline of seven (7) days, with such objection deadline set from the date the notice is filed with the Court, and (B) a statement that in the absence of a timely filed objection, the proposed order may enter without further notice and hearing.

(2) Any objection or response to the motion shall be no more than five (5) pages and shall state the specific legal and factual bases for the objection, be filed no later than the response date, and be served upon the 2004 Parties and the Notice Parties. The Court shall schedule a hearing on the matter as soon as is practical.

(3) The failure to file a response or objection pursuant to this Rule shall not prejudice the proposed examinee, witness, or party from whom documents are sought from filing a motion for protective order, to quash the subpoena, or to vacate an order entered pursuant to the motion after the seven (7) day period has passed.

(4) The failure to comply with the requirements of D. Conn. L. Civ. R. 37 shall be grounds for overruling any objection filed to a motion.

Local Bankr. R. 2014-1 Employment of Professionals.

(a) Statement Required by Rule 2016(b).

The statement required by FRBP 2016(b), Form B2030, shall be filed with any application for employment of counsel for the Debtor or any application or motion seeking substitution of counsel for the Debtor. A copy of an engagement or retainer agreement shall be filed with Form B2030. The failure to fully complete and file Form B2030 with any application or motion seeking employment or substitution of employment may result in denial of the application.

(b) Retroactive or *Nunc Pro Tunc* Employment.

(1) If an application to employ a professional is filed within thirty (30) days after the commencement of services provided by that professional, the application shall be deemed contemporaneously filed unless the Court orders otherwise.

(2) If an application to employ a professional is filed more than thirty (30) days after the commencement of services by the professional and the application seeks retroactive or *nunc pro tunc* relief, the application shall include:

(A) an affidavit setting forth the facts relating to the late filing of the application; and

(B) the legal authority the applicant relies on as to why the retroactive or *nunc pro tunc* relief sought is appropriate under applicable law.

(c) Any application seeking approval of a contingent fee shall: (i) have annexed to it the engagement or retainer agreement; and. (ii) sufficient information to confirm its enforceability under applicable laws and the Connecticut Rules of Professional Conduct.

(d) Maintenance of Retainer Funds.

Unless the Court orders otherwise, in a Chapter 9, 11, 12, and 13 case, any professional employed by a Debtor or a trustee shall deposit funds paid upon or in anticipation of the commencement of the case for professional services and expenses to be rendered after the petition date, regardless of the source of funds (*i.e.*, whether received from the Debtor, an insider of the Debtor as defined in 11 U.S.C. § 101(31), or a third party), in a trust account,

clients' funds account, escrow account, or IOLTA account consistent with Rule 1.15 of the Connecticut Rules of Professional Conduct.

(e) Application of Retainer Funds.

Any funds required to be deposited into in a trust account, clients' funds account, escrow account, or IOLTA account consistent with Rule 1.15 of the Connecticut Rules of Professional Conduct shall not be applied to fees earned or expenses incurred by a professional after the petition date absent a prior court order authorizing such application.

Local Bankr. R. 2014-2 Retention of Ordinary Course Professionals.

Where appropriate, the Debtor in a Chapter 11 case in which a trustee has not been appointed, the Debtor in a Chapter 12 or 13 case, or a trustee appointed in a Chapter 7, 11, 12 or 13 case, upon motion and notice, may for good cause seek to hire and compensate certain professionals and advisors in the ordinary course of business, who serve in roles ancillary to the core administration of the estate, or in the ordinary course of the Debtor's business.

Local Bankr. R. 2015-1 Post-Confirmation Reports.

Within forty-five (45) days after the entry of an order confirming a plan in a Chapter 11 case and, until the entry of the final decree, every ninety (90) days thereafter, the debtor-in-possession, trustee, distributor, or plan proponent shall file a report with the Court and serve a copy upon any extant committee appointed in the case, and the United States Trustee, which report shall set forth the action taken and progress made in the consummation of the plan pursuant to 11 U.S.C. § 1106(a)(7).

Local Bankr. R. 2016-1 Compensation of Professionals.

Applications for allowance of compensation and reimbursement of expenses shall, at a minimum:

(a) Include a Fee Application Cover Sheet;

(b) Comply with the Court's Guidelines for Allowance of Compensation and Expense Reimbursement of Professionals; and

(c) Comply with any other applicable guidelines and Court orders.

Local Bankr. R. 2016-2 Compensation of Debtor's Counsel in Chapter 13 Cases.

(a) **Prepetition Retainers.** The amount of any retainer received by the Debtor's counsel paid within one year before the filing of the petition in bankruptcy or agreed to be paid for services rendered or to be rendered in contemplation of or in connection with the bankruptcy case shall be included in the Disclosure of Compensation of Attorney for Debtor, Form B2030.

(b) Unless otherwise ordered by the Court, if the Debtor's counsel's total amount of fees prior to entry of a confirmation order is $4,000.00 or less, the Disclosure of Compensation of Attorney for Debtor, Form B2030 shall be sufficient and the filing of an itemized application for compensation shall be excused.

(c) Nothing in this Rule shall be construed to limit the Court's discretion to review the amount of fees paid to or agreed to be paid to the Debtor's counsel, and to enter appropriate orders allowing, disallowing, disgorging, or reducing such fees.

Local Bankr. R. 2017-1 Committees in Chapter 9, 11, and 12 Cases.

Within five (5) days of the appointment of any committee, the United States Trustee shall file with the Court a list containing the names, addresses, and telephone numbers of persons serving on such committee. If after reasonable efforts a creditors' committee is not constituted, a statement to that effect stating the reasons for not appointing such a committee shall be filed by the United States Trustee with the Court. The United States Trustee shall facilitate the initial organizational meeting of any committee and appropriately advise it of its authority, duties and responsibilities.

PART III. CLAIMS AND DISTRIBUTION TO CREDITORS AND EQUITY INTEREST HOLDERS; PLANS

Local Bankr. R. 3001-1 Proofs of Claim: Secured Claims In Individual Debtor Case.

Proofs of claim filed for secured claims against a residence in individual Debtor cases, in addition to the requirements of FRBP 3001, 3002, and 3002.1 shall:

(a) Be filed in compliance with the Instructions for the Official Proof of Claim Form. For Chapter 13 cases, this rule applies in addition to the requirements of FRBP 3002 and FRBP 3002.1; and

(b) Include as attachments Official Bankruptcy Forms B410-A, B410S-1 and B410S-2, as applicable, in compliance with their instructions.

Local Bankr. R. 3003-1 Filing Proofs of Claim or Interest in a Chapter 9 or 11 Case, Notice to Disputed, Contingent, Unliquidated Creditors.

Unless otherwise ordered, the Debtor in a Chapter 11 case shall serve creditors whose claims are listed on the Schedules as disputed, contingent, or unliquidated with a notice of deadline for filing proofs of claim upon the earlier of forty-five (45) days prior to the proof of claim bar date or the initial confirmation hearing scheduled in the case. Order and Notice to Disputed, Contingent and Unliquidated Creditors.

Local Bankr. R. 3007-1 Claim Objections.

(a) **Contents of the Objection.** Every objection to a claim shall identify the proof of claim, if any, by claim number as set forth in the Claims Register, the claimant, the amount, the priority classification, and the filing date of the proof of claim. If the amount or classification of the claim is disputed, the objection shall state the amount of the claim, if

any, that is not in dispute and the classification considered proper by the objecting party. The objection shall state with particularity the basis for the objection. The objecting party must attach the Local Form 420B Notice of Objection to Claim Form to every objection to a claim.

(b) **Service.** The objecting party shall serve any claim objection and the notice of hearing upon the claimant at the address provided on the proof of claim, and if applicable, upon the claimant's attorney of record. The objecting party shall file a Certificate of Service with the objection.

Local Bankr. R. 3007-2 Omnibus Claim Objection Procedures.

If an omnibus claim objection is to be filed, the objecting party must attach the Local Form 420B Notice of Objection to Claim Form to the omnibus claim objection, and the following procedures shall be followed:

(a) The objecting party shall object to no more than one hundred (100) proofs of claim in one pleading;

(b) Copies of the claims need not be attached to the omnibus claim objection. However, the objecting party shall comply with Local Bankr. R. 3007-1(a) and notify each claimant that a copy of the claim may be obtained from the objecting party upon request; and,

(c) The notice of hearing and objection shall be served in accordance with FRBP 2002(g) and FRBP 7004.

Local Bankr. R. 3007-3 Estimation of Claims.

(a) If a claim is objected to or is filed in an unliquidated amount, the objecting party, the claimant, the trustee, the Debtor in possession, or any plan proponent may file a motion requesting that the claim be estimated in accordance with 11 U.S.C. § 502(c). Unless the Court orders otherwise, filing a motion to estimate commences a contested matter and shall follow the Contested Matter Procedure set forth in Local Bankr. R. 9014-1.

(b) The motion to estimate shall include those purposes (*e.g.*, voting, allowance, etc.) for which estimation is sought, and an explanation of why estimation, as opposed to full trial of the claim objection, is appropriate. As soon as practicable following filing of the motion to estimate, the movant shall consult with the claimant and any objecting party to determine whether either opposes the motion.

Local Bankr. R. 3015-1 Chapter 12 – Confirmation.

Unless the Court orders otherwise, an objection to confirmation of a Chapter 12 Plan shall be filed no later than seven (7) days prior to the date set for the plan confirmation hearing.

Local Bankr. R. 3015-2 Chapter 13 - Confirmation.

(a) Unless the Court orders otherwise, an objection to confirmation of a Chapter 13 Plan shall be filed no later than seven (7) days prior to the date set for the plan confirmation hearing.

(b) Unless the Court orders otherwise, the confirmation hearing will be held after the Proof of Claim Bar Date set in each case has passed. The Debtor's attorney, or the Debtor, if not represented by counsel, must appear at the confirmation hearing unless specifically excused by Court order.

Local Bankr. R. 3016-1 Chapter 11 - Plan.

(a) Extension of Exclusivity Period.

If the Debtor desires an extension of the exclusivity period for filing a Plan of Reorganization, the Debtor shall file a motion prior to the expiration of the exclusivity period requesting the extension that includes a statement of the reason(s) why a plan has not been filed and an appropriate timetable of the steps to be taken in order to file a plan.

(b) Small Business Cases.

If the Debtor desires an extension of the periods provided for filing or confirming a Plan of Reorganization in a small business case as provided in 11 U.S.C. § 1121(e)(3), then the Debtor shall file and serve a motion requesting the extension, as described in subsection (a), upon all parties in interest. The motion must be filed in advance of the expiration of the time periods provided in 11 U.S.C. § 1121(e) to provide at least fourteen (14) days notice of the hearing as required by the Contested Matter Procedure provided for under these rules. Expedited or emergency hearings will be granted only in exceptional circumstances.

Local Bankr. R. 3017-1 Transmission and Notice of Plan and Disclosure Statement.

(a) **Transmittal.** Unless the Court orders otherwise, the proponent of a plan shall transmit all notices and other documents required by FRBP 3017(a).

(b) **Disclaimer Other Than in Small Business Cases.** Except in a case where the Debtor is a small business, before a proposed disclosure statement has been approved by the Court, the proposed disclosure statement shall have on its cover, in boldface type, the following or comparable language:

This is not a solicitation of acceptance or rejection of the plan. Acceptances or rejections may not be solicited until a disclosure statement has been approved by the Bankruptcy Court. This disclosure statement is being submitted for approval but has not been approved by the Court.

Local Bankr. R. 3017-1.1 Consideration of Disclosure Statement in a Small Business Case.

Disclaimer in Small Business Cases. In a case where the Debtor is a small business, if the Court conditionally approves a proposed disclosure statement, the conditionally approved disclosure statement shall have on its cover, in boldface type, the following language, or words of similar import:

The Debtor in this case is a "small business" as defined in the Code. The Debtor has received conditional approval of this Disclosure Statement; the Court will consider final approval, and any timely filed objections thereto, at the time of or before the hearing on confirmation of the plan.

Local Bankr. R. 3017-2 Approval of Disclosure Statement in Small Business Cases.

(a) Procedure for Conditional Approval Under Federal Rule of Bankruptcy Procedure 3017.1.

A plan proponent in a small business case may seek conditional approval of a disclosure statement, subject to final approval after notice and hearing, by filing a motion with the Court contemporaneously with the filing of the proposed Plan of Reorganization. Such motion shall contain a Certificate of Service evidencing service upon the parties and shall be accompanied by a proposed order.

(b) Waiver.

A plan proponent in a small business case may seek to waive the requirement of a disclosure statement because the proposed Plan of Reorganization itself provides adequate information. Such waiver may be sought by motion to be filed contemporaneously with the proposed plan of reorganization.

Local Bankr. R. 3018-1 Certification of Acceptances and Rejections of Chapter 11 Plans.

Unless the Court orders otherwise, not less than two (2) business days prior to the hearing on confirmation, the proponent of a Chapter 11 plan, or other party who receives the ballots accepting or rejecting such plan, shall file with the Court a certification of the amount and number of allowed claims or interests in each class accepting or rejecting the plan. On the basis of the certification, the Court may find that the plan has been accepted or rejected.

Local Bankr. R. 3020-1 Chapter 11 - Confirmation.

Unless the Court orders otherwise, an objection to confirmation of a Chapter 11 Plan of Reorganization shall be filed and served no later than four (4) days prior to the date set for a hearing on confirmation of the plan.

Local Bankr. R. 3022-1 Application for Final Decree.

Unless the Court orders otherwise, the date for filing an application for a final decree in a Chapter 11 case will be set by the Court at the confirmation hearing. The application for the final decree shall: (i) contain a breakdown of the disbursements, as applicable from the commencement of the case, for fees for the Debtor's attorney, other professional fees and expenses, any Chapter 11 trustee fees, and fees for the trustee's attorney; (ii) state the percentage of dividend paid and to be paid, or whether the future dividend percentage is not yet determinable; and (iii) state the steps taken to consummate the plan and whether the initial plan distribution is complete.

PART IV. THE DEBTOR: DUTIES AND BENEFITS

Local Bankr. R. 4001-1 Automatic Stay; Relief from Stay Worksheet.

A Motion for Relief from Stay Worksheet shall be completed and filed with all motions seeking relief under 11 U.S.C. § 362(d) with respect to real property.

Local Bankr. R. 4001-2 Continuation or Imposition of Automatic Stay.

(a) **Motion and Hearing Required**. Any party that seeks a continuation or imposition of the automatic stay under 11 U.S.C. §§ 362(c)(3)(B) or (c)(4)(B) shall file a motion with the Court, on notice to all parties against whom the movant seeks to continue or impose the stay. The motion shall be filed with the petition or as soon as practicable thereafter.

(b) **Content of Motion**. An affidavit or declaration of the movant shall be attached to the motion and shall:

(1) specifically allege the identity of the creditor(s) as to which the movant seeks to continue or impose the stay;

(2) identify, by case number, any and all prior bankruptcy filings by the Debtor;

(3) state whether the Debtor has had more than one previous case pending within the preceding year;

(4) state whether any previous case was dismissed within the preceding year after the Debtor failed to perform any of the acts set forth in 11 U.S.C. § 362(c)(3)(C)(i)(II);

(5) state whether there has been a substantial change in the financial or personal affairs of the Debtor and, if so, support the statement with specific factual allegations;

(6) state whether any creditor moved for relief from the automatic stay in a previous case and, if so, the disposition of that motion; and

(7) allege specific facts entitling the movant to relief.

Local Bankr. R. 4001-3 Use of Cash Collateral and Debtor in Possession Financing.

In order to facilitate the expeditious hearing and review of motions seeking authority to use cash collateral and seeking approval of debtor in possession financing, a checklist for each motion pursuant to 11 U.S.C. § 363 and 11 U.S.C. § 364 shall be completed and attached to the motion and shall clearly and concisely disclose the following:

(a) **Contents of Motion.** The following provisions, to the extent applicable, are added to the enumerated lists of material provisions set forth in FRBP 4001(b)(1)(B), (c)(1) and (d)(1)(B):

(1) pricing and economic terms, including letter of credit fees, commitment fees, any other fees, and the treatment of costs and expenses to the lender, any agent for the lender, and their respective professionals;

(2) any effect on existing liens of the granting of collateral or adequate protection provided to the lender and any priority or super priority provisions;

(3) any carve-outs, or subordinations, from liens or super priorities;

(4) any cross-collateralization provision that elevates pre-petition debt to administrative expense (or higher) status or that secures pre-petition debt with liens on post-petition assets (which liens the creditor would not otherwise have by virtue of the pre-petition security agreement or applicable law);

(5) any provision that applies the proceeds of post-petition financing to pay, in whole or in part, pre-petition debt or which otherwise has the effect of converting pre-petition debt to post-petition debt (*i.e.*, any "roll-up" provision);

(6) any provisions that would affect the Court's power to consider the equities of the case under 11 U.S.C. § 552(b)(1);

(7) Any terms that provide that the use of cash collateral or the availability of credit will cease on (i) the filing of a challenge to the lender's pre-petition lien or the lender's pre-petition claim based on the lender's pre-petition claim; (ii) entry of an order granting relief from the automatic stay other than an order granting relief from the stay with respect to material assets; (iii) the grant of a change of venue with respect to the case or any adversary proceeding; (iv) management changes or the departure, from the Debtor, of any identified employees; (v) the expiration of a specified time for filing a plan; or (vi) the making of a motion by a party in interest seeking any relief (as distinct from an order granting such relief);

(8) any provision establishing a deadline for, or otherwise requiring, the sale of property of the estate or filing or confirming a plan;

(9) in jointly administered cases, terms that govern the joint liability of Debtors including any provision described in subdivision (e) of this rule; and

(10) any provision for the funding of non-debtor affiliates with cash collateral or proceeds of the loan, as applicable, and the approximate amount of such funding.

(b) **Disclosure of Efforts to Obtain Financing and Good Faith.** A motion for authority to obtain credit pursuant to 11 U.S.C. § 364 shall describe in general terms the efforts of the trustee or debtor in possession to obtain financing, the basis upon which the debtor in possession or trustee determined that the proposed financing is on the best terms available, and material facts bearing on the issue of whether the extension of credit is being extended in good faith.

(c) Inadequacy of Notice After Event of Default.

(1) If the proposed order contains a provision that modifies or terminates the automatic stay or permits the lender to enforce remedies after an event of default, either the proposed order shall require at least seven (7) days' notice to the trustee or debtor in possession, the United States Trustee and each committee appointed under 11 U.S.C. §§ 1102 or 1114 (or the largest creditors if no committee has been appointed under 11 U.S.C. § 1102), before the modification or termination of the automatic stay or the enforcement of the lender's remedies, or the motion shall explain why such notice provision is not contained in the proposed order.

(2) If the proposed order contains a provision that terminates the use of cash collateral, either the proposed order shall require at least five (5) days' notice before the use of cash collateral ceases (provided that the use of cash collateral conforms to any budget in effect) or the motion shall explain why such notice provision is not contained in the proposed order.

(d) Joint Obligations. In jointly-administered cases, if one or more Debtors will be liable for the repayment of indebtedness for funds advanced, used or transferred to or for the benefit of another Debtor, the motion and the proposed order shall describe, with specificity, any provisions of the agreement or proposed order that would affect the nature and priority, if any, of any inter-debtor claims that would result if a Debtor were to repay debt incurred by or for the benefit of another Debtor.

(e) Investigation Period Relating to Waivers and Concessions as to Prepetition Debt. If a motion seeks entry of an order in which the Debtor stipulates, acknowledges or otherwise admits to the validity, enforceability, priority, or amount of a claim that arose before the commencement of the case, or of any lien securing the claim, either the proposed order shall include a provision that permits a committee appointed under 11 U.S.C. § 1102 and other parties in interest to undertake an investigation of the facts relating thereto, and proceedings relating to such determination, or the motion shall explain why the proposed order does not contain such a provision. The minimum time period for such committee or other party in interest to commence, or to file a motion to obtain authority to commence, any related proceedings as representative of the estate shall ordinarily be sixty (60) days from the date of entry of the order authorizing the use of cash collateral or the obtaining of credit, or such other period of time as the Court orders for cause shown prior to the expiration of such period.

(f) Content of Interim Orders. A motion that seeks entry of an emergency or interim order before a final hearing under FRBP 4001(b)(2) or (c)(2) shall describe the amount and purpose of funds sought to be used or borrowed on an emergency or interim basis and shall set forth facts to support a finding that immediate or irreparable harm will be caused to the estate if immediate relief is not granted before the final hearing.

(g) Provisions of the Proposed Order.

(1) Findings of Fact.

(A) A proposed emergency or interim order shall include a finding that immediate and irreparable loss or damage will be caused to the estate if immediate financing or authorization of use of cash collateral is not obtained and should state with respect to notice only that the hearing was held pursuant to FRBP 4001(b)(2) or (c)(2), that notice was given to certain parties in the manner described, and that the notice was, in the Debtor's belief, the best available under the circumstances.

(B) A proposed order may include factual findings as to notice and the adequacy thereof.

(C) To the extent that a proposed order incorporates by reference to, or refers to a specific section of, a pre-petition or post-petition loan agreement or other document, the proposed order shall also include a statement of such section's import.

(2) Cross-Collateralization and Rollups. Unless otherwise determined by the Court, a proposed order approving cross-collateralization or a rollup shall include language that reserves the right of the Court to unwind, in whole or in part, after notice and hearing, the post-petition protection provided to the pre-petition lender or the pay down of the pre-petition debt, whichever is applicable, in the event that there is a timely and successful challenge to the validity, enforceability, extent, perfection, or priority of the pre-petition lender's claims or liens, or a determination that the pre-petition debt was undersecured as of the petition date, and the cross-collateralization or rollup unduly advantaged the lender.

(3) Waivers, Consents, or Amendments with Respect to the Loan Agreement. A proposed order may permit the parties to enter into waivers or consents with respect to the loan agreement or amendments thereof without the need for further Court approval provided that (i) the agreement as so modified is not materially different from that approved, (ii) notice of all amendments is filed with the Court, and (iii) notice of all amendments (other than those that are ministerial or technical and do not adversely affect the Debtor) are provided in advance to counsel for any committee appointed under 11 U.S.C. §§ 1102 or 1114, all parties requesting notice, and the United States Trustee.

(4) Conclusions of Law. A proposed order may provide that the Debtor is authorized to enter into the loan or other agreement, but it shall not state that the Court has examined and approved the loan or other agreement, unless specifically authorized by the Court.

(5) Order to Control. The proposed order shall state that to the extent that a loan or other credit agreement differs from the order, the Court Order shall control.

(6) Statutory Provisions Affected. The proposed order shall specify those provisions of the Bankruptcy Code, Bankruptcy Rules, and Local Rules relied upon as authority

for granting relief, and shall identify those sections that are, to the extent permitted by law, being limited or abridged.

(7) **Conclusions of Law Regarding Notice.** A proposed order may contain conclusions of law with respect to the adequacy of notice under 11 U.S.C. §§ 363 and 364 and FRBP 4001.

Local Bankr. R. 4002-1 Documents to Be Delivered to Trustee Prior to Section 341 Creditors' Meeting.

(a) In Chapter 7 cases, no later than seven (7) days prior to the first scheduled meeting of creditors, the Debtor shall deliver to the trustee in a legible form the documents listed in Appendix I with the completed Domestic Support Obligation Disclosure and Personal Injury Information Forms, to the extent that they apply, and such other documents as the trustee reasonably requests and as he/she deems relevant to and in aid of the prompt administration of the case and the bankruptcy estate. The documents shall be delivered in the form reasonably requested by the trustee. If documents apply but are not available, the Debtor shall inform the trustee why the documents are not available. The Debtor shall use best efforts to provide copies of the documents that are unavailable to the trustee as soon as possible thereafter.

(b) In Chapter 13 cases, no later than seven (7) days prior to the first scheduled meeting of creditors, the Debtor shall deliver to the trustee in a legible form the documents listed in Appendix J with the completed Domestic Support Obligation Disclosure and Personal Injury Information Forms, to the extent that they apply, and such other documents as the trustee reasonably requests and as he/she deems relevant to and in aid of the prompt administration of the case and the bankruptcy estate. The documents shall be delivered in the form reasonably requested by the trustee. If documents apply but are not available, the Debtor shall inform the trustee why the documents are not available. The Debtor shall use best efforts to provide copies of the documents that are unavailable to the trustee as soon as possible thereafter.

(c) Unless the Court orders otherwise, copies of all payment advices or other evidence of payment received by an individual Debtor within sixty (60) days before the date of the filing of the petition from any employer of the Debtor:

(1) shall not be filed with the Court; and

(2) shall be provided to the Chapter 7 Trustee, Chapter 12 Trustee, or Chapter 13 Trustee, as the case may be, no later than seven (7) days prior to date of the initially scheduled Section 341 Creditors' Meeting.

Local Bankr. R. 4004-1 Entry of Discharge in Individual Chapter 11, Chapter 12, and Chapter 13 Cases.

(a) In accordance with the applicable provisions of 11 U.S.C. §§ 1141, 1228, and 1328, an individual Debtor seeking the entry of a discharge in Chapter 11, Chapter 12, and Chapter 13 cases shall file a Certification and Application for Entry of Discharge (the "Application"), on forms approved for use by the Court.

(b) The Application forms approved for use in Chapter 11, Chapter 12, and Chapter 13 cases are:

(1) Chapter 11: Certification and Application for Entry of Discharge After Completion of Plan

(2) Chapter 11: Certification and Application for Entry of Discharge Before Completion of Plan Payments

(3) Chapter 12: Certification and Application for Entry of Discharge After Completion of Plan Payments

(4) Chapter 12: Certification and Application for Entry of Discharge Before Completion of Plan Payments – Hardship Discharge

(5) Chapter 13: Certification and Application for Entry of Discharge After Completion of Plan Payments

(6) Chapter 13: Certification and Application for Entry of Discharge Before Completion of Plan Payments – Hardship Discharge

(c) An Application filed in accordance with this Rule will be reviewed as soon as practicable after filing and will be approved or set for a hearing at the discretion of the Court.

PART V. COURTS AND CLERKS

Local Bankr. R. 5003-1 Clerk of Court - General Authority.

(a) **Clerk of Court Authorized to Amend Form of Creditor List.** The Clerk of Court shall be authorized to change the form of the Creditor List required by Local Bankr. R. 1007-1(a) to meet requirements of any automated case management system employed by the Clerk. The Bankruptcy Clerk shall give appropriate notice to the bar of any such change in form.

(b) **Clerk of Court Authorized to Refuse Certain Forms of Payment.** The Bankruptcy Clerk shall maintain a list of all attorneys and law firms whose checks or credit or debit cards have been dishonored. The Bankruptcy Clerk may refuse future check, credit or debit card payments from such attorneys or firms and require an alternative form of payment.

Local Bankr. R. 5005-1 Filing Papers - Requirements.

D. Conn. L. Civ. R. 10 applies to pleadings and documents filed with the Bankruptcy Court.

Conn LBR 5010-1 Reopening Cases.

A motion to reopen a case pursuant to 11 U.S.C. § 350(b) and FRBP 5010 shall state with specificity the reason for the reopening. The Court, upon a finding of cause, may grant the motion. A filing fee for a case reopened pursuant to 11 U.S.C. § 350(b) and FRBP 5010 shall be required unless the case is reopened to correct an administrative error, or on account of actions relating to the Debtor's discharge.

Local Bankr. R. 5011-1 Withdrawal of Reference.

A motion for withdrawal of the reference provided under 28 U.S.C. §§ 1334 and 157 shall be filed with the Clerk of the Bankruptcy Court. The Clerk of the Bankruptcy Court shall promptly transmit the motion to the Clerk of the United States District Court and notify the movant of the transmission. The movant shall notify all other parties of the transmission. Following transmission of the motion to the Clerk of the District Court, all further filings with respect to the motion shall be filed with the Clerk of the District Court.

Local Bankr. R. 5073-1 Photography, Broadcasting, Recording, and Televising.

Absent an order of the Court, no person may photograph, electronically record, televise, or broadcast a judicial proceeding. This rule shall not apply to ceremonial proceedings with permission of the Court or electronic recordings by an official Court reporter or other authorized Court personnel.

PART VI. COLLECTION AND LIQUIDATION OF THE ESTATE

Local Bankr. R. 6004-1 Sale of Estate Property – General.

(a) Unless property of the estate is to be sold free and clear of liens with liens attaching to the proceeds pursuant to 11 U.S.C. § 363(f), the notice of a proposed sale of property of the estate is sufficient if given pursuant to FRBP 2002(a)(2).

(b) If property of the estate is to be sold free and clear of liens with liens attaching to the proceeds pursuant to 11 U.S.C. § 363(f), in addition to the notice provided for in (a) of this rule, the moving party shall file a motion which names as a respondent all entities asserting a lien on or interest in the property to be sold, describes with particularity the nature of the lien or interest claimed, how it is perfected and whether or not the lien or interest is disputed by the movant. The motion and proposed order shall also detail what items will be paid at the time of consummation of the sale and what items will be paid pursuant to a future order of the Court.

(c) No trustee, appraiser, auctioneer, officer, director, stockholder, agent, employee, or relative of a trustee, appraiser, or auctioneer, shall directly or indirectly purchase any of the property of any bankruptcy estate in which such trustee, appraiser, or auctioneer is employed, retained or engaged.

(d) Unless otherwise ordered by the Court: (i) a public sale shall be advertised at least fourteen (14) days before the sale, although the trustee may require further advertising; (ii) the property to be sold shall be open to public inspection for such reasonable period prior to the sale as the trustee may determine; and (iii) an auctioneer shall, before receiving bids, announce the terms of sale, including the statement that no sale is final without the approval of the trustee and the Bankruptcy Court if required by the order authorizing the auction. If the auction is conducted on the Internet/electronically, this announcement shall be posted

(e) A purchaser at any public sale shall not be entitled to a refund on account of an immaterial discrepancy between the assets offered for sale by the auctioneer and the assets as listed in any inventory that is provided to bidders prior to the sale. Any property that, because of reclamation proceedings or for other reasons, is not included in the sale, shall be segregated and conspicuously marked "not included in sale," and such fact shall be announced by the

auctioneer before the sale. Except upon prior approval of the Court, only items constituting assets of the estate being administered shall be sold at any sale held pursuant to provisions of the Bankruptcy Code, and such sales shall not be conducted in conjunction with any non-bankruptcy sale.

(f) When the trustee acts as auctioneer, he or she shall receive no compensation in excess of the amount provided by the Bankruptcy Code and Rules.

(g) Unless the Court orders otherwise, trustees must be in attendance throughout all in-person auction sales and attend all subsequent closings for the sale of property of the estate.

(h) The sanctions that may be imposed for violation of this rule, include, but are not limited to, disgorgement, fines, and the disqualification of a person from future employment on behalf of bankruptcy estates.

(i) Internet Auction Mechanisms

(1) With prior Court approval, after appropriate notice as required by FRBP 2002(a), a Chapter 7 Trustee, Chapter 11 Trustee, Chapter 11 debtor- in-possession, Chapter 12 Trustee, and Chapter 13 Debtor (collectively, the "Movant"), may sell any property of the estate by public auction through the use of an automated Internet auction, listing or brokerage mechanism ("Internet Auction Mechanism").

(2) In any motion requesting such approval, the movant must:

(A) Identify the name and uniform resource locator(s) (URL) of the proposed Internet Auction Mechanism;

(B) State why the movant believes that use of the Internet Auction Mechanism is in the best interests of the estate;

(C) Disclose whether the movant has or any party in interest is known to have any connections with the proposed Internet Auction Mechanism or any expected bidder;

(D) Disclose all fees associated with use of the Internet Auction Mechanism;

(E) Disclose whether use of the Internet Auction Mechanism is subject to rules, policies, procedures or terms or conditions and, if so summarize any such rules, policies, procedures or terms or conditions that are likely to result in any restrictions on bidding for the asset(s) proposed to be sold or limitations on the estate representative in offering asset(s) for sale with full or partial reserve or otherwise controlling the determination to sell each asset;

(F) Identify the mechanism for payment to the estate;

(G) Unless the Internet Auction Mechanism is maintained and operated by the auctioneer represent that, to the best knowledge of the movant, the Internet Auction Mechanism will not provide auction services or any other services beyond access to its automated on-line services and related customer support; and

(H) Request authority to:

(i) comply with any rules, policies, procedures, or terms or conditions of the Internet Auction Mechanism disclosed in the motion and enter into any required agreements in support thereof;

(ii) consummate such sale(s); and

(iii) pay any and all fees associated with use of the Internet Auction Mechanism, each without further order of the Court.

(j) Nothing in this Rule shall limit applicability of the requirements of Local Bankr. R 6005-1 with respect to any auctioneer hired by an estate representative to provide services beyond access to an Internet Auction Mechanism.

(k) Unless the Court orders otherwise, a listing placed on an Internet Auction Mechanism shall state the bankruptcy case name and number and that the sale procedure has been approved by the United States Bankruptcy Court for the District of Connecticut.

Local Bankr. R. 6004-2 Sales and Sale Procedures Motions.

(a) **Applicability of Rule.** Except as otherwise provided in these Local Rules or ordered by the Court, this rule applies to motions to sell property of the estate under 11 U.S.C. § 363(b) ("Sale Motions") and motions seeking approval of sale, bid or auction procedures in anticipation of or in conjunction with a Sale Motion ("Sale Procedures Motions").

(b) **Sale Motions.** Except as otherwise provided in these Local Rules, the Bankruptcy Code, the Bankruptcy Rules or an Order of the Court, all Sale Motions shall attach or include the following:

(1) If applicable, a copy of the proposed purchase agreement, or a form of such agreement substantially similar to the one the Debtor reasonably believes it will execute in connection with the proposed sale.

(2) A copy of a proposed form of sale order.

(3) A request, if necessary, for the appointment of a consumer privacy ombudsman under 11 U.S.C.§ 332.

(4) **Provisions to be Highlighted.** The Sale Motion must highlight material terms, including but not limited to: (a) whether the proposed form of sale order and/or the underlying purchase agreement constitutes a sale or contains any provision of the type set forth below; (b) the location of any such provision in the proposed form of order or purchase agreement; and (c) the justification for the inclusion of the following material provisions:

(A) **Sale to Insider.** If the proposed sale is to an insider, as defined in 11 U.S.C. § 101(31), the Sale Motion must: (a) identify the insider; (b) describe the insider's relationship to the Debtor; and (c) set forth any measures taken to ensure the fairness of the sale process and the proposed transaction.

(B) **Agreements with Management.** If a proposed buyer has discussed or entered into any agreements with management or key employees regarding compensation or future employment, the Sale Motion must disclose: (a) the material terms of any such agreement; and (b) what measures have been taken to ensure the fairness of the sale and the proposed transaction in the light of any such agreements.

(C) **Releases.** The Sale Motion must highlight any provisions pursuant to which an entity, individual or party is being released or claims against any entity are being waived or otherwise satisfied. The Sale Motion must also describe the consideration, if any, to the estate for any such release.

(D) **Private Sale/No Competitive Bidding.** The Sale Motion must disclose whether an auction is contemplated, and highlight any provision in which the Debtor has agreed not to solicit competing offers for the property subject to the Sale Motion or to otherwise limit shopping of the property.

(E) **Closing and Other Deadlines.** The Sale Motion must highlight any deadlines for the closing of the proposed sale or deadlines that are conditions to closing the proposed transaction.

(F) **Good Faith Deposit.** The Sale Motion must highlight whether the proposed purchaser has submitted or will be required to submit a good faith deposit and, if so, the conditions under which such deposit may be forfeited.

(G) **Interim Arrangements with Proposed Buyer.** The Sale Motion must highlight any provision pursuant to which a Debtor is entering into any interim agreements or arrangements with the proposed purchaser, such as interim management arrangements (which, if out of the ordinary course, also must be subject to notice and a hearing under 11 U.S.C. § 363(b) of the Bankruptcy Code) and the terms of such agreements.

(H) **Use of Proceeds.** The Sale Motion must highlight any provision pursuant to which a Debtor proposes to release sale proceeds on or after the closing without further Court order, or to provide for a definitive allocation of sale proceeds between or among various sellers/lenders or collateral.

(I) **Tax Exemption.** The Sale Motion must highlight any provision seeking to have the sale declared exempt from taxes under 11 U.S.C. § 1146(a) of the

Bankruptcy Code, the type of tax (e.g., recording tax, stamp tax, use tax, capital gains tax) for which the exemption is sought. It is not sufficient to refer simply to "transfer" taxes and the state or states in which the affected property is located.

(J) **Record Retention.** If the Debtor proposes to sell substantially all of its assets, the Sale Motion must highlight whether the Debtor will retain, or have reasonable access to, its books and records to enable it to administer its bankruptcy case.

(K) **Sale of Avoidance Actions.** The Sale Motion must highlight any provision pursuant to which the Debtor seeks to sell or otherwise limit its rights to pursue avoidance claims under Chapter 5 of the Bankruptcy Code.

(L) **Requested Findings and Order as to Successor Liability.** The Sale Motion and proposed Order should highlight any provisions relating to the proposed purchaser's responsibility as a successor.

(M) **Sale Free and Clear of Unexpired Leases.** The Sale Motion must highlight any provision by which the Debtor seeks to sell property free and clear of a possessory leasehold interest, license, or other right.

(N) **Credit Bid.** The Sale Motion must highlight any provision by which the Debtor seeks to allow, disallow, or affect in any manner, credit bidding pursuant to 11 U.S.C. § 363(k).

(O) **Relief from Bankruptcy Rule 6004(h).** The Sale Motion must highlight any provision whereby the Debtor seeks relief from the fourteen-day stay imposed by FRBP 6004(h).

(P) **Carve-Outs and/or "Gifts".** The Sale Motion must highlight any provision by which the lender(s) or party-in-interest is allowing the distribution of its collateral for the benefit of others.

(Q) **Residual Assets.** The Sale Motion must describe what residual assets, if any, will exist following the Sale Closing.

(c) **Sale Procedures Motions.** A Debtor may file a Sale Procedures Motion seeking approval of an order (a "Sale Procedures Order") approving bidding and auction procedures either as part of the Sale Motion or by a separate motion filed in anticipation of an auction and a proposed sale. The Court will only schedule a hearing to consider approval of bidding and sale procedures in accordance with the applicable Rules. The Sale Procedures Motion should highlight the following provisions in any Sale Procedures Order:

(1) **Provisions Governing Qualification of Bidders.** Any provision governing an entity becoming a qualified bidder, including but not limited to, an entity's obligation to:

(A) Deliver financial information by a stated deadline to the Debtor and other key parties (ordinarily excluding other bidders);

(B) Demonstrate its financial wherewithal to consummate a sale;

(C) Maintain the confidentiality of information obtained from the Debtor or other parties or execute a non-disclosure agreement; and

(D) Make a non-binding expression of interest or execute a binding agreement.

(2) **Provisions Governing Qualified Bids.** Any provision governing a bid being a qualified bid, including, but not limited to:

(A) Any deadlines for submitting a bid and the ability of a bidder to modify a bid not deemed a qualified bid;

(B) Any requirements regarding the form of a bid, including whether a qualified bid must be (a) marked against the form of a "stalking horse" agreement or a template of the Debtor's preferred sale terms, showing amendments and other modifications (including price and other terms), (b) for all of the same assets or may be for less than all of the assets proposed to be acquired by an initial or "stalking horse" bidder, or (c) remain open for a specified period of time;

(C) Any requirement that a bid include a good faith deposit, the amount of that deposit, and under what conditions the good faith deposit is not refundable; and

(D) Any other conditions a Debtor requires for a bid to be considered a qualified bid or to permit a qualified bidder to bid at an auction.

(3) **Provisions Providing Bid Protections to "Stalking Horse" or Initial Bidder.** Any provisions providing an initial or "stalking horse" bidder a form of bid protection, including, but not limited to the following:

(A) **No-Shop or No-Solicitation Provisions**. Any limitations on a Debtor's ability or right to solicit higher or otherwise better bids;

(B) **Break-Up/Topping Fees and Expense Reimbursement.** Any agreement to provide or seek an order authorizing break-up or topping fees and/or expense reimbursement, and the terms and conditions under which any such fees or expense reimbursement would be paid;

(C) **Bidding Increments.** Any requirement regarding the amount of the initial overbid and any successive bidding increments; and

(D) **Treatment of Break-Up and Topping Fees and Expense Reimbursement at Auction.** Any requirement that the "stalking horse" bidder receive a "credit" equal to the break-up or topping fee and or expense reimbursement when bidding at the auction and in such case whether the "stalking horse" is deemed to have waived any such fee and expense upon submitting a higher or otherwise better bid than its initial bid at the auction.

(4) **Modification of Bidding and Auction Procedures.** Any provision that would authorize a Debtor, without further order of the Court, to modify any procedures regarding bidding or conducting an auction.

(5) **Closing with Alternative Backup Bidders.** Any provision that would authorize the Debtor to accept and close on alternative qualified bids received at an auction in the event that the bidder selected as the "successful bidder" at the conclusion of the auction fails to close the transaction within a specified period.

(d) Provisions Governing the Auction. Unless otherwise ordered by the Court, the Sale Procedures Order shall:

(1) Specify the date, time, and place at which the auction will be conducted, and the method for providing notice to parties of any changes thereto; and

(2) Provide that each bidder participating at the auction will be required to certify in writing that it has not engaged and will not engage in any collusion with respect to the bidding or the sale.

(e) Expedited Sale Disclosures. In connection with any hearing to approve the sale of substantially all assets at any time before sixty (60) days after the filing of the petition, a motion for an order authorizing a sale procedure and hearing or the sale motion itself when regularly noticed, should include factual information on the following points:

(1) Creditors' Committee. If a creditors' committee existed pre-petition, indicate the date and manner in which the committee was formed, as well as the identity of the members of the committee and the companies with which they are affiliated.

(2) Counsel for Committee. If the pre-petition creditors' committee retained counsel, indicate the date counsel was engaged and the selection process, as well as the identity of committee counsel.

(3) Sale Contingencies. Statement of all contingencies to the sale agreement, together with a copy of the agreement.

(4) Creditor Contact List. If no committee has been formed, a list of contact persons, together with available contact information for each of the twenty (20) largest unsecured creditors.

(5) Administrative Expenses. Assuming the sale is approved, an itemization and an estimate of administrative expenses relating to the sale to be incurred before closing and the source of payment for those expenses.

(6) Deductions from Proceeds of Sale. Itemize all deductions, including any

applicable taxes, that are to be made from gross sale proceeds and include a brief description of the basis for any such deductions. If the amount of a deduction will not be fixed until the date of the closing, an estimate may be provided.

(7) **Debt Structure of Debtor.** A brief description of the Debtor's debt structure, including the amount of the Debtor's secured debt, priority claims, and general unsecured claims.

(8) **Need for Quick Sale.** An extensive description of why the assets of the estate must be sold on an expedited basis. Include a discussion of alternatives to the sale.

(9) **Negotiating Background.** A description of the length of time spent in negotiating the sale, and which parties in interest were involved in the negotiation, along with a description of the details of any other offers to purchase, including, without limitation, the potential purchaser's plans in connection with the retention of the Debtor's employees.

(10) **Marketing of Assets.** A description of the manner in which the assets were marketed for sale, including the period of time involved and the results achieved.

(11) **Decision to Sell.** The date on which the Debtor accepted the offer to purchase the assets.

(12) **Relationship of Buyer.** A statement identifying the buyer and setting forth all of the buyer's (including its officers, directors and shareholders) connections with the Debtor, creditors, any other party in interest, their respective attorneys, accountants, the United States Trustee or any person employed in the office of the United States Trustee.

(13) **Post Sale Relationship with Debtor.** A statement setting forth any relationship or connection the Debtor (including its officers, directors, shareholders, and employees) will have with the buyer after the consummation of the sale, assuming it is approved by the Court.

(14) **Relationship with Secured Creditors.** If the sale involves the payment of all or a portion of secured debt(s), a statement of all connections between Debtor's officers, directors, employees, or other insiders and each secured creditor involved (for example, release of insider's guaranty).

(15) **Insider Compensation.** Disclosure of current compensation received by officers, directors, key employees, or other insiders pending approval of the sale.

(16) **Successor Liability.** Any sale requesting findings or the entry of relief regarding successor liability shall delineate the scope and form of notice and the relief requested.

Local Bankr. R. 6005-1 Employment of Auctioneers.

(a) Unless otherwise ordered by the Court, the following shall apply to the employment of all auctioneers and the conduct of auctions.

(b) The employment of an auctioneer shall be submitted to the Court for approval upon application setting forth:

(1) The need for an auctioneer's services;

(2) A description of the property to be sold, its estimated value, and the location thereof;

(3) How the auctioneer is to be paid, and, if payment is to be made from assets of the estate, whether the estate will have adequate funds with which to pay the auctioneer's fee;

(4) If the items to be auctioned constitute collateral, entirely or in part, whether or not the party claiming a security interest in such collateral has agreed to pay any or all of the auctioneer's expenses;

(5) To the extent additional compensation or reimbursement of assistants is sought, how many assistants will be required to help the auctioneer and why such assistance is required, a statement by the trustee in support of the number required and the expense to be incurred for each assistant, based upon an hourly fee; and

(6) A bond obtained for the purpose of the auction in an amount such as will exceed the estimated value of the property to be sold by at least twenty-five percent (25%), a copy of which shall be attached to the application to employ.

(c) An auctioneer employed with Court approval shall not act until he or she gives in each estate, at his or her own expense, a surety bond in favor of the United States of America, to be approved by and in such sum as may be fixed by the Court, conditioned upon:

(1) The faithful and prompt accounting for all monies and property which may come into his or her possession as auctioneer;

(2) Compliance with all rules, orders, and decrees of the Court; and

(3) The faithful performance of his or her duties in all respects.

(d) Said bond shall contain a provision that it may not be canceled or terminated without sixty (60) days' notice being given to the Clerk and the United States Trustee. In lieu of a bond in each case, an auctioneer may be permitted to file a blanket bond covering all cases in which he or she may act. Such blanket bond shall be in favor of the United States of America, shall be in the sum of one million dollars ($1,000,000.00), and shall be conditioned for each estate on the same terms as bonds in separate estates.

(e) Compensation and Expenses.

(1) Any allowance of compensation and reimbursement of expenses to an auctioneer shall be paid only upon proper application and subject to the approval of the Court.

(2) An auctioneer shall be reimbursed for reasonable and necessary expenses directly related to the sale, including printing, advertising, insurance, and bond costs. Where the auctioneer has a blanket bond, the auctioneer may be reimbursed a proportionate amount of the costs, based upon the value of the assets sold by the auctioneer in the particular estate. When directed by the trustee to transport goods, the auctioneer shall be reimbursed for expenditures related thereto. No travel expenses shall be allowed except as ordered by the Court. The auctioneer may be reimbursed for his or her expenses only if the application for reimbursement is supported by a sworn affidavit, setting forth the specific expenses incurred and the necessity for such. Vouchers, invoices, receipts, or other appropriate supporting documentation shall accompany the application. Where disbursements were made for advertising, copies of the actual advertisements shall be attached to the affidavit.

(f) A person shall not at any time, directly or indirectly, designate or refer to himself or herself as "Official United States Auctioneer," or as "Official Bankruptcy Auctioneer," or use any similar title or designation which states expressly or by implication that such person is an officer of the United States District Court or Bankruptcy Court, or that such person holds any permanent designation by the Court as an auctioneer.

(g) Every auctioneer acting hereunder shall at all times keep proper records of all transactions and shall submit a report of each sale which shall include the following information:

(1) The time and place of sale;

(2) The gross amount of the sale and when property is sold in lots, the items in each lot and the amount received for each lot, with the name of the purchaser, as well as any bulk bid;

(3) An itemized statement of the expenditures, disbursements, and commissions allowable under this Rule, together with appropriate vouchers as described in paragraph (e)(2) above; and

(4) Whenever articles are sold free and clear of liens, with the liens to attach to the proceeds, the articles and liens shall be itemized separately.

(h) Except as otherwise ordered by the Court, a trustee shall not delegate any of his or her fiduciary responsibilities to an auctioneer.

(i) The sanctions that may be imposed for violation of this Rule, include, but are not limited to, the disqualification of the person from future employment on behalf of bankruptcy estates.

Local Bankr. R. 6005-2 Employment of Appraisers.

(a) In addition to Local Bankr. R. 2014-1.1, all applications for the appointment of an appraiser or a valuation expert (“appraiser”) shall be filed with the Court for approval. Said applications shall contain at a minimum the following information:

(1) A statement setting forth in what manner and by whom the costs of the appraisal will be paid, and if payment is to be made from assets of the estate, a statement that the estate has adequate funds with which to pay the appraisal fee;

(2) The name and address of the appraiser and the estimated maximum amount of the appraisal fee;

(3) A description of the item(s) to be appraised, their estimated value and the time required for the appraisal; and

(4) If the appraiser sought to be appointed will incur travel expenses in connection with the appraisal, an explanation as to why a local appraiser is unavailable or unsuitable.

(b) All applications for allowance of appraiser's fees for services rendered or reimbursement of expenses which exceed one thousand dollars ($1,000.00) or more, shall, in addition to the requirements set forth in the Bankruptcy Code and FRBP 2016(a), contain the following information:

(1) The date of the order of appointment;

(2) In concise form, a general narrative statement of the nature of the services provided; and

(3) A statement, based upon records prepared contemporaneously with the services rendered, indicating:

(A) The dates the services were rendered;

(B) The identity of the person or persons rendering such services; and

(C) The total compensation sought by each person providing the services.

Local Bankr. R. 6070-1 Tax Returns and Tax Refunds in Chapter 12 and 13 Cases.

The Chapter 12 and Chapter 13 Trustees are authorized to endorse on behalf of any Chapter 12 or Chapter 13 Debtor for deposit to the Chapter 12 or Chapter 13 Trustee's trust fund account, any and all federal, state, or local income tax refunds payable to the Debtor.

PART VII. ADVERSARY PROCEEDINGS

Local Bankr. R. 7001-1 Adversary Proceedings - General.

An adversary complaint shall be filed in the division in which the related Debtor case is pending.

Local Bankr. R. 7002-1 Adversary Proceeding Cover Sheet.

Every adversary proceeding shall be accompanied by an adversary proceeding cover sheet, Official Form B1040.

Local Bankr. R. 7005-1 Service of Pleadings and Other Papers by Electronic Means.

Parties are permitted to make service through the Bankruptcy Court's CM/ECF system, as permitted by FRCP 5(b)(2)(E) and D. Conn. L. Civ. R. 5. This rule is not applicable to the service of process of a summons and complaint, which must be served in accordance with FRBP 7004.

Local Bankr. R. 7007-1 Motion Practice.

Motion practice in adversary proceedings follows the Local Rules for the District Court, including without limitation D. Conn. L. Civ. R. 7 and 56.

Local Bankr. R. 7007-2 Briefs.

(a) Length.

A brief shall not exceed twenty-five (25) pages (excluding the table of contents and table of authorities). A reply brief shall not exceed ten (10) pages. Permission to file a brief in excess of these page limitations will be granted only on motion, filed at least seven (7) days before the deadline for the filing, upon a showing of cause.

(b) *Amicus* Briefs.

An *amicus* brief may not be filed without leave of the Court. The brief shall specifically set forth the interest of the *amicus curiae* in the outcome of the litigation.

Local Bankr. R. 7012-1 Motions to Dismiss.

D. Conn. L. Civ. R. 12 applies to motions to dismiss adversary proceedings, including the requirement that any represented party moving to dismiss a complaint of a self-represented party/*Pro Se* Filer/Litigant shall file and serve as a separate document a "Notice to Self-Represented Litigant Concerning Motion to Dismiss".

Local Bankr. R. 7016-1 Pretrial Procedures.

(a) Initial Pretrial Conference-Initial Pretrial Order/Initial Joint Pretrial Order.

Upon the filing of the complaint, a summons will be issued which will contain a date and time for the initial pretrial conference in the adversary proceeding. Unless otherwise ordered, an initial pretrial order/initial joint pretrial order shall be filed seven (7) days before the initial Pretrial Conference scheduled in the adversary proceeding. If the defendant(s) has/have not appeared seven (7) days prior to the initial pretrial conference, the plaintiff shall file the initial pretrial order. If the defendant(s) has/have appeared, the parties shall file an initial joint pretrial order. The initial pretrial order/initial joint pretrial order shall contain the following information:

(1) a summary of the claims and defenses of each party;

(2) a list of any additional matters that might aid in scheduling or the disposition of the case; and

(3) the signature of each attorney.

(b) Conflict Between Orders and Local Rules.

If a conflict exists between any pretrial order, joint pretrial order, scheduling order, or other order entered by the Court in an adversary proceeding and these Local Bankruptcy Rules, the provisions of the order(s) of the Court shall control in the adversary proceeding.

Local Bankr. R. 7026-1 Discovery; Duty of Disclosure; Filing of Discovery

D. Conn. L. Civ. R. 26 applies to discovery in adversary proceedings.

Local Bankr. R. 7037-1 Discovery Disputes.

D. Conn. L. Civ. R. 37 applies to discovery disputes.

Local Bankr. R. 7055-1 Default and Default Judgment.

(a) Request for Entry of Default by Bankruptcy Clerk.

Before the Clerk or Deputy Clerk is required to enter a default, the party requesting such entry shall file with the Court a written request for entry of default, submit a proposed form of entry of default, and file any other materials required by FRCP 55(a).

(b) Compliance with Service Members Civil Relief Act (50 U.S.C. § 3931)

The plaintiff shall file an affidavit in compliance with 50 U.S.C. § 3931 with any motion for default judgment against an individual.

(b) Order Scheduling Hearing on Default Judgment; Failure to Obtain Default Judgment.

A hearing on a Motion for Default Judgment may be scheduled by the Court. If a defendant has been in default for ninety (90) days or more, the Court may require the plaintiff to move for entry of a default judgment. If the plaintiff fails to do so within the prescribed time, the Court may dismiss the proceeding, without prejudice, as to that defendant.

Local Bankr. R. 7056-1 Summary Judgment.

D. Conn. L. Civ. R. 56 applies to motions for summary judgment, including the requirement that any represented party moving for summary judgment against a self-represented party/*Pro Se* Filer/Litigant shall file and serve as a separate document a "Notice to Self-Represented Litigant Concerning Motion for Summary Judgment".

Local Bankr. R. 7067-1 Registry Fund.

(a) Deposit.

The deposit of any money into the registry of the Court shall be as directed by written order of the Court. Funds so deposited shall be invested by the Clerk of the Court in accordance with the terms of the order. All payments for deposit shall be made payable to "Clerk, U.S. Bankruptcy Court" and are accepted subject to collection.

(b) Withdrawal.

The withdrawal of funds in the registry shall be in accordance with a written order of the Court. The disbursement of accrued interest shall only be made if the order so provides. Any order for the distribution of less than all funds and accrued interest on deposit with the Court shall be denominated "Order for Partial Distribution from the Registry of the Court," otherwise the order shall be treated as an Order for Final Distribution. Whenever an Order for Final Distribution from the registry of the Court does not provide for the distribution of all funds or interest on deposit, the Clerk of the Court shall pay such funds into the Treasury of the United States. This rule applies to both adversary proceedings and bankruptcy cases.

(c) Statement of Payee's Name, Address, and Tax Identification Number.

All orders authorizing disbursement from the registry shall state the payee's name, address, tax identification number, redacted to include only the last four (4) digits of the number, and the dollar amount to be paid. Prior to receiving any disbursement from the registry, each payee shall deliver to the Clerk of the Court an executed IRS Form W-9.

PART IX. GENERAL PROVISIONS

Local Bankr. R. 9010-1 Appearances.

An attorney entering an appearance in a case under the Bankruptcy Code, or any matter commenced by a complaint or motion, shall first file an appearance with the Court and serve the same upon the Debtor or the debtor-in-possession, any trustee, any committee and its counsel, the United States Trustee, appearing counsel, and parties requesting notice, and, if an adversary proceeding, any party to such proceeding.

Local Bankr. R. 9013-1 Form of Pleading of Certain Contested Matters.

Motions seeking relief under the following sections of the Bankruptcy Code shall comply with the requirements of FRBP 7010:

Section 362(d) - Relief from the automatic stay;
Section 363(c) - Use of cash collateral;
Section 363(f) - Sale free and clear of interests in property;
Section 364(d) - Obtain or incur debt secured by a senior or equal lien;
Section 365(a)- (f) - Assumption or rejection of executory contracts and unexpired leases;
Section 506 - Determination of secured status; and
Section 522(f) - Avoidance of fixing of liens.

Local Bankr. R. 9013-2 Motions Filed with Petition in Chapter 11 Cases.

(a) Any motion or application in which the Debtor requests a hearing (a "First Day Hearing") or the entry of an order with less than seven (7) days' notice and prior to the earlier of the creditors' committee formation meeting or the Section 341 meeting of creditors shall be governed by this Local Rule. Requests for relief under this Local Rule shall be confined to matters required to avoid irreparable harm to the assets of the estate and to maintain ongoing business operations and such other matters as the Court may deem appropriate.

(b) Within forty-eight (48) hours of the entry of an order entered under this Local Rule ("First Day Order"), the Debtor shall serve copies of all motions and applications filed with the Court as to which a First Day Order has been entered, as well as all First Day Orders, on all other parties entitled to notice of such applications and motions under applicable rules, and such other entities as the Court may direct.

Local Bankr. R. 9014-1 Contested Matters and the Contested Matter Procedure.

(a) The Federal Rules of Bankruptcy Procedure govern all Contested Matters filed with the Court. Unless an application or motion does not follow the Contested Matter Procedure or is an exception to the Contested Matter Procedure as set forth in sections (m) and (n) of this Local Rule, the application or motion should follow the Contested Matter Procedure.

(b) Unless otherwise provided by applicable statute or rule, or unless the Court orders otherwise, this Local Bankr. R. 9014-1 shall be referred to as the "Contested Matter Procedure" and shall govern all Contested Matters as defined by Federal Rule of Bankruptcy Procedure 9014.

(c) A Certificate of Service demonstrating that service has been made upon all parties entitled

thereto by applicable Rule or Court order shall be filed with all documents referred to in this Contested Matter Procedure.

(d) **Commencement of Contested Matter.** All Contested Matters shall contain a PROPOSED ORDER and a NOTICE. A list of the Court's preferred forms of proposed orders for common motions is set forth here: The NOTICE shall include:

(1) A response deadline of fourteen (14) days or twenty-one (21) days, as applicable. *See,* FRBP 2002(a) and 9014. The response deadline shall be set from the date the NOTICE was filed with the Court (the "Response Date"); and

(2) A statement that in the absence of a timely filed response, the proposed order may enter without further notice and hearing.

(e) **Response to Contested Matter.**

Any response to the Contested Matter shall be no more than ten (10) pages and shall state the specific legal and factual bases therefore, be filed no later than the Response Date, and be served upon the party who filed the Contested Matter and all parties originally served with the Contested Matter.

(f) **Notice of Hearing.**

Upon the timely filing of a response, a NOTICE OF HEARING shall be sent by the Clerk's Office to the party who filed the Contested Matter. The party who filed the Contested Matter shall then serve the NOTICE OF HEARING on all parties to whom service of the Contested Matter was initially made.

(g) **Reply.**

Any Reply to the response shall be no more than five (5) pages and shall be filed no later than three (3) days before the scheduled hearing on the Contested Matter.

(h) **Initial Hearing**. The first hearing scheduled in a Contested Matter (the "Initial Hearing"), will not be an evidentiary hearing at which witnesses may testify or documents will be admitted into evidence unless:

(1) The Court gives notice to the parties that such hearing will be an evidentiary hearing;

(2) The Motion or Application requests emergency relief and is made at the commencement of the case;

(i) **Procedures for Initial non-evidentiary Hearing.** The Court will conduct a status/scheduling conference to address the Contested Matter, which, unless otherwise ordered, will include stipulations concerning admissibility of documentary or other evidence, stipulations of fact, the filing and/or service of witness and exhibit lists with proposed exhibits, and the scheduling of an evidentiary hearing.

(j) Continuances: Request for Continuance of Initial Hearing.

(1) At least seven (7) days before the scheduled Initial Hearing, a request by a party in interest for a continuance of the Initial Hearing, must be made by filing a Request for Continuance of Initial Hearing form.

(2) If the Request for a Continuance of the Initial Hearing is granted, a NOTICE OF FINAL HEARING, which states the date and time thereof, shall be sent by the Clerk's Office to the party who filed the matter. The party who filed the matter shall then serve the NOTICE OF FINAL HEARING on all parties on whom service was originally made.

(3) If the Request for a Continuance of Initial Hearing is not granted, the Contested Matter will be heard as scheduled.

(k) Continuances: Motion for Continuance of Final Hearing.

(1) At least three (3) business days before the date set for the Final Hearing, a Request for Continuance of the Final Hearing shall be made by motion and served upon all parties on whom service was originally made. The motion shall state in detail the reasons for the requested continuance and state whether any prior continuance has been granted.

(2) If the Request for a Continuance of the Final Hearings granted, a Notice of Continued Final Hearing, which states the date and time thereof, shall be sent by the Clerk's Office to the party who filed the Contested Matter. The party who filed the Contested Matter shall then serve the Notice of Continued Final Hearing on all parties on whom service was originally made.

(3) Unless the motion for continuance is granted by the Court at least one (1) business day before the Final Hearing, the Contested Matter will be heard as scheduled.

(l) Extension of Time Due to Continuance of Hearing.

Unless an order granting a continuance states otherwise, a continuance of the hearing on the Contested Matter automatically extends the time for filing and serving reply documents in accordance with the procedure governing the filing of a Reply as set forth in paragraph 9014-1(f).

(m) Motions/Applications that do not follow Contested Matter Procedure and *may* be scheduled for a hearing.

All motions or applications that do not follow the Court's Contested Matter Procedure and may be scheduled for a hearing are set forth in Appendix M.

(n) Exceptions to the Contested Matter Procedure.

Exceptions to the Contested Matter Procedure and will be set for a hearing are set forth in Appendix N.

Local Bankr. R. 9019-1 Motions to Compromise.

(a) Filing

(1) A motion to compromise a dispute under FRBP 9019 shall be filed in the bankruptcy case.

(2) A motion to compromise an adversary proceeding shall be filed in the main bankruptcy case and in the adversary proceeding. It shall bear the style of the main bankruptcy case and the adversary proceeding.

(b) Notice.

(1) Motions to compromise adversary proceedings are governed by Local Bankr. R. 9007-1.

(2)

(A) Motions to compromise and motions that contemplate a dismissal of an objection to discharge under 11 U.S.C. § 727 shall identify the cause of action and any consideration paid or agreed to be paid and shall be served on all creditors and parties in interest.

(B) The Clerk shall issue a notice of hearing for any such motion that includes the information that creditors and parties in interest may seek to intervene in the adversary proceeding if they choose. The movant's counsel shall serve the notice, the motion and the proposed order on all creditors in the Debtor's case, and shall file a Certificate of Service in the adversary proceeding.

Local Bankr. R. 9019-2 Alternative Dispute Resolution.

(a) Referral of a Case or Proceeding to Mediation.

The Court, either *sua sponte* or upon the motion of any party, may order parties to participate in mediation and other forms of non-binding alternative dispute resolution ("ADR") and may order the parties to allocate expenses in such proportion as the Court finds appropriate. The Court may also stay proceedings and discovery during the pendency of an ADR process.

(b) Other ADR Methods.

Upon motion and agreement of the parties, the Court may submit a case or proceeding to binding arbitration, early neutral evaluation, or mini-trial.

Local Bankr. R. 9027-1 Removal.

(a) Filing.

A removed claim or cause of action related to a bankruptcy case shall be filed in the Bankruptcy Court as an adversary proceeding and assigned directly to a Bankruptcy Judge. The filing shall contain a completed Adversary Proceeding Cover Sheet.

(b) Filing Fee.

The adversary proceeding filing fee is due upon the filing of the notice of removal. A fee is not required if the party removing the case is the Debtor, or child support creditor. If the party removing the case is the trustee or Debtor in possession, a motion to defer filing fee may be filed along with a proposed order.

(c) Attachments.

A notice of removal shall include a copy of the docket sheet, and shall be accompanied by a copy of all pleadings from the Court from which the claim or cause of action is removed. The plaintiff(s) and defendant(s) shall be identical to the plaintiff(s) and defendant(s) in the Court from which the claim or cause of action is removed.

(d) Compliance with FRBP 7008 and FRBP 7012(b).

If a complaint or an answer for an adversary proceeding fail to comply with FRBP 7008 and FRBP 7012(b), the filing party shall file an amended complaint and/or amended answer addressing entry of final orders within five (5) days after the filing of the notice of removal.

Local Bankr. R. 9036-1 Notice by Electronic Transmission.

Subject to applicable rule or statute, parties are authorized to serve notices through the Court's CM/ECF system. However, neither service of process for a summons and complaint in an adversary proceeding under FRBP 7004 or of a subpoena under FRBP 9016 may be made by electronic transmission.

Local Bankr. R. 9070-1 Exhibits.

Unless the Court orders otherwise, all parties are required to comply with the procedure for filing proposed exhibits using the CM/ECF system in accordance with Appendix A.

Local Bankr. R. 9077-1 Sealed Documents.

D. Conn. L. Civ. R. 5(e) applies to proceedings before the Bankruptcy Court.

Local Bankr. R. 9083-1 Attorneys - Admission to Practice.

D. Conn. L. Civ. R. 83.1 applies to motions for admission of attorneys *pro hac vice*.

Local Bankr. R. 9083-2 Attorneys - Discipline and Disbarment.

D. Conn. L. Civ. R. 83.2 applies to suspension or disbarment of counsel by the Court.

Local Bankr. R. 9083-3 Attorneys - Requirement of Local Counsel.

D. Conn. L. Civ. R. 83.1(c) applies to motions for admission of attorneys *pro hac vice*, and the requirement to maintain a local office.

Local Bankr. R. 9083-4 Attorneys - Withdrawals.

D. Conn. L. Civ. R. 7(e) applies to motions for withdrawal of an appearance.

Local Bankr. R. 9083-5 Change of Contact Information or Name.

(a) Attorneys.

When an attorney who is a registered user of CM/ECF changes the attorney's business address, e-mail address, telephone number, facsimile number, or name, the attorney must modify this information in CM/ECF, following the procedures set forth in the Administrative Procedures for Electronic Case Filing Manual, within three (3) business days of any change.

(b) Non-Attorneys.

Any individual or entity filing a proof of claim, or participating in a bankruptcy case *pro se* must file notice of any modification to its mailing address within seven (7) days of any change.

APPENDIX A

ADMINISTRATIVE PROCEDURES FOR ELECTRONIC FILING

Administrative Procedures for Electronic Case Filing

Effective February 2018

1. SCOPE OF ELECTRONIC FILING

(a) Short Title

The Administrative Procedures for Electronic Case Filing may be abbreviated and referred to as the "Administrative Procedures" or if addressed individually, as "ECF Procedure # " and are available in their current version on the Court's website: www.ctb.uscourts.gov

(b) Definitions

"Electronic Case Filing" (ECF) refers to documents filed in electronic format.

"Conventional Filing" refers to documents filed in paper format.

"Filer" refers to any entity with an approved login and password, registered for full use of the ECF system in compliance with these Administrative Procedures.

"User" refers to a person or entity with an approved login and password, registered for limited use of the ECF system in compliance with ECF Procedure number 2(b) below.

(c) Electronic Case Filing

The Court will only accept documents filed in electronic format in compliance with these Administrative Procedures, unless otherwise authorized by order of the court, and as excepted in paragraph (d) below. Failure to file electronically, except as authorized in subsections (d) and (e) below, will result in the issuance of a Court's Motion to Dismiss or Strike, and may result in the eventual dismissal or striking of the non-compliant document. Persistent non-compliance with these procedures may result in referral for disciplinary action.

(d) Conventional Filing Authorized

The following documents may be filed conventionally:

(1) documents under seal pursuant to an order of the court allowing the filing conventionally in compliance with ECF procedure number 8;

(2) documents filed by *Pro se* parties;

(3) proofs of claim;

(4) motions to proceed pro hac vice;

(5) other limited documents or filings, as ordered by the Court.

(e) Exemption from Electronic Filing

Exemption from electronic filing is available only upon motion granted for cause shown in exceptional circumstances, and attorneys seeking an exemption must follow the instructions in section 15 of these Administrative Procedures.

2. REGISTRATION and TRAINING

(a) Required Registration Procedure for Filers

1. Eligibility for Registration as a Filer

The following persons or entities are eligible to register as Filers in the Court's ECF system: (a) attorneys admitted to practice in the United States Bankruptcy Court for the District of Connecticut, including those admitted pro hac vice; (b) case trustees; (c) Assistant United States Trustees; (d) Assistant United States Attorneys; and (e) other entities the Court determines appropriate. In order to register as a Filer, an entity must complete a Filer Registration form (ECF Form 1), or Pro Hac Vice Registration form (ECF Form 1a). Registration will be made in a form prescribed by the Clerk of Court and requires the Filing User's name, bar number, address, telephone number, Internet e-mail address and, in the case of an attorney, a declaration that the attorney is authorized to practice in this Court. Members of a Filer's staff are encouraged to participate in the on-line ECF training tutorial.

2. Training for Filers

Filers will be required to complete training as required by the Clerk of Court. Applicants may train through the Court's on-line ECF Training Tutorial. All applicants will be required to successfully complete the Court's On-line Test for Filers in order to be assigned a filer login and password, unless the filer specifies that they have a current login and password from another CM/ECF court. On-line training may be accessed at any time. If the on-line test is not satisfactorily completed, the Clerk of Court, may require the applicant to participate in online training. Applicants with a current and valid ECF registration and login issued by another United States Bankruptcy Court will be issued a login and password upon completion of the first two pages of the registration form.

3. Submission of registration forms

The signed registration form and on-line test, if applicable, may be submitted either by regular mail to The United States Bankruptcy Court, 450 Main Street, Hartford, CT 06103, ATTN: ECF Registration Desk, or via email at ctb_ecf_help@ctb.uscourts.gov.Attorneys who are acting trustees must register and will receive different logins for use as either an attorney and/or a trustee.

4. Address changes

Registered Filers shall immediately notify the Court of any changes in the Filer's e-mail address by sending an e-mail to ctb_ecf_help@ctb.uscourts.gov.

(b) Required Registration Procedure for Users

1. Eligibility to register as User

Except as provided in ECF Procedure 1(d)("Conventional Filing Authorized"), the following persons or entities are eligible to register as Users in the Court's ECF system: Any entity, including entities who file proofs of claim and/or requests for notice but are not appearing as parties in the case. In order to register as a User, an entity must complete a User registration form (ECF Form 2). Users shall consult the Court's CM/ECF on-line training tutorial

www.ctb.uscourts.gov. for instructional material on how to file proofs of claim, requests for notice and other events available to Users.

2. Training for Users

Users will be required to complete the Court's On-line ECF training tutorial and successfully complete the on-line test for Users in order to be assigned a User login and password. The signed User registration form (ECF Form 2) and a completed on-line test, should be mailed to the United States Bankruptcy Court, 450 Main St., Hartford, CT 06103, Attn: ECF Registration Desk or by email to ctb_efc_help@ctb.uscourts.gov. Registered Users shall immediately notify the Court of any changes in the User's email address by sending an e-mail to ctb_ecf-help@ctb.uscourts.gov. Applicants with a current and valid ECF registration and login issued by another United States Bankruptcy Court will be issued a login and password upon completion of the first two pages of the registration form.

(c) Suspension or Revocation of Use

The Court may, for cause, enter an order suspending or revoking a Filer's or User's access to the ECF system. Further, the Clerk of Court, upon information received, which indicates potential risk or harm to the ECF system may, without prior notice, temporarily suspend participation in the ECF system by any Filer or User, and shall provide prompt notification of such action to the Filer or User. In the event of suspension or revocation the Filer or User will be required to correct any condition that led to the suspension or revocation, and may be required to take the online training in order to have access to the system restored.

3. LOGINS, PASSWORDS AND SECURITY`

(a) Login and Password

Once the registration and on-line test are reviewed for accuracy, the Court will send an email message notifying the Filer or User of the login and password assigned. The email message ensures that the Filer or User has a properly functioning email address which will be used by the Court's ECF system.

(b) Password Security

Every Filer or User is required to protect the security of the assigned password. If there is any reason to believe the security of the assigned password may have been compromised, the Filer or User must immediately notify the Court's Information Technology Department by email to CTB_ECF_Help@ctb.uscourts.gov. A Filer or User may be subject to civil liability, court sanctions or other consequences for failure to take required action in connection with the security of the assigned password. Members of a Filer's or User's staff are encouraged to participate in either on-site or on-line ECF training, but will not receive a separate login and password. Filers or Users are responsible for the entries made by any person using that Filer's or User's password and login.

4. ELECTRONIC NOTICE AND SERVICE

a) Request, waiver and consent

Registration as a Filer constitutes waiver of the right to personal service or first class mail service. Registration as a Filer also constitutes a written request for, and consent to, electronic service via receipt of a "Notice of Electronic Filing" from ECF of all filed documents, including Orders and Judgments, to which the Filer is entitled. The Notice of Electronic Filing that is automatically generated by the courts Electronic Filing System constitutes service or notice of the filed document on Filers. Parties who are not Filers, must be provided service of any pleading or other

document electronically files in accordance with the Federal Rules of Civil Procedure, Federal Rules of Bankruptcy Procedure and the Local Rules.

b) Certificates of Service

Except with regard to the method of service authorized by these Procedures, the provisions of the Federal Rules of Bankruptcy Procedure continue to govern the content of a certificate of service. A certificate of service must be included with all documents filed electronically, indicating that service was accomplished through the Notice of Electronic Filing for-parties or counsel who are registered Filers, or specify how service was made if the party or counsel being served is not a registered Filer.

c) Personal Service Requirements Not Abrogated

Nothing contained in this procedure relieves counsel of the burden of providing personal service under Fed. R. Bankr. P. 7004, 9014 or Fed. R. Civ. P. 4.

d) Rule 9006(f)

When there is a right or requirement to do some act or undertake some proceeding within a prescribed period after service, the additional three days created by Fed. R. Bankr. P. 9006(f) shall apply.

5. CONSEQUENCES OF ELECTRONIC FILING

(a) Filing and Entry on the Docket

Once an electronic transmission of a document is made in accordance with these administrative procedures, and has been received by the Court, the document shall be considered filed for all purposes as required by the Federal Rules of Bankruptcy Procedure and the Local Rules of Bankruptcy Procedure of this Court. The document will be entered on the court docket kept by the clerk pursuant to Rule 5003.

(b) Official Record

When a document has been filed through ECF, the official record is the electronic recording of the document as stored by the Court, and the filing party is bound by the document as filed. A document filed through ECF is deemed filed at the date and time stated on the Notice of Electronic Filing from the Court. Documents filed pursuant to these procedures as a conventional paper filing will be time stamped and converted to electronic format and stored in the ECF system and the electronic version will become the official record.

(c) Filing Date and Time

Filing a document electronically does not alter the filing deadline for that document. Unless otherwise ordered, filing must be completed before midnight local time where the Court is located in order to be considered timely filed that day. Conventional paper filings will be deemed filed as of the date and time they are file stamped by the Clerk's Office.

(d) Appropriate Title of ECF Documents

A Filer or User electronically filing a pleading or other document shall be responsible for designating the appropriate title for that pleading or other document by selecting among the categories provided through the ECF system.

(e) Corrections

In the event that a docket entry must be corrected, the clerk's office will correct the entry and the electronic Filer or User will receive notification of the corrected docket entry via NEF.

(f) Payments of Required Fees

(1) Fees to be paid using Internet Credit Card Procedure

All required fees, with the exception of those listed in section below, must be promptly paid using Pay.gov. In the event that internet credit card processing is not available at the time of filing, payment must be made within 48 hours by going to the CM/ECF Utilities Menu - "Internet Payments Due".

(2) Fees to be paid by mail or at the clerk's office. The following fees must be paid by mail, or in person at the Clerk's office:

- Sanctions
- Treasury (small dividends)
- Treasury (registry funds)
- Any replacement check for a filing fee
- Inter-district Index fee
- Rental deposits due in connection with pre-petition eviction judgment against an individual who rentsresidence.

6. COURT ORDERS

(a) Entry of Orders

The Clerk of Court shall enter all orders and judgments in ECF, which shall constitute entry on the docket kept by the Clerk under Rules 5003 and 9021. The electronic signature of the Court or the entry of the order on the docket shall have the same force and effect as if manually signed and docketed as a conventional filing.

(b) Filing Proposed Orders.

Unless otherwise ordered by the Court, all proposed orders shall be filed with the underlying motion or application which shall be docketed as one event and one document. When applicable, the proposed order should contain the language set forth on this Court's website. The submission requirements may change from time to time, and Filers should consult these procedures, and the Court's CM/ECF website for any amendments. www.ctb.uscourts.gov

(c) Notice to Filers of Orders.

Immediately upon the entry of an order or judgment in a case, including an adversary proceeding, the Clerk's office shall electronically transmit to all Filers who represent the contesting parties and to such other Filers and Users as the Court shall direct, a Notice of Electronic Filing. Electronic transmission of the Notice of Electronic Filing constitutes the notice required by Rule 9022 and service shall be deemed complete upon transmission.

(d) Notice to Others of Orders.

Immediately upon the entry of an order or judgment in a case, including an adversary proceeding, the Clerk's office or such others as the court shall direct, shall give notice to contesting parties who are neither Filers nor Users, and to such other entities as the Court shall direct, in accordance with the Federal Rules of Bankruptcy Procedure.

7. FILING FORMAT REQUIREMENTS

(a) Definitions. "Electronically Generated Text" is electronic text generated by converting or printing to Portable Document Format (PDF) from the original word processing file, so that the text of the document may be electronically searched and copied. "Scanned Material" is an electronic image of text or other material in PDF format produced by a scanning or imaging process.

(b) PDF Requirements. All documents transmitted via the ECF system shall be in Electronically Generated text, so that the text of the document may be searched and copied, except as provided in subsection (c) below.

(c) Attachments, Exhibits and Other Documents. Unless otherwise ordered, all exhibits for evidentiary hearings and trials shall be submitted in PDF format to the ECF system. All attachments, exhibits, and other documents not available as Electronically Generated Text (i.e., those that must be scanned) shall be transmitted to the ECF system, as Scanned Material in PDF format.

(d) Size Limitations Per Transmission. Each transmission to the ECF system shall not exceed ten (10) megabytes total file size. Files which exceed ten (10) megabytes shall be broken into smaller files and transmitted to the ECF system as attachments to the main document.

8. FILING OF DOCUMENTS UNDER SEAL

(a) Definition. A document may be filed under seal only upon a court order or pursuant to statute or rule.

(b) Filing Requirements. Unless otherwise ordered by the Court, a motion to file a document under seal shall be filed electronically. The motion shall not contain confidential or privileged information. The proposed order authorizing the filing of a document under seal shall be filed electronically unless otherwise ordered by the court. A document ordered to be filed under seal shall be filed electronically via the courts CM/ECF system. The event to be used is “file a sealed document”, which appears under the miscellaneous section of the CM/ECF events. The sealed document will be unavailable for viewing by everyone except for, the Judge, Clerk, Chief Deputy and the filer of the sealed document.

(c) Protection of Privacy Interests. Any entity may file a motion seeking an order limiting electronic access to or prohibiting the electronic filing of certain specifically identified materials on the grounds that such material is subject to protected privacy interests and that electronic access or electronic filing of those materials is likely to prejudice those privacy interests. If the Court determines that access should be limited or that electronic filing would unduly prejudice those privacy interests, then the materials shall be filed as ordered by the Court. Unless otherwise directed, the Court order determining access to or prohibiting the electronic filing shall be filed electronically.

9. RETENTION REQUIREMENTS

(a) Retention of Original Signatures. Petitions, lists, schedules, statements, amendments, pleadings, affidavits, and other documents that must contain original signatures or that require verification under Rule 1008 or an unsworn declaration as provided in 28 U.S.C.§ 1746, shall be filed electronically by Filers and Users. The documents containing the original signature must be retained by the Filer or User who files such a pleading, document, or other matter for five (5) years after the closing of the case or proceeding. This retention does not affect or replace any other retention period required by other applicable laws or rules. Paper documents containing original signatures or verification received by the court from pro se filers, or as otherwise ordered by the court, will be retained and/or disposed of by the court pursuant to procedures as established by the director of the Administrative Office of the United States Courts.

(b) Production of Documents. On the request of the Court or other authorized entities, the Filer or User must provide original documents for review.

(c) Sanctions. Failure to maintain original documents for the specified period shall subject the Filer or User to sanctions.

1. SIGNATURES

(a) Electronic Filing Constitutes Signature. Except as provided in section 9 of the Administrative Procedures, the transmission by a Filer or User to the ECF system of any document constitutes any required signature of that Filer or User on such document. The Filer need not manually sign a transmitted document. The transmission is the equivalent of a signed paper for all purposes, including, without limitation, the Federal Rules of Bankruptcy Procedure, including Rule 9011, the Bankruptcy Code, and the Local Bankruptcy Rules of this Court.

(b) Electronic Filing Constitutes Certification. The transmission by a Filer or User of any document constitutes certification by the Filer or User that all persons indicated on such document have signed the document and have executed an original prior to electronic filing with the Court.

(c) Form of Electronic Signatures.

(1) Required Information for Filers and Users. A document transmitted via ECF shall include a signature block setting forth the Filer's or User's name, complete address, telephone number, email address, and the Filer's Connecticut's federal court bar registration number and firm affiliation, if applicable, preceded by a signature line on which is typed "/s/ Name" where the Filer's or User's signature would otherwise appear in a signed document.

(2) Required Information for Other Entities. A document transmitted via ECF requiring or containing signatures of entities who are not Filers or Users shall either (a) show an image of such signature as it appears in the original signed document, or (b) bear the name of the signatory preceded by "/s/ Name" typed in the space where the signature would otherwise appear in a signed document, accompanied by the signature block information recited in subsection (c)(1) above. When an original signature is required, or has been executed, it must be maintained in accordance with Procedure 9(a) above.

(3) Multiple Attorney/Party Signatures. A document requiring or containing signatures of more than one entity or counsel shall contain the signature information recited in subsections (c)(1) and/or (c)(2) above.

2. TECHNICAL FAILURE

A Filer or User whose ECF filing is made untimely as a result of technical failure may through motion seek appropriate redress from the Court. Filers and Users are responsible for consulting the Court's website to determine any scheduled system unavailability due to maintenance. Technical difficulties should be reported to the Court's ECF Help desk immediately at www.ctb_ecf_help@ctb.uscourts.gov. Conventional filings may be authorized by the Clerk's Office in the event of recurrent or persistent ECF system failure or other technical failure, if time is of the essence

3. PUBLIC ACCESS

(a) Public Access at the Court. The public may view all documents in the ECF System at no charge at any divisional office of the Court during regular business hours 9 am to 4 pm, Monday through Friday The Clerk's offices are located in Hartford, New Haven and Bridgeport.

(b) Internet Access. Internet access to the ECF system is limited to Public Access to Court Electronic Records ("PACER") system subscribers. Filers and Users may take advantage of the "one free look" provided with the Notice of Electronic Filing to download documents referenced in each Notice of Electronic Filing. In accordance with the Bankruptcy Court Fee Schedule established pursuant to 28 U.S.C. § 1930, User fees are charged for accessing certain detailed case information. Information regarding subscribing to PACER is available on the Court's web site at www.ctb.uscourts.gov and at the clerk's offices. The one free look is available for fifteen (15) days from the date the document was entered on the docket.

(c) Copies And Certified Copies. Copies and certified copies of electronically filed documents may be purchased at the Clerk's Office. The fee for copying and certification will be in accordance with 28 U.S.C. § 1930 and Judicial Conference Policy.

4. PRIVACY

In compliance with the policy of the Judicial Conference of the United States, and the EGovernment Act of 2002, and in order to promote electronic access to case files while also protecting personal privacy and other legitimate interests, parties shall refrain from including, or shall partially redact where inclusion is necessary, the following personal data identifiers from all documents and pleadings filed with the Court, including exhibits thereto, whether filed electronically or conventionally, unless otherwise ordered by the Court or required by statute, the Federal Rules of Bankruptcy Procedure, or the Official Bankruptcy Forms:

(a) Social Security Numbers. If an individual's social security number must be included in a pleading, only the last four digits of that number should be used, with the exception of the Statement of Social Security Number Form B121.

(b) Names of Minor Children. If the involvement of a minor child must be mentioned, only the initials of that child should be used. On Schedule I of Official Bankruptcy Form 6, list the relationship and age of the debtor's dependents (e.g., Son, Age 6);

(c) Dates of Birth. If an individual's date of birth must be included in a pleading, only the year should be used. On Schedule I of Official Bankruptcy Form 6, list the age of each of the debtor's dependents;

(d) Financial Account Numbers. If financial account numbers are relevant, only the last four digits of these numbers should be used. On Schedules D, E, and F of Official Bankruptcy Form 6, debtors, if they so choose, may include their full account numbers to assist the trustee and creditors.

NOTE: In compliance with the E-Government Act of 2002, a party wishing to file a document containing the personal data identifiers listed above may file an un-redacted document under seal. This document shall be retained by the Court as part of the record. The Court may, however, still require the party to file a redacted copy for the public file. The responsibility for redacting personal identifiers rests solely with counsel and the parties. The Clerk will not review documents for compliance with this procedure.

5. REGISTRATION FORMS

When completing any of the following forms and accompanying test, please return them either via email at ctb_ecf_help@ctb.uscourts.gov or by mail to the Office of the Bankruptcy Court Clerk, 450 Main Street, Hartford, CT 06103, Attn: ECF Registration. We will contact you regarding your registration and password after review of the submitted information.

ECF Form No 1. Filer Registration Form

ECF Form No1a. Pro Hac Vice Filer Registration Form

ECF Form No 2. User Registration Form

6. MOTION FOR EXEMPTION FROM ELECTRONIC FILING OVERVIEW AND PROCEDURES

Overview

All documents filed in any case or adversary proceeding must be filed electronically, unless otherwise ordered by the Court upon motion granted for cause shown. The Court will not refuse any document for filing, but attorneys

who file documents conventionally without obtaining an exemption order risk dismissal or striking of the document, and may be subject to sanctions.

***Pro Se* Filers/litigants**

Parties who are not attorneys are not subject to mandatory electronic filing procedure for applying for exemption. No blanket exemptions will be granted to attorneys. Exemption from Electronic Filing must be sought on a case by case basis. A Motion for Exemption should be submitted to the Court. The motion should be submitted in paper with the first paper document submitted for filing. Documents submitted without a motion will not be refused for filing, but may result in the issuance of a Court's Motion to Dismiss or Strike, which will be set for hearing before the assigned judge.

Not-yet-trained exemption

The attorney must take the necessary on line courses to become familiar on how to file documents electronically through and include a reference to that in the motion for exemption.

Trained-but-no-login exemption

Attorneys who have completed ECF training but who have not yet obtained a login and password may be granted an exemption for 15 days to complete their preparation for ECF filing.

Other-circumstances exemption

In addition to the exemptions listed above, the Court may grant exemptions from electronic filing where exceptional circumstances justify such relief. The circumstances should be described in detail in the motion. Exemptions for exceptional circumstances will be made on a case by case basis, and orders granting the exemption will apply only in the particular case in which the order was entered.

Out-of-district attorneys

The Court's electronic filing requirements and the exemptions thereto apply to all attorneys, whether or not located in the district, and whether or not admitted to practice in the district.

Sanctions

Any attorney who files documents in paper form, who fails to submit a motion for exemption, or who continues to file documents in paper form after a motion for exemption has been denied or after an exemption has expired, may risk striking of the document or dismissal of the case, and ultimately be subject to disciplinary action. When an attorney attempts a filing in violation of the above requirements, the following procedure will be followed:

1. The document will be docketed by the Clerk's office.

2. The Clerk shall refer the matter to the assigned judge. The matter may be dismissed or stricken from therecord.

APPENDIX B

RELIEF FROM STAY WORKSHEET-REAL ESTATE

Fillable form

I ______________________ (Name and Title) of ________________________ (Name of Organization/Corporation/ Moving Party) (hereinafter, "Movant") hereby declare (or certify, verify, or state) as follows:

BACKGROUND INFORMATION

1. Real property address which is the subject of this motion: _________________________

2. Lender Name: ____

3. Date of Mortgage: ____

4. Post-Petition payment address: ____

5. The manner in which the movant perfected its interest in the property:

   ____

   ____

6. All other material liens and encumbrances on the property:

   ____

   ____

DEBT/VALUE REPRESENTATIONS

7. Total pre-petition and post-petition indebtedness of Debtor(s) to Movant at the time of filing the motion: $____

8. Movant's estimated market value of the real property:$____________________________

9. Source of estimated valuation: ____

STATUS OF DEBT AS OF THE PETITION DATE

10. Total pre-petition indebtedness of Debtor(s) to Movant as of petition filing date:

A. Amount of principal: $____

B. Amount of interest: $_______________________________________

C. Amount of escrow (taxes and insurance): $_____________________

D. Amount of forced placed insurance expended by Movant: $_______

E. Amount of Attorney's fees billed to Debtor(s) pre-petition: $____________

F. Amount of pre-petition late fees, if any, billed to Debtor(s): $___________

11. Contractual interest rate:____

(If interest rate is (or was) adjustable, please list the rate(s) and dates(s) the rate(s) was/were in effect on a separate sheet and attach the sheet as an exhibit to this form; please list the exhibit number here:)

____

12. Explain any additional pre-petition fees, charges or amounts charged to Debtor's/Debtor's account and not listed above:

____

(If additional space is needed, please list the amounts on a separate sheet and attach the sheet as an exhibit to this form; please list the exhibit number here: .)

____

AMOUNT OF ALLEGED POST-PETITION DEFAULT (AS OF (MM/DD//YYYY)

13. Date last payment was received: __________________________________(mm/dd/yyyy)

14. Alleged total number of payments post-petition from filing of petition through payment due on_(mm/dd/yyyy):______________________________________

15. List all post-petition payments alleged to be in default:

SCHEDULE OF PAYMENTS THAT WERE DUE:

Date Payment Due	**Payment Amount Due Post Petition**
Totals:	$

SCHEDULE OF PAYMENTS THAT WERE RECEIVED

Date	Amount Received	Amount Applied to Principal and Interest	Amount Applied to Escrow	Late Fee Charged (if any)	Amount applied to legal fees or costs (specify)
Totals:	$	$	$	$	

16. Amount of Movant' s Attorney's fees billed to Debtor for the preparation, filing and prosecution of this motion: $_______________

17. Amount of Movant's filing fee for this motion: $_______________

18. Other Attorney's fees billed to Debtor post-petition: $_______________

19. Amount of Movant's post-petition inspection fees:$_______________
    Amount of Movant's post-petition appraisal/broker's price opinion: $_______________

20. Amount of forced placed insurance or insurance provided by the Movant post-petition:
    $_______________

21. Sum held in suspense by Movant in connection with this contract, if applicable:
    $_______________

22. Amount of other post-petition advances or charges: i.e., taxes, insurance incurred by Debtor, etc.: $_______________

23. Amount and date of post-petition payments offered by the Debtor and refused by the Movant:

    $ _______________ Date: _______________

    $ _______________ Date: _______________

    $ _______________ Date: _______________

REQUIRED ATTACHMENTS TO MOTION

The following exhibits are attached to the motion in support of the relief requested.

1. Copies of documents that indicate Movant's interest in the subject property. For purposes of example only, a complete and legible copy of the promissory note or other debt instrument together with a complete and legible copy of the mortgage and any assignments in the chain from the original mortgagee to the current moving party.

2. Copies of documents establishing proof of standing to bring this Motion.

3. Copies of documents establishing that Movant's interest in the real property was perfected. For the purposes of example only, a complete and legible copy of mortgage containing the applicable recording information.

CERTIFICATION AND DECLARATION FOR BUSINESS RECORDS

I certify that the information provided in this worksheet and/or exhibits attached to this worksheet is derived from records that were made at or near the time of the occurrence of the matters set forth by, or from information transmitted by, a person with knowledge of those matters, were kept in the course of the regularly conducted activity; and were made by the regularly conducted activity as a regular practice.

[remainder of page intentionally left blank, text continued on next page]

I further certify that copies of any transactional documents attached to this worksheet as required by paragraphs 1, 2, and 3, immediately above, are true and accurate copies of the original documents, I further certify that the original documents are in movant's possession, except as follows:

____

____

I/we declare (or certify, swear, affirm, verify or state) that the foregoing is true and correct.

Executed on________________[date]

____
[signature]

____
[title]

Subscribed and sworn to before me this______________ [date]

____
Notary Public: [name]
My commission expires: _________________

APPENDIX C
Fillable form

FEE APPLICATION COVER SHEET

Interim/Final Fee Application of: ____

Time Period: ____

Bankruptcy Petition Filed: ____

Date of Entry of Retention Order: ____

Amount Requested		**Reductions**	
Fees	$________________	Voluntary Fee Reductions	$________________
Expenses	$________________	Expenses	$________________
TOTAL	$________________		

Retainer Request:		**Expense Detail:**		**Expense Detail:**	
Retainer Received	$______________	Copies:	$______________	Copies – per page cost and total	$___________
Prior award applied	$______________	Travel:	$______________		
Balance before this request	$______________	Other:			

Hours and Rates:

Hours/Rates per professional:

1. ____________________________
2. ____________________________
3. ____________________________

APPENDIX D

GUIDELINES FOR COMPENSATION AND EXPENSE REIMBURSEMENTS OF PROFESSIONALS

In order to provide professionals with clear and concise procedures for compensation and reimbursement of expenses, applications for compensation and reimbursement of expenses filed shall conform substantially to the following requirements:

A. Contents of Applications for Compensation and Reimbursement of Expenses.

All applications should include sufficient detail to demonstrate compliance with the standards set forth in 11 U.S.C. § 330. The fee application should also contain sufficient information about the case and the applicant to facilitate a review without searching for relevant information in other documents. The following will facilitate review of the application.

1. Information about the Applicant and the Application. The following information should be provided in every fee application:

   a. Date the bankruptcy petition was filed, date of the order approving employment, identity of the party represented, date services commenced, and whether the applicant is seeking compensation under a provision of 11 U.S.C. other than § 330.

   b. Terms and conditions of employment and compensation, source of compensation, existence and terms controlling use of a retainer, and any budgetary or other limitations on fees.

   c. Names and hourly rates of all applicant's professionals and paraprofessionals who billed time, explanation of any changes in hourly rates from those previously charged, and statement of whether the compensation is based on the customary compensation charged by comparably skilled practitioners in cases other than cases under title 11.

   d. Whether the application is interim or final, and the dates of previous orders on interim compensation or reimbursement of expenses along with the amounts requested and the amounts allowed or disallowed, amounts of all previous payments, and amount of any allowed fees and expenses remaining unpaid .

   e. Whether the party on whose behalf the applicant is employed has been given the opportunity to review the application and whether that party has approved the requested amount.

f. When an application is filed more than once every 120 days after the order for relief or after a prior application to the Court, the date and terms of the order allowing leave to file at shortened intervals.

g. Time period of the services or expenses covered by the application.

2. Case Status. The following information should be provided to the extent that it is known to or can be reasonably ascertained by the applicant:

a. In a Chapter 7 case, a summary of the administration of the case including all moneys received and disbursed in the case, when the case is expected to close, and, if applicant is seeking an interim award, whether it is feasible to make an interim distribution to creditors without prejudicing the rights of any creditor holding a claim of equal or higher priority.

b. In a Chapter 11 case, whether a plan and disclosure statement have been filed and, if not yet filed, when the plan and disclosure statement are expected to be filed; whether all quarterly fees have been paid to the United States Trustee; and whether all monthly operating reports have been filed.

c. In a Chapter 12 or 13 case, where the Debtor's attorney is the applicant, whether the application complies with § 330(a)(4)(B); whether the application is in accordance with the 2016(b) statement that was filed at the beginning of the case; and whether approval of the application would have an effect on the Debtor's plan.

d. In every case, the amount of cash on hand or on deposit, the amount and nature of accrued unpaid administrative expenses, and the amount of unencumbered funds in the estate.

e. In every case, any material changes in the status of the case that occur after the filing of the fee application should be raised, orally or in writing, at the hearing on the application or, if a hearing is not required, prior to the expiration of the time period for objection.

3. Fee Application Cover Sheet. All applications should include a cover sheet (see Appendix C) or a summary that provides a synopsis of the following information:

a. Total compensation and expenses requested and any amount(s) previously requested.

b. Total compensation and expenses previously awarded by the court;

c. Name and applicable billing rate for each person who billed time during the period , and date of bar admission for each attorney;

d. Total hours billed and total amount of billing for each person who billed time during billing period; and

e. Computation of blended hourly rate for persons who billed time during period, excluding paralegal or other paraprofessional time.

4. Reimbursement for Actual, Necessary Expenses. The following factors are relevant to a determination that an expense is proper:

a. Whether the expense is reasonable and economical.

b. Whether the requested expenses are customarily charged to non-bankruptcy clients of the applicant.

c. Whether applicant has provided a detailed itemization of all expenses including the date incurred, description of expense (type of travel, type of fare, rate, destination), method of computation, and, where relevant, name of the person incurring the expense and purpose of the expense. Itemized expenses should be identified by their nature (long distance telephone, copy costs, messengers, computer research, airline travel, etc.) and by the month incurred. Unusual items require more detailed explanations and should be allocated, where practicable, to specific projects.

d. Whether applicant has prorated expenses where appropriate between the estate and other cases (travel expenses applicable to more than one case) and has adequately explained the basis for any such proration.

e. Whether expenses incurred by the applicant to third parties are limited to the actual amounts billed to, or paid by, the applicant on behalf of the estate.

B. Confidentiality Requests

If an applicant believes that there is a need to omit any information or description of services as privileged or confidential, the applicant must first get the approval of the court; provided, however, that if such a request is granted, the court may require that any application also contain a set of unredacted time records for in camera inspection.

C. Voluntary Reduction of Fees or Disbursements

If an applicant is not requesting all of the fees or disbursements to which it might be entitled based on the applicable hourly rates multiplied by the hours expended or based on the court order authorizing retention, the voluntary reduction must be identified in the application, including the amount of the reduction taken. If the voluntary reduction pertains to services which continue to appear in the detailed description of services rendered or to disbursements that continue to be listed, the entries for which no compensation or reimbursement is sought must be identified.

D. Provisions Regarding Disbursements

1. No Enhanced Charges for Disbursements. Except to the extent that disbursements are prohibited by these Amended Guidelines, the disbursements sought must be billed at rates, and in accordance with, practices customarily employed by the applicant and generally accepted by the applicant's clients.

2. Photocopies. Photocopies shall be reimbursable at the lesser of $0.20 per page or cost.

APPENDIX E

LOCAL FORM CHAPTER 13 PLAN AND INSTRUCTIONS

United States Bankruptcy Court
District of Connecticut

Filing Instructions for the Local Form Chapter 13 Plan

The Local Form Chapter 13 Plan is a fillable PDF document that contains active programming elements. Once the PDF fillable document is completed with all necessary information, it must be converted to a PDF format that eliminates the active programming elements so that it can be filed on the Court's electronic case filing system, known as CM/ECF.

Converting The Fillable PDF Document to a PDF Format That May Be Filed (Mandatory)

The fillable PDF document can be converted to a PDF format that eliminates the active programming elements so that it is acceptable to use for uploading to CM/ECF in at least two ways:

1. The user can "print to PDF" by following these steps:

    - Open completed form
    - Click on the PRINT button on the form.
    - Printer dialogue box opens – select "Adobe PDF" as the printer.
    - Click on print button – this will create a non-editable form ready to be filed on CM/ECF. You will be asked to name the document for saving in your local directory.
        - *Note that it is recommended that users create a different name for the PDF document to be filed so that the fillable PDF format document is retained for future editing if necessary.*

2. The user can physically print the PDF form and then scan the paper copy into a PDF document to use for filing by following these steps:

    - Open completed form.
    - Click on the PRINT button on the form.
    - Printer dialogue box opens – select your printer.
    - Scan the paper document and save as a PDF document for filing on CM/ECF.

Saving the Fillable PDF Document for Further Editing (Recommended)

It is recommended that users first save the fillable PDF document to a local directory on their computer. Once that is done, the form should retain information that is input so that it populates to the form when opened later. If a user anticipates that a Chapter 13 Plan may be modified in the future, it will be important to save a copy of the Chapter 13 Plan as a fillable PDF document (i.e., keep a copy in PDF fillable format even though you will need to print it to file the original version of the form to file it as described above).

To save the fillable PDF document to a local directory, follow these steps:

- From the Adobe Menu Bar Select "File"
- Then, select "Save" or "Save As" and type a name for the document
- Save to your local directory on your computer

Revised 12/8/2017

UNITED STATES BANKRUPTCY COURT
DISTRICT OF CONNECTICUT

Fill in this information to identify your case:

Debtor 1* [ ] [ ] [ ]
First Name Middle Name Last Name
Social Security Number: XXX - XX - [ ][ ][ ][ ]
(Enter only last 4 digits)

Debtor 2*
Spouse, if filing [ ] [ ] [ ]
First Name Middle Name Last Name
Social Security Number: XXX - XX - [ ][ ][ ][ ]
(Enter only last 4 digits)

Case number [ ]
(If known)

*For purposes of this Chapter 13 Plan, "Debtor" means "Debtors" where applicable.

CHAPTER 13 PLAN

☐ Original Plan

☐ [ ] Amended Plan (Indicate 1st, 2nd, etc.) ECF No. of prior plan [ ]

☐ [ ] Modified Plan (Indicate 1st, 2nd, etc.) ECF No. of prior plan [ ]

Amended Plan: Only complete this section if this is an amended plan before confirmation.
Sections of the Plan that have been amended (list):

	Plan Section(s)	Amendment(s) (Describe)

If your plan amendment affects all creditors of a certain class (secured, priority or unsecured non-priority) check each class of creditors affected. If the changes above affect only individual creditors, list each below.

All Creditors (check all that apply):

- ☐ secured
- ☐ priority
- ☐ unsecured, non-priority

☐ The amendement affects individual creditors. List each below.

	Creditor Name(s)	Proof of Claim Number	Type of Claim

Modified Plan: Only complete this section if this is a modified plan after confirmation.
Sections of the Plan that have been modified (list):

	Plan Section(s)	Modification(s) (Describe)

If your plan modification affects all creditors of a certain class (secured, priority or unsecured non-priority) check each class of creditors affected. If the changes above affect only individual creditors, list each below.

All Creditors (check all that apply):

- ☐ secured
- ☐ priority
- ☐ unsecured, non-priority

☐ The modification affects individual creditors. List each below.

	Creditor Name(s)	Proof of Claim Number	Type of Claim

I. NOTICES

To Debtors: Plans that do not comply with local rules and judicial rulings may not be confirmable. All plans, amended plans and modified plans shall be served upon all creditors by the Debtor and a certificate of service shall be filed with the Clerk.

"Collateral" as used in this Chapter 13 Plan means the property securing a claim.

If the Debtor intends to determine the secured status of a claim pursuant to 11 U.S.C. § 506, or if the Debtor intends to avoid the fixing of a lien that impairs the Debtor's exemption pursuant to 11 U.S.C. § 522(f), then the Debtor must do two things: (1) indicate the Debtor's intention in this Chapter 13 Plan in the space below; and (2) file a separate motion pursuant to 11 U.S.C. § 506 or 11 U.S.C. § 522(f) following the Contested Matter Procedure or local rules adopted after December 1, 2017. If a separate motion is not filed then the Debtor will not be entitled to relief pursuant to 11 U.S.C. § 506 or 11 U.S.C. § 522(f).

The Debtor must check the appropriate box (Included or Not Included) in the chart below. If an item is checked as "Not Included," or if both boxes are checked, the provision will be ineffective if later set out in this Chapter 13 Plan.

The valuation of a secured claim pursuant to 11 U.S.C. § 506, set out in Section 3.2, which may result in a partial payment or no payment at all to the secured creditor.	☐ Included	☐ Not Included
Avoidance of a judicial lien or nonpossessory, nonpurchase-money security interest pursuant to 11 U.S.C. § 522(f), set out in Section 3.3.	☐ Included	☐ Not Included
Assumption or rejection of executory contracts or unexpired leases pursuant to 11 U.S.C. § 365, set out in Section VI.	☐ Included	☐ Not Included

To Creditors: Your rights may be affected by this Chapter 13 Plan. **You must file a timely proof of claim in order to be paid.** *See* Fed.R.Bankr.P. 3002. Your claim may be modified or eliminated. You should read this Chapter 13 Plan carefully and discuss it with your attorney if you have one in this bankruptcy case. If you do not have an attorney, you may wish to consult one.

If you oppose the Chapter 13 Plan's treatment of your claim or any provision of this Chapter 13 Plan, you or your attorney must file an objection to confirmation **no later than 7 days before the date set for confirmation of the Chapter 13 Plan**, unless otherwise ordered by the Bankruptcy Court. The Bankruptcy Court may confirm this Chapter 13 Plan without further notice if no objection to confirmation is filed. *See* Fed.R.Bankr.P. 3015.

This Chapter 13 Plan does not allow claims. The fact that your claim is classified in this Chapter 13 Plan does not mean that you will receive payment.

To All Parties: The Chapter 13 Plan contains no non-standard provisions other than those set out in Section VII. The Debtor must check one box in the chart below indicating whether any non-standard provision is Included or Not Included in Section VII of this Chapter 13 Plan.

Non-standard provisions, set out in Section VII.	☐ Included	☐ Not Included

II. PLAN PAYMENTS AND LENGTH OF PLAN

The Debtor shall submit all or such portion of future earnings or other future income of the Debtor to the supervision and control of the Chapter 13 Standing Trustee as is necessary for the execution of this Chapter 13 Plan as required by 11 U.S.C. § 1322(a)(1). Payments by the Debtor will be made as set forth in this Section II.

2.1 Payments to Chapter 13 Standing Trustee.

The Debtor will make payments to the Chapter 13 Standing Trustee as follows:

$		per		for		months.
$		per		for		months.
$		per		for		months.

If fewer than 60 months of payments are specified, additional monthly payments may be made to the extent necessary to make the payments to creditors specified in this Chapter 13 Plan.

2.2 Source of Payments to the Chapter 13 Standing Trustee.

Check all that apply.

☐ The Debtor will make payments pursuant to a payroll deduction order.

Fill in employer information for payroll deduction:

Employer Name:	
Employer Address:	
Employee Identification No:	

(Note: Redact SSN so only last 4 digits appear)

☐ The Debtor will make payments directly to the Chapter 13 Standing Trustee at the following address (include case number on payment):

Roberta Napolitano, Chapter 13 Standing Trustee
PO Box 610
Memphis, TN 38101-0610

2.3 Income Tax Refunds.

Check one.

☐ The Debtor will retain any income tax refunds received during the plan term. Note the Chapter 13 Standing Trustee may reduce the Debtor's deduction for payment of taxes in calculating disposable income if this option is selected.

☐ The Debtor will supply the Chapter 13 Standing Trustee with a copy of each income tax return filed during the plan term within 14 days after filing the return and will turn over to the Chapter 13 Standing Trustee all income tax refunds received during the Chapter 13 Plan term.

☐ The Debtor will treat income tax refunds as follows:

2.4 Additional Payments.

Check one.

☐ **None**. *If "None" is checked, the rest of this subpart need not be completed or reproduced.*

☐ The Debtor will make additional payment(s) to the Chapter 13 Standing Trustee from other sources, as specified below. Describe the source, estimated amount, and date of each anticipated payment.

Source:		Est. Amount $:		Date:	
Source:		Est. Amount $:		Date:	

Source: [ ] Est. Amount $: [ ] Date: [ ]

2.5 Estimated Total Payments.

The estimated total payments to be made by the Debtor under this Chapter 13 Plan to the Chapter 13 Standing Trustee is:

$ [ ]

2.6 Order of Payments to Creditors by the Chapter 13 Standing Trustee

Payments by the Chapter 13 Standing Trustee to classes of claims shall be made in the following order:

[ ]

The Chapter 13 Standing Trustee shall make payments from the funds received from the Debtor pursuant to this Chapter 13 Plan until satisfaction of all costs of administration, all claims entitled to priority under 11 U.S.C. § 507, the present value of all allowed secured claims, and payments to unsecured creditors as provided in this Chapter 13 Plan.

III. TREATMENT OF SECURED CLAIMS

3.1 Secured Claims That Will Not Be Modified.

Secured claims that will not be subject to a valuation motion pursuant to 11 U.S.C. § 506, or to avoidance pursuant to 11 U.S.C. § 522(f), shall be described in this section.

☐ **None**. *If "None" is checked, the rest of this subpart need not be completed or reproduced.*

☐ There are secured claims treated in this Chapter 13 Plan that are not going to be modified.

☐ Arrears payments (Cure) will be disbursed by the Chapter 13 Standing Trustee and regular payments (Maintain) will be disbursed by the Debtor, as specified below.

1. Creditor: [ ]

Last 4 Digits of Account No.: ☐☐☐☐

Arrearage / Payoff on Petition Date: [ ]

Interest Rate on Arrearage: [ ]

Regular Payment (Maintain) by Debtor:* [ ] /month

☐ Real Property

☐ Principal Residence

☐ Other (describe)

[ ]

Address of Collateral:

[ ]

Check below regarding real property taxes and insurance:

☐ Mortgage payments include escrow for:

☐ Real estate taxes

☐ Homeowners Insurance

☐ Debtor pays directly for:

☐ Real estate taxes

☐ Homeowners Insurance

☐ Personal Property/Vehicle

Description of Collateral (include first digit and last four digits of VIN# for any vehicle): ☐ - ☐☐☐☐

*Note: Amounts set forth in this section are estimates subject to reasonable adjustment.

2. Creditor:

Last 4 Digits of Account No.: ☐☐☐☐

Arrearage / Payoff on Petition Date:

Interest Rate on Arrearage:

Regular Payment (Maintain) by Debtor:* /month

☐ Real Property

☐Principal Residence

☐Other (describe)

Address of Collateral:

Check below regarding real property taxes and insurance:

☐ Mortgage payments include escrow for:

☐ Real estate taxes

☐ Homeowners Insurance

☐ Debtor pays directly for:

☐ Real estate taxes

☐ Homeowners Insurance

☐ Personal Property/Vehicle

Description of Collateral (include first digit and last four digits of VIN# for any vehicle): ☐ - ☐☐☐☐

*Note: Amounts set forth in this section are estimates subject to reasonable adjustment.

3. Creditor:

Last 4 Digits of Account No.: ☐☐☐☐

Arrearage / Payoff on Petition Date:

Interest Rate on Arrearage:

Regular Payment (Maintain) by Debtor:* /month

☐ Real Property

☐Principal Residence

☐Other (describe)

Check below regarding real property taxes and insurance:

☐ Mortgage payments include escrow for:

☐ Real estate taxes

☐ Homeowners Insurance

☐ Debtor pays directly for:

Address of Collateral: [ ]

☐ Real estate taxes

☐ Homeowners Insurance

☐ Personal Property/Vehicle

Description of Collateral (include first digit and last four digits of VIN# for any vehicle): ☐ - ☐☐☐☐

[ ]

*Note: Amounts set forth in this section are estimates subject to reasonable adjustment.

Unless otherwise ordered by the Court, the amounts listed on a proof of claim filed before the filing deadline under Fed.R.Bankr.P. 3002(c) control over any contrary amounts listed above as to the current installment payment and arrearage. In the absence of a contrary, timely filed proof of claim, the amounts stated above are controlling. If relief from the automatic stay is ordered as to any item of Collateral listed in this Section, then, unless otherwise ordered by the Court, all payments under this paragraph by the Chapter 13 Standing Trustee as to that Collateral will cease, and all secured claims based on that Collateral will no longer be treated by this Chapter 13 Plan.

The Debtor shall pay current real property taxes, personal property taxes, and insurance for property (Collateral) to be retained prior to and after confirmation of any Chapter 13 Plan.

3.2. Secured Claims Subject to Valuation Motion.

☐ **None.** *If "None" is checked, the rest of this subpart need not be completed or reproduced.*

☐ The Debtor intends to seek an order of the Bankruptcy Court valuing a claim pursuant to 11 U.S.C. § 506.

Secured Claims that are Subject to a Separate Motion or Adversary Proceeding Based on Valuation.

Valuations under 11 U.S.C. § 506 may be sought to determine how a secured creditor's claim will be treated in a chapter 13 plan. This Chapter 13 Plan does not value claims. To value a claim pursuant 11 U.S.C. § 506, the Debtor must file and serve a separate motion pursuant to Fed.R.Bankr.P. 3012, 7004 and 9014(b). Any other form of relief sought by a debtor, including a determination of the extent, validity, and/or priority of a secured creditor's lien, must be determined in an adversary proceeding pursuant to Fed.R.Bankr.P. 7001.

The information provided below is for information purposes only, and the Debtor's valuation stated herein is subject to change, without the need to modify this Chapter 13 Plan, based on the resolution of any motion or adversary proceeding on valuation. The amount of the creditor's claim in excess of the valuation determined by the Court for the Collateral shall be treated with other general unsecured claims and paid *pro rata* provided that the creditor timely files a proof of claim.

The Debtor intends to file a motion requesting that the Court determine the value of the secured claims listed below. For each non-governmental secured claim listed below, the Debtor states that the value of the secured claim should be as set out below. For secured claims of governmental units, unless otherwise ordered by the Court, the value of a secured claim listed in a proof of claim controls over any contrary amount listed below. For each listed claim, the value of the secured claim as determined by the Court will be paid in full with interest at the rate stated below, upon an order of the Court on the Debtor's Motion.

The portion of any allowed claim that exceeds the amount of the secured claim will be treated as an unsecured claim under Section V of this Chapter 13 Plan. If the amount of a creditor's secured claim is listed below as having no value, the creditor's allowed claim will be treated in its entirety as an unsecured claim under Section V of this Chapter 13 Plan. Unless otherwise ordered by the Court, the amount of the creditor's total claim listed on the proof of claim controls over any contrary amounts listed in this paragraph.

The holder of any claim listed below will retain the lien on the Collateral of the Debtor or the estate(s) until the earlier of:

(a) payment of the underlying debt determined under nonbankruptcy law, or

(b) discharge of the underlying debt under 11 U.S.C. § 1328, at which time the lien will terminate.

1. Real Property: ☐ NONE

1. Creditor:	Creditor's Total Claim Amount:	**Proposed Secured Claim Amount**
Last 4 Digits of Account No.: ☐☐☐☐ Real Property ☐Principal Residence ☐Other (describe) Address of Collateral:	Value of Collateral: Secured Portion of Creditor's Lien: Unsecured Portion of Creditor's claim*: Interest Rate: Check below regarding real property taxes and insurance: ☐ Mortgage payments include escrow for: ☐ Real estate taxes ☐ Homeowners Insurance ☐ Debtor pays directly for: ☐ Real estate taxes ☐ Homeowners Insurance *Unsecured portion will be treated in Section IV or V, as appropriate.	Total Secured Claim to be treated in this Chapter 13 Plan: If claim is for taxes, list principal amount of tax:

2. Creditor:	Creditor's Total Claim Amount:	**Proposed Secured Claim Amount**
[ ] Last 4 Digits of Account No.: [ ][ ][ ][ ] Real Property ☐Principal Residence ☐Other (describe) [ ] Address of Collateral: [ ]	[ ] Value of Collateral: [ ] Secured Portion of Creditor's Lien: [ ] Unsecured Portion of Creditor's claim*: [ ] Interest Rate: [ ] Check below regarding real property taxes and insurance: ☐ Mortgage payments include escrow for: ☐ Real estate taxes ☐ Homeowners Insurance ☐ Debtor pays directly for: ☐ Real estate taxes ☐ Homeowners Insurance *Unsecured portion will be treated in Section IV or V, as appropriate.	Total Secured Claim to be treated in this Chapter 13 Plan: [ ] If claim is for taxes, list principal amount of tax: [ ]
3. Creditor:	**Creditor's Total Claim Amount:**	**Proposed Secured Claim Amount**
[ ] Last 4 Digits of Account No.: [ ][ ][ ][ ] Real Property ☐Principal Residence ☐Other (describe) [ ] Address of Collateral: [ ]	[ ] Value of Collateral: [ ] Secured Portion of Creditor's Lien: [ ] Unsecured Portion of Creditor's claim*: [ ] Interest Rate: [ ] Check below regarding real property taxes and insurance:	Total Secured Claim to be treated in this Chapter 13 Plan: [ ] If claim is for taxes, list principal amount of tax: [ ]

	☐ Mortgage payments include escrow for: ☐ Real estate taxes ☐ Homeowners Insurance ☐ Debtor pays directly for: ☐ Real estate taxes ☐ Homeowners Insurance *Unsecured portion will be treated in Section IV or V, as appropriate.	

2. Vehicles: ☐ NONE

1. Creditor: ______ Last 4 Digits of Account No.: ☐☐☐☐ Check one below: ☐ Claim incurred 910 days or more pre-petition ☐ Claim incurred less than 910 days pre-petition	Value of Collateral: ______ Value of Creditor's Lien: ______ Interest Rate: ______ Description of Collateral (include first digit and last four digits of VIN# for any vehicle): ☐ - ☐☐☐☐ ______	**Payment** Total Secured Claim to be treated in this Chapter 13 Plan: ______ If claim is for taxes, list principal amount of tax: ______
2. Creditor: ______ Last 4 Digits of Account No.: ☐☐☐☐ Check one below: ☐ Claim incurred 910 days or more pre-petition ☐ Claim incurred less than 910 days pre-petition	Value of Collateral: ______ Value of Creditor's Lien: ______ Interest Rate: ______ Description of Collateral (include first digit and last four digits of VIN# for any vehicle): ☐ - ☐☐☐☐ ______	**Payment** Total Secured Claim to be treated in this Chapter 13 Plan: ______ If claim is for taxes, list principal amount of tax: ______
3. Creditor: ______ Last 4 Digits of Account No.: ☐☐☐☐ Check one below:	Value of Collateral: ______ Value of Creditor's Lien: ______	**Payment** Total Secured Claim to be treated in this Chapter 13 Plan: ______

☐ Claim incurred 910 days or more pre-petition ☐ Claim incurred less than 910 days pre-petition	Interest Rate: ☐ Description of Collateral (include first digit and last four digits of VIN# for any vehicle): ☐ - ☐☐☐☐	If claim is for taxes, list principal amount of tax:

3. Personal Property: ☐ NONE

1. Creditor: Last 4 Digits of Account No.: ☐☐☐☐ Check one below: ☐ Claim incurred one (1) year or more pre-petition. ☐ Claim incurred less than one (1) year post-petition.	Value of Collateral: Value of Creditor's Lien: Interest Rate: Description of Collateral:	**Payment** Total Secured Claim to be treated in this Chapter 13 Plan: If claim is for taxes, list principal amount of tax:
2. Creditor: Last 4 Digits of Account No.: ☐☐☐☐ Check one below: ☐ Claim incurred one (1) year or more pre-petition. ☐ Claim incurred less than one (1) year post-petition.	Value of Collateral: Value of Creditor's Lien: Interest Rate: Description of Collateral:	**Payment** Total Secured Claim to be treated in this Chapter 13 Plan: If claim is for taxes, list principal amount of tax:
3. Creditor: Last 4 Digits of Account No.: ☐☐☐☐ Check one below: ☐ Claim incurred one (1) year or more pre-petition. ☐ Claim incurred less than one (1) year post-petition.	Value of Collateral: Value of Creditor's Lien: Interest Rate: Description of Collateral:	**Payment** Total Secured Claim to be treated in this Chapter 13 Plan: If claim is for taxes, list principal amount of tax:

3.3 Secured Claims Subject To Avoidance (11 U.S.C. § 522(f)).

☐ **None.** *If "None" is checked, the rest of this subpart need not be completed or reproduced.*

☐ The Debtor is seeking to avoid the fixing of judicial liens pursuant to 11 U.S.C. § 522(f). Judicial liens or nonpossessory, nonpurchase money security interests securing the claims may be avoided to the extent that they impair the exemptions under 11 U.S.C. § 522(f) as listed below. A separate motion must be filed and served pursuant to Fed.R.Bankr.P. 7004 and applicable local rules.

To avoid liens pursuant to 11 U.S.C. § 522(f), the Debtor must file and serve a separate motion on the affected creditor(s) pursuant to Fed.R.Bankr.P. 3012, 7004 and 9014(b). The Debtor may at a later date seek to avoid a judicial lien held by a creditor not listed below. The details below are provided for informational purposes only, and are subject to change, without the need to modify this Chapter 13 Plan, based on the resolution of the Debtor's motion to avoid lien. The amount of the creditor's avoided lien, if any, shall be treated with other general unsecured claims and paid *pro rata* provided that the creditor timely files a proof of claim. The amount of the judicial lien or security interest that is avoided will be treated as an unsecured claim in Section IV or V as applicable, to the extent allowed. The amount, if any, of the judicial lien or security interest that is not avoided will be paid in full as a secured claim under this Chapter 13 Plan. *See*, 11 U.S.C. § 522(f) and Fed.R.Bankr.P. 4003(d). The Debtor discloses the intention to avoid liens held by the following creditors.

1. Creditor:	Collateral:
Last 4 Digits of Account No.: ☐☐☐☐	Basis for exemption:
Total Amount of Creditor's Claim:	Amount of claimed exemption that could be claimed:
	Amount of Claim to be treated as unsecured claim:
2. Creditor:	Collateral:
Last 4 Digits of Account No.: ☐☐☐☐	Basis for exemption:
Total Amount of Creditor's Claim:	Amount of claimed exemption that could be claimed:
	Amount of Claim to be treated as unsecured claim:

3. Creditor:		Collateral:	
Last 4 Digits of Account No.: ☐☐☐☐		Basis for exemption:	
Total Amount of Creditor's Claim:		Amount of claimed exemption that could be claimed:	
		Amount of Claim to be treated as unsecured claim:	

3.4 Surrender of Collateral.

☐ **None.** *If "None" is checked, the rest of this subpart need not be completed or reproduced.*

☐ The Debtor elects to surrender to each creditor listed below the Collateral identified. Upon entry of an order confirming this Chapter 13 Plan, pursuant to 11 U.S.C. § 362(c)(1) the stay of an act against property of the estate provided in 11 U.S.C. § 362(a) terminates because the Collateral surrendered pursuant to this Chapter 13 Plan is no longer property of the bankruptcy estate. *See*, 11 U.S.C. § 1327(b).

	Name of Creditor	Last 4 Digits of Account No.	Description of Collateral (Address, Vehicle, etc.)
1.		☐☐☐☐	
2.		☐☐☐☐	
3.		☐☐☐☐	

IV. TREATMENT OF FEES AND PRIORITY CLAIMS [as defined in 11 U.S.C. § 507 and 11 U.S.C. § 1322(a)(4)]

4.1 Applicability Of Post-Petition Interest.

The Chapter 13 Standing Trustee's fees and all allowed priority claims, including domestic support obligations other than those treated in Section 4.4, will be paid in full without post-petition interest. If the court determines the Debtor is solvent or is to be treated as solvent under this Chapter 13 Plan, the Court may order post-petition interest be paid on claims.

If this Chapter 13 Plan proposes to pay post-petition interest on priority claims because the Debtor is being treated as if he or she were solvent, then interest shall be paid, if applicable, as follows: 18% interest per annum to creditors holding priority and general unsecured, municipal tax claims; 12% interest per annum to the State of Connecticut Department of Revenue Service's priority and general unsecured state tax claims; and, _____% interest per annum to the Internal Revenue Service's priority and general unsecured federal tax claims.

4.2 Trustee's Fees.

The Chapter 13 Standing Trustee's fees are governed by statute and may change during the course of the case but are estimated to be 10% of plan payments.

4.3 Administrative Attorney's Fees. ☐ PRO BONO

Total Fees:	Total Expenses:	Paid Prior to Confirmation:	Balance Due:

Total Allowance Sought: __________ (Fees and Expenses)

Payable __________ [Check one] ☐ Through this Chapter 13 Plan ☐ Outside of this Chapter 13 Plan

Payable __________ [Check one] ☐ Through this Chapter 13 Plan ☐ Outside of this Chapter 13 Plan

Payable __________ [Check one] ☐ Through this Chapter 13 Plan ☐ Outside of this Chapter 13 Plan

Attorneys shall file applications for allowance of compensation and reimbursement of expenses pursuant to 11 U.S.C. § 330 if the total allowance sought exceeds $4,000.00 before confirmation of this Chapter 13 Plan. The Court will consider allowance of compensation and reimbursement of expenses without such an application if the total allowance sought equals or is less than $4,000.00.

4.4 Domestic Support Obligation(s).

☐ **None.** *If "None" is checked, the rest of this subpart need not be completed or reproduced.*

The allowed priority claims listed below are based on domestic support obligations, including domestic support obligations that have been assigned to or are owed to a governmental unit and will be paid less than the full amount of the claim under 11 U.S.C. § 1322(a)(4).

☐ There are domestic support obligations.

If this Chapter 13 Plan proposes less than full payment of a domestic support obligation then payments in this section shall be for a term of 60 months. *See,* 11 U.S.C. § 1322(a)(4). If the Debtor has domestic support obligations, use only the initials of minor children and do not list confidential information.

1. Name of Creditor: ____________________

Proof of Claim Number: __________

☐ Current and paid outside of this Chapter 13 Plan.

☐ Not Current, and to be paid under this Plan as follows:

2. Name of Creditor: ____________________

Proof of Claim Number: __________

☐ Current and paid outside of this Chapter 13 Plan.

☐ Not Current, and to be paid under this Plan as follows:

3. Name of Creditor: ____________________

Proof of Claim Number: __________

☐ Current and paid outside of this Chapter 13 Plan.

☐ Not Current, and to be paid under this Plan as follows:

4.5 <u>Priority Claims.</u>

☐ **None.** *If "None" is checked, the rest of this subpart need not be completed or reproduced.*

This Chapter 13 Plan may provide for less than full payment of all claims entitled to priority under 11 U.S.C.§ 507(a)(1)(b) only if the Chapter 13 Plan provides that all of the Debtor's projected disposable income for a 5-year period beginning on the date that the first payment is due under this Chapter 13 Plan will be applied to make payments under the Chapter 13 Plan. This Chapter 13 Plan treats claims entitled to priority pursuant to 11 U.S.C. § 507 and 11 U.S.C. § 1322(a)(4), as follows:

1. Name of Creditor: [ ]
Proof of Claim Number: [ ]
Total Due: [ ]
Amount of Principal Due: [ ]
Amount of Interest Due: [ ]
Interest to be Paid Through Chapter 13 Plan? ☐ Yes ☐ No Interest Rate: [ ]

2. Name of Creditor: [ ]
Proof of Claim Number: [ ]
Total Due: [ ]
Amount of Principal Due: [ ]
Amount of Interest Due: [ ]
Interest to be Paid Through Chapter 13 Plan? ☐ Yes ☐ No Interest Rate: [ ]

3. Name of Creditor: [ ]
Proof of Claim Number: [ ]
Total Due: [ ]
Amount of Principal Due: [ ]
Amount of Interest Due: [ ]
Interest to be Paid Through Chapter 13 Plan? ☐ Yes ☐ No Interest Rate: [ ]

V. TREATMENT OF UNSECURED NON-PRIORITY CREDITORS

5.1. Unsecured Non-Priority Claims, Dividend To Be Paid.

☐ **None.** *If "None" is checked, the rest of this subpart need not be completed or reproduced.*

Through this Chapter 13 Plan the Debtor proposes to pay the general unsecured creditors holding claims totaling:

[ ]

a dividend of [ ] [ ] over a period of [ ] months

VI. EXECUTORY CONTRACTS AND UNEXPIRED LEASES

☐ **None.** *If "None" is checked, the rest of this section need not be completed or reproduced.*

☐ The Debtor is seeking to assume or reject executory contracts or unexpired leases pursuant to 11 U.S.C. § 365. A separate motion must be filed and served pursuant to Fed.R.Bankr.P. 7004, 9014(b) and applicable local rules. The details below are provided for informational purposes only, and are subject to change, without need to modify this Chapter 13 Plan, based on resolution of the Debtor's motion to assume or reject.

☐ **Assumed Contracts or Leases.** The Debtor shall make current installment payments or lease payments as specified below, subject to any contrary Court order or rule. Arrearage payments will be disbursed by the Chapter 13 Standing Trustee pursuant to the confirmation order.

Name of Creditor	Description of Leased Property or Executory Contract	Current Installment Payment	Amount of Arrearage to be Paid	Treatment of Arrearage (Refer to Other Plan Section if Applicable)
Proof of Claim Number:		$ To be paid by Debtor.	$ To be disbursed by Trustee.	
Proof of Claim Number:		$ To be paid by Debtor.	$ To be disbursed by Trustee.	
Proof of Claim Number:		$ To be paid by Debtor.	$ To be disbursed by Trustee.	

☐ **Rejected Contracts or Leases**

Name of Creditor	Description of Leased Property or Executory Contract	Estimated Claim to Be Treated in Section V

Notice of Proof of Claim Bar Date:

The counter-party to a rejected contract or rejected lease shall file a proof of claim within thirty (30) days after entry of an order confirming this Chapter 13 Plan.

VII NON-STANDARD PLAN PROVISIONS

☐ **None.** *If "None" is checked, the rest of this section need not be completed or reproduced.*

Non-standard provisions must be set forth below, or in an attachment. A non-standard provision is a provision not otherwise included in the Local Form Chapter 13 Plan or deviating from it. Non-standard provisions set out elsewhere in this Chapter 13 Plan are void.

PURSUANT TO 11 U.S.C. § 1327(b), PROPERTY OF THE ESTATE WILL VEST IN THE DEBTOR UPON ENTRY OF AN ORDER CONFIRMING THIS CHAPTER 13 PLAN.

I declare that the information set forth in the foregoing Chapter 13 Plan is true and correct and is sworn to under penalty of perjury. **By signing and filing this document each Debtor certifies that the wording and order of the provisions in this Chapter 13 Plan are identical to those contained in the Connecticut Local Form Chapter 13 Plan and that this Chapter 13 Plan contains no non-standard provisions other than those set out in Section VII.**

(Debtor Signature) (Joint Debtor Signature)

Debtor (Type Name) Date Joint Debtor (Type Name) Date

Attorney with permission to sign on Debtor's behalf Date

[Note: Each attorney signature on this document is subject to Fed.R.Bankr.P. 9011.]

Note: An original document with the Debtor's inked signature must be maintained by Debtor's attorney.

APPENDIX F

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF CONNECTICUT

CHAPTER 12 OPERATING ORDER

Having filed a petition for relief for a family farmer or family fisherman under Chapter 12 of the Bankruptcy Code, the Debtor and the Debtor's counsel are hereby directed to conform to the following rules, regulations, and procedures:

1. 11 U.S.C. §521 requires the Debtor to cooperate with the Chapter 12 Trustee appointed in this case. The Debtor is also required to furnish information required by the Chapter 12 Trustee in supervising the, administration of this case, including regular reports of operations of the Debtor's farming/fishing enterprise. The Debtor and the Debtor's attorney of record are required to give the Chapter 12 Trustee and such others as directed, notice of all motions and other pleadings filed in this case, as specified in the Federal Rules of Bankruptcy Procedure.

2. The Debtor shall provide the Chapter 12 Trustee with the following financial and informational reports, with a copy to the Office of the U.S. Trustee, 150 Court Street, Room 302, New Haven, CT 06510:

a. Summary of Operations for Chapter 12 Case. The attached form report is an information report showing the Debtor's, results from last year's operation, and estimates or projections for the current or next crop year. This report should be completed and filed with the Clerk of the Court within __days of the filing of the Chapter 12 Petition in Bankruptcy. **[Form to be attached.]**

b. Monthly Cash Receipts and Disbursements Statement. The attached form is to be completed and filed with the Clerk of the Court no later than the 15th day following the end of each month and report all of the Debtor's receipts or income, in cash, by check, or by any other means, received during the month. The receipts should be itemized by kind, quantity, and dollar amount, for example: "Sold 2,000 bushels of corn - $2,000", "Sold 10 beef cattle - $4000", "Sold 5 tons of hay - $275." Likewise, all expenses paid in cash or by check should be itemized. All cash received must be deposited in the Debtor-in-possession's bank account and all payments for expenses should be made by check to extent feasible. If cash is paid by the Debtor, a written receipt must be obtained and kept in a file or envelope. Household or family living expenses need not be itemized, but a lump-sum of funds used or spent for household or family living expenses should be shown. Operating expenses should be itemized under appropriate headings such as fuel, feed, veterinary expenses, repairs, etc. A copy of this report must be timely served upon the Chapter 12 Trustee and the Office of the United States Trustee. **[Form to be attached.]**

c. Tax Deposit Statement. If the Debtor is a family farm/fishing corporation or if the Debtor has employees for which the Debtor is legally required to withhold income taxes or pay social security taxes, the Debtor must complete the tax deposit statement attached to this Order and timely provide evidence to the Chapter 12 Trustee of the full and timely payment of such taxes. **[Tax deposit statement to be attached.]**

d. Insurance Statement. Within 14 days after the filing of the petition or Order of Conversion to this Chapter 12, the Debtor shall provide the Chapter 12 Trustee with a verified statement or written evidence from the Debtor's insurance carrier or broker that the Debtor has fire, casualty and extended coverage on the Debtor's buildings and the equipment, motor vehicle insurance on all vehicles operated on public highways, and workers compensation insurance; if applicable. If no such insurance is currently in effect, the Debtor must explain why it is not in force. The Debtor shall immediately notify the Chapter 12 Trustee and the Office of the United States Trustee of any lapse, cancellations, of proposed cancellation of any such insurance coverage.

3. Commencing on the day the Chapter 12 petition was filed, the Debtor shall commence keeping books and records for the new separate taxable entity. The Debtor shall do the following:

a. The books and records of the Debtor shall be closed as of the date of filing the bankruptcy petition, and a new set of books and records must be kept, thereafter, for the Debtor-in-possession under Chapter 12

b. All the Debtor’s bank accounts shall be closed immediately upon the filing of the Chapter 12 petition, and new bank accounts opened. All amounts from the old account and all receipts from on or after the petition date shall be deposited in the new bank accounts, and all disbursements shall be made by check. The new bank accounts shall be in the name of the Debtor as "Chapter 12 Debtor-in-possession," and this description shall also appear on the new bank pre-numbered bank checks and deposit slips for this checking account.

c. The Debtor shall keep a file (or envelope) with copies of all bills, invoices and sales slips for purchases or payments the Debtor makes after the petition is filed.

4. Both the Debtor and the Debtor's attorney shall attend the § 341 Creditors’ Meeting, at which time the Debtor will be examined under oath by the Chapter 12 Trustee and by any creditors who may attend. The Debtor shall bring to the meeting a copy of the Debtor's last year's federal, state, and local (if required) income tax returns and all schedules filed with the return, including Schedule F. The copy of the income tax returns shall be presented to the Chapter 12 Trustee at the First Meeting, if not earlier supplied to the Chapter 12 Trustee.

5. It is the responsibility and duty of the Chapter 12 Debtor to prepare and timely file all federal, state, and local tax returns required by applicable law. It is advisable in the complex area of bankruptcy and taxation that the Debtor retain a qualified tax preparer to perform the obligations to file federal and state returns. Neither the United States Trustee

nor the Chapter 12 Trustee are permitted to give any tax advice to individual Debtors. Copies of the federal, state, and local tax returns which are filed by the Debtor for any period commencing with the filing of the Chapter 12 petition through the completion of the confirmed plan shall be timely provided to the Chapter 12 Trustee and the United States Trustee's office.

6. Chapter 1, 3 (except for Section 361) and 5 of the Bankruptcy Code also apply to a case under Chapter 12 of the Bankruptcy Code. The Debtor shall not:

   a. Retain or employ attorneys, accountants, appraisers, auctioneers or other professional persons without court approval. This includes employing the attorney who filed the petition to provide services after the filing. See 11 U.S.C. § 327.

   b. Compensate any attorney, accountant, appraiser, auctioneer or other professional except as allowed by the Court. See 11 U.S.C. § 330.

   c. Use cash collateral (or cash equivalence) without the consent of the secured creditor or court authorization. See 11 U.S.C. § 363(c)(2). Cash collateral includes proceeds, products, offspring, rents, or profits of property subject to a security interest when reduced as cash.

   d. Obtain credit or incur unsecured debt other than in the ordinary course of business without court authorization. See 11 U.S.C. § 364(c).

   e. Incur secured debt without court authorization. See 11 U.S.C. § 364(c).

   f. Pay any creditor for goods or services provided before the filing of the petition except as provided in a confirmed plan. See 11 U.S.C. § 549.

7. A Chapter 12 plan shall be filed within 90 days of the date that the petition was filed, unless the court extends the time. 11 U.S.C. § 1221. Failure to comply is cause for dismissal under 11 U.S.C. § 1208.

8. The Debtor shall file objections to claims within 45 days of the confirmation order and proceed promptly with the prosecution and resolution of any such objections so as not to unduly delay the Chapter 12 Trustee's distributions to creditors.

9. Plan Confirmation Requirements. The Court shall confirm a plan only if the plan provides a basis for determining whether the requirements of 11. U.S.C § 1225 (a) and (b) have been met. The requirements of §§ 1225(a)(4), 1225 (a)(5)(B)-(C) and 1225(a)(6)-(7) may be deemed not satisfied if the plan does not contain at least the following information:

   a. A statement disclosing any change of the Debtor's assets or liabilities from the date of filing of the petition through the date of filing of the plan.

   b. A cash-flow projection for the life of the proposed plan, including and identifying the Debtor's farm/fisherman and non-fisherman income sources.

   c. Assumptions and sources upon which the cash-flow projection is based, with historical or other data justifying such assumptions.

d. Farm/fisherman and expense information in a form comparable to Internal Revenue Code Schedule F forms filed by the Debtor for the previous ___ years plus a statement of the Debtor’s non-farm/non-fisherman income for the tax year preceding the filing of the plan.

e. Projected administrative expenses, including attorney fees.

f. A plan summary indicating the dates, amounts, and payees of all amounts to the paid under the plan.

g. If the plan proposes the sale of assets, a statement from the qualified accountant or attorney, setting forth the probable tax consequences thereof.

h. The basis of any valuation of property, including names of appraisers and dates of appraisal, if any.

i. A statement with detailed information, specifying the need for the plan payments to be made over a period longer than three years.

j. If the Debtor proposes to retain secured property, a statement itemizing such property, the value of the property, and the basis of the valuation estimate.

k. A liquidation analysis sufficient to show compliance with 11 U.S.C. § 1225(a)(4), including a statement from a qualified tax accountant or attorney as to tax liabilities from liquidation, if any.

l. A projected disposable income statement for the term of the plan.

m. In the event the Debtor asserts that certain taxes are to be treated as general unsecured claims under 11 U.S.C. § 1222(a)(2)(A), the Debtor shall provide to the affected governmental units copies of the Debtor's complete tax returns for the three years prior to the filing of Chapter 12 relief.

n. The Debtor has paid all amounts that are required under a domestic support obligation and that first become payable after the date of the filing of the petition if the Debtor is required by a judicial or administrative order, or by statute, to pay such domestic support obligation.

o. In a Chapter 12 case, the Debtor must file the certification of payment of domestic support obligations (Appendix "H") with the Court at least seven days prior to the expiration of the Objection to Confirmation deadline. A certification must be filed prior to the confirmation of all original plans and all amended plans and all post-confirmation amended plans. If the certification is not filed with the Court, the confirmation or approval may be denied. The Certification should not be filed before the applicable plan is filed.

10. Tax returns. A Debtor operating under a confirmed plan shall file post-petition tax returns, both state and federal, and pay post-petition taxes, both state and federal, on a timely basis. The Debtor shall comply with all requirements of Title 26 of the United States Code or applicable state tax code. Failure to file post-petition federal or state tax returns or failure to timely pay post-petition federal or state tax liabilities, in the manner prescribed by Title 26, or applicable state law, absent a showing of good cause, may be considered a material

default of a confirmed plan. All post-petition federal and state tax returns and all post-petition federal and state tax liabilities are included in this paragraph, including returns or liabilities for which the Debtor is a responsible party under 26 U.S.C. § 6672 or similar state laws. Complete copies of such tax returns shall be timely provided to the Chapter 12 Trustee.

11. If the Chapter 12 Trustee and/or United States Trustee require periodic reports after confirmation of a plan of reorganization until the court grants a final decree, the information required to be reported and the frequency of the reports shall be determined at the time the plan is confirmed.

12. Failure to comply. Failure of the Debtor to comply with the instructions contained in this Order may be grounds for dismissal of the Chapter 12 case under § 1208.

APPENDIX G

GUIDELINES FOR THE SALE OF SUBSTANTIALLY ALL ASSETS UNDER 11 U.S.C. § 363

These guidelines recognize that parties in interest may sometimes perceive the need to act expeditiously on seeking authorization for the sale of substantially all estate assets. These guidelines are intended to provide a framework for such requests and to provide procedural protection to the parties in interest. The Court will consider requests to modify these guidelines to fit the circumstances of a particular case.

OVERBIDS AND BREAK UP/TOPPING FEES

1. Break-up/Topping Fees. Any request for the approval of a break up/topping fee shall be supported by a statement of the conditions under which the break-up/topping fee would be payable and the factual basis on which the seller determined the provision was reasonable.

   Break-up fees/Topping fees, overbid amounts and other similar provisions will be reviewed on a case by case basis and approved if supported by evidence and case law.

SECTION 363 SALES WITHIN 60 DAYS OF THE FILING OF THE PETITION

1. The Motion to Sell. A Motion to approve the sale of substantially all assets at any time before 60 days after the filing of the petition shall include the following information:

   a. Creditors' Committee. Indicate the date any committee was formed, as well as the identity of the members of the committee and the companies with which they are affiliated.

   b. Counsel for Committee. If the pre-petition creditors' committee retained counsel, indicate the date counsel was engaged and the selection process, as well as the identity of committee counsel.

   c. Sale Contingencies. Statement of all contingencies to the sale agreement, together with a copy of the agreement.

   d. Creditor Contact List. If no committee has been formed, a list of contact persons, together with fax and phone numbers for each of the largest 20 unsecured creditors.

   e. Administrative Expenses. Assuming the sale is approved, an itemization and an estimate of administrative expenses relating to the sale to be incurred prior to closing and the source of payment for those expenses.

f. Proceeds of Sale. An estimate of the gross proceeds anticipated from the sale, together with an estimate of sale proceeds coming into the estate. Itemize all deductions that are to be made from gross sale proceeds and include a brief description of the basis for any such deductions.

g. Debt Structure of Debtor. A brief description of the Debtor's debt structure, including the amount of the Debtor's secured debt, priority claims and general unsecured claims.

h. Need for Quick Sale. A description of why the assets of the estate must be sold on an expedited basis. Include a discussion of alternatives to the sale.

i. Negotiations. A description of the length of time spent in negotiating the sale, and which parties in interest were involved in the negotiation, along with a description of the details of any other offers to purchase, including, without limitation, the potential purchaser's plans in connection with retention of the Debtor's employees.

j. Marketing of Assets. A description of the manner in which the assets were marketed for sale, including the period of time involved and the results achieved.

k. Decision to Sell. The date on which the Debtor accepted the offer to purchase the assets.

l. Relationship of Buyer. A statement identifying the buyer and setting forth all of the buyer's (including its officers, directors and shareholders) connections with the Debtor, creditors, any other party in interest, their respective attorneys, accountants, the U.S. Trustee or any person employed in the office of the U.S. Trustee.

m. Post Sale Relationship with Debtor. A statement setting forth any relationship or connection the Debtor (including its officers, directors, shareholders and employees) will have with the buyer after the consummation of the sale, assuming it is approved.

n. Relationship with Secured Creditors. If the sale involves the payment of all or a portion of secured debt(s), a statement of all connections between Debtor's officers, directors, employees or other insiders and each secured creditor involved (for example, release of insider's guaranty).

o. Insider Compensation. Disclosure of current compensation received by officers, directors, key employees or other insiders pending approval of the sale.

2. Proposed Order Approving Sale. A proposed order approving the sale shall be included with the motion.

3. Good Faith Finding. There must be an evidentiary basis for a finding of good faith under 11 U.S.C §363(m).

4. Financial Ability to Close. Unless the court orders otherwise, any bidder must be prepared to demonstrate to the satisfaction of the court, through an evidentiary hearing, its ability to consummate the transaction if it is the successful bidder, along with evidence regarding any financial contingencies to closing the transaction.

APPENDIX H
Fillable Form

CHECKLIST FOR MOTIONS AND ORDERS FOR USE OF CASH COLLATERAL AND POST- PETITION FINANCING

This is to certify that the following checklist information reflects the substantive content of the motion and proposed order for use of cash collateral or for post-petition financing pursuant to 11 U.S.C. §§ 363 and/or 364 as indicated below:

Answer each question Yes, No, or N/A

		Answer
1.	Identification of Proceeding:	
a.	Preliminary motion/order	________
b.	Final motion/order	________
c.	Continuing use of cash collateral (§ 363)	________
d.	New financing (§ 364)	________
e.	Combination of §§ 363 and 364 financing	________
f.	Emergency hearing (immediate and irreparable harm)	________
2.	Representations:	
a.	Brief history of Debtor's businesses and status of Debtor's prior relationships with lender	________
b.	Brief statement of purpose and necessity of financing	________
c.	Brief statement of type of financing (i.e.) accounts receivable, inventory)	________
d.	Are lender's pre-petition security interest(s) and liens deemed valid, fully perfected and non-avoidable?	________
	(i) Are there provisions to allow for objections to above?	________
e.	Is there a post-petition financing agreement between lender and Debtor?	________
f.	If there is an agreement, are lender's post-petition security interests and liens deemed valid, fully perfected and non-avoidable?	________
g.	Has lender's non-cash collateral been appraised?	________
h.	Insert date of latest appraisal	________
i.	Is Debtor's proposed budget attached?	________
j.	Are all pre-petition loan documents identified?	________
k.	Are pre-petition liens?	________
l.	Are there pre-petition guaranties of debt?	________
3.	Grant of Liens:	
a.	Do post-petition liens secure pre-petition debts?	________
b.	Is there cross-collateralization?	________

c. Is the priority of post-petition liens equal to or higher than existing liens? __________
d. Do post-petition liens have retroactive effect? __________
e. Are there restrictions on granting further liens or liens of equal or higher priority? __________
f. Is lender given liens on claims under §§ 506(c), 544-50 and §§ 522? __________
    (i) Are lender's attorney's fees to be paid? __________
    (ii) Are Debtor's attorney's fees excepted from § 506(c)? __________
g. Is lender given liens upon proceeds of causes of action under §§ 544, 547, and 548? __________

4. Administrative Priority Claims: __________

a. Is lender given an administrative priority? __________
b. Is administrative priority higher than § 507(a)? __________
c. Is there a conversion of pre-petition secured claim to post-petition administrative claim by virtue of use of existing collateral? __________

5. Adequate Protection (§ 361): __________

a. Is there post-petition debt service? __________
b. Is there a replacement/additional § 361(1) lien? __________
c. Is the lender's claim given super-priority? __________
   (§ 364(c) or (d)) [designate] __________
d. Are there guaranties? __________
e. Is there adequate insurance coverage? __________

6. Waiver/Release Claims v. Lender: __________

a. Debtor waives or releases claims against lender, including, but not limited to, claims under §§ 506(c), 544-550, 552, and 553 of the Code? __________
b. Does the Debtor waive defenses to claim or liens of lender? __________
c. Is the proposed lender also the pre-petition lender? __________
d. New post-petition lender? __________
e. Is the lender an insider? __________

7. Modification of Stay: __________

a. Is any modified lift of stay allowed? __________
b. Will the automatic stay be lifted to permit lender to exercise self-help upon default without further order? __________
c. Are there any other remedies exercisable without further order of court? __________
d. Is there a provision that any future modification of order shall not affect status of Debtor's post-petition obligations to lender? __________

8. Creditors' Committee:

a. Has creditors' committee been appointed? ___________
b. Does creditors' committee consent? ___________

9. Restrictions on Parties in Interest:

a. Is a plan proponent restricted in any manner, concerning modification of lender's rights, liens and/or causes? ___________
b. Is the Debtor prohibited from seeking to enjoin the lender in pursuit of rights? ___________
c. Is any party in interest prohibited from seeking to modify this order? ___________
d. Is the entry of any order conditioned upon payment of debt to lender? ___________
e. Is the order binding on subsequent trustee on conversion? ___________

10. *Nunc Pro Tunc*:

a. Does any provision have retroactive effect? ___________

11. Notice and Other Procedures:

a. Is shortened notice requested? ___________
b. Is service requested to shortened list? ___________
c. Is time to respond to be shortened? ___________
d. If final order sought, have 15 days elapsed since service of motion pursuant to FRBP 4001(b)(2)? ___________
e. If preliminary order sought, is cash collateral necessary to avoid immediate and irreparable harm to the estate pending a final hearing? ___________
f. Is a Certificate of Conference included? ___________
g. Is a Certificate of Service included? ___________
h. Is there verification of transmittal to U.S. Trustee included pursuant to FRBP 9034? ___________
i. Has an agreement been reached subsequent to filing motion? ___________

    i. If so, has notice of the agreement been served pursuant to FRBP 4001(d)(l)? ___________
    ii. Is the agreement in settlement of motion pursuant to FRBP 4001(d)(4)? ___________
    iii. Does the motion afford reasonable notice of material provisions of the agreement pursuant to FRBP 4001(d)(4)? ___________
    iv. Does the motion provide for opportunity for hearing pursuant to FRBP 9014? ___________

SIGNED this the____day of ________________

By:____________________________________

APPENDIX I

DOCUMENTS TO BE PRODUCED TO TRUSTEE IN CHAPTER 7 CASES PRIOR TO SECTION 341 CREDITORS MEETING

The following must be brought by the Debtor to the Section 341 Creditor's Meeting in order to have the meeting concluded:

1. Valid government-issued photo identification;

2. Proof of the Debtor's social security number by any document issued by a third party (a tax return is not acceptable proof but a W-2 issued by the Debtor's employer is acceptable proof).

The following documents must be received by the Trustee at least seven (7) days prior to the meeting of creditors:

1. Photocopies of pay stubs and any/all income received by the Debtor and spouse, if any, (whether or not a joint petition has been filed) during the 60-day period prior to the filing of the Bankruptcy Petition.

2. A complete copy of the Debtor's last two (2) years of filed Federal and State Tax Returns with all schedules, W-2 and/or 1099 forms or Tax Transcript redacted for all Social Security Numbers and the names of any dependents.

3. A copy of the statement for any bank account, brokerage account or other account in which the Debtor had money on deposit on the date of the filing of the petition. This includes any such accounts which are in the Debtor's name for convenience or anticipated probate reasons.

4. If the Debtor or non-filing spouse, if any, have any income from self-employment: a sworn Profit and Loss statement indicating the income and/or loss for the sixty (60) days prior to filing of the Bankruptcy Petition dated and signed by the Debtor or non-filing spouse, if any, under penalty of perjury.

5. If the Debtor owns real estate or a mobile home:

   a. An appraisal or comparative market analysis with at least 3 comparable sales listed that is no more than one (l) year old and that is dated and signed by the person providing the value. A tax assessment, Zestimate or similar valuation is not acceptable;

   b. A title search or copy of all mortgages recorded on the land records which include the volume and pages of recordation;

   c. A copy of the recorded deed with property description or a title search;

d. A payoff statement or monthly statement from each mortgage holder showing the balance due on the mortgage(s);

e. Circle or highlight the value of the property and the balance due on the mortgage(s).

6. If the Debtor has purchased, sold, obtained an equity line or mortgage, transferred or refinanced any real property in the four (4) years before the filing of the Bankruptcy Petition:

   a. A copy of the Closing Disclosure and the Loan Estimate;

   b. An accounting of how the Debtor used the money the net proceeds received from the sale, equity line, mortgage or refinancing.

7. If the Debtor has creditors with a lien on a motor vehicle, boat or any other type of property: proof of the amount owed to the creditor as of the filing of the Bankruptcy Petition and proof of the value of the property.

8. If the Debtor has filed or plan to file any lawsuit against anyone for any reason:

   a. A letter from the attorney representing the Debtor regarding the status of the lawsuit and its value;

   b. The attached form completed in full and including the name and address of the Debtor's attorney in the lawsuit.

9. If the Debtor owns an interest in a business, including but not limited to limited liability company, corporation, partnership, joint venture of personal business.

   a. Documents stating the value of the Debtor's interest in the business;

   b. If not previously filed as part of Schedule J, a statement of the monthly expenses of the business;

   c. A balance sheet disclosing assets and liabilities as of the filing of the Bankruptcy Petition.

10. If the Debtor owns any shares or stocks: documents regarding the number of stocks owned in each company and the value of the stock as of the filing of the Bankruptcy Petition.

11. If the Debtor owns any jewelry valued at more than $5,000.00 (other than a wedding or engagement ring): evidence of the value of the jewelry.

12. If the Debtor has a retirement plan such as an IRA, 401 (K), KEOGH or SEP: documents which state the type of plan and its current value.

13. If the Debtor has any annuity contracts: documents which state the type of annuity and its current value.

14. If the Debtor owns a motor vehicle, boat, or trailer: a valuation of the property provided by an independent and recognized source that is dated within six (6) months of the filing of the Bankruptcy Petition.

15. If the Debtor has been divorced: a copy of the final divorce agreement or order and the judgment.

16. If the Debtor has been divorced in the two (2) years prior to the filing of the Bankruptcy Petition: a copy of any and all financial affidavits that filed with the Court in the divorce case.

17. If the Debtor is obligated to pay alimony and/or support pursuant to a Court order: a completed Domestic Support Obligation Disclosure Form.

DOMESTIC SUPPORT OBLIGATION DISCLOSURE FORM
Fillable Form

PERSONAL INJURY INFORMATION

DEBTOR NAME: ____
CASE NUMBER: ____

Date of Accident ________________

Type of claim (check one)

	car accident	___________
	medical malpractice	___________
	slip and fall	___________
Who was injured:	Husband	___________
	Wife	___________
	Both	___________

Nature of injury? ____

Were you admitted to the hospital as a result of injuries received in this accident? Yes ____ No _____

If yes,	Husband	Number of days hospitalized	__________
	Wife	Number of days hospitalized:	__________

Have you had any additional hospitalizations or operations as a result of this accident? Yes ____ No _____

If yes,	Husband	Number of days hospitalized	__________
	Wife	Number of days hospitalized:	__________

Have you lost work as a result of your injuries? Yes ____ No _____

If yes, how many days ___________

Have you returned to work? Yes ____ No _____

If so, when ___________

Name, address, phone number & email address of attorney representing you:

____

____

I certify that the foregoing statements made by me are true to the best of my knowledge, information and belief. I am aware that if any of the foregoing statements made by me are willfully false, I am subject to punishment.

Signature Debtor ________________________________

Signature Co-Debtor ________________________________

APPENDIX J

DOCUMENTS TO BE PRODUCED TO TRUSTEE IN CHAPTER 13 CASES PRIOR TO SECTION 341 CREDITORS MEETING

The following must be brought by the Debtor to the Section 341 Creditor's Meeting in order to have the meeting concluded:

1. Valid government-issued photo identification;

2. Proof of the Debtor's social security number by any document issued by a third party (a tax return is not acceptable proof but a W-2 issued by the Debtor's employer is acceptable proof).

The following must be received by the trustee no later than seven (7) days prior to the Section 341 meeting:

1. Copies of the paystubs the Debtor and the debtor's spouse received during the six month period preceding the filing of the case, containing year to date information. The Debtor must provide updated pay stubs before the confirmation hearing;

2. Copies of state and federal income tax returns of the Debtor and the Debtor's spouse for the most recent two years with accompanying W-2 forms, 1099s and all other attachments regardless of any applicable extensions of time;

3. An affidavit from any non-filing party contributing money to the Debtor's income plus copies of the contributor's state and federal income tax returns for the preceding two years with accompanying W-2 forms, photocopies of their last four payroll stubs and/or operating reports if the contributor is self-employed;

4. A recent valuation, containing at least three comparable sales less than one year old for each piece of real estate owned by the Debtor;

5. A list of the name(s) and address(es) of anyone to whom the Debtor must pay child support by court order;

6. Copies of bank statements for all accounts which the Debtor controls or in which the Debtor holds an interest for the six month period prior to filing ONLY if the Debtor is above median, receives commissions, or operates a business. All other Debtors must submit statements showing the balance in each account which the Debtor controls or in which the Debtor holds an interest for the filing date only.

7. If the Debtor or Debtor's spouse is operating a business, monthly operating statements for the current year must be filed each and every month with the court, the United States Trustee, the Standing Trustee and any governmental unit charged with responsibility for collection or determination of any tax arising out of such operation.

8. If the Debtor has an ownership interest in any non-publicly traded corporation, company, partnership or any other type of business entity, the following documentation must be submitted to the Trustee: a balance sheet reflecting the entity's assets and liabilities as of the petition date, tax returns for the entity for the preceding two years.

9. If the Debtor owns rental property separate monthly operating reports for each property must be submitted to the Trustee each and every month. Copies of executed leases for all current tenants must also be submitted.

APPENDIX K

ORDER AND NOTICE TO DISPUTED, CONTINGENT, AND UNLIQUIDATED CREDITORS

UNITED STATES BANKRUPTCY COURT
DISTRICT OF CONNECTICUT

IN RE:	)	CASE NO.
	)	CHAPTER 11
DEBTOR.	)	RE: ECF No.:

ORDER INSTRUCTING DEBTOR TO COMPLETE, FILE, AND SERVE NOTICE OF DISPUTED, CONTINGENT, OR UNLIOUIDATED CLAIM AND NOTICE OF DEADLINE FOR FILING PROOF OF CLAIM

Upon the Debtor's Schedules/Amended Schedules filed in the case (ECF No.___), it is hereby

ORDERED: The Debtor shall complete, file, and serve the attached Notice of Disputed, Contingent, or Unliquidated Claim and Notice of Deadline for Filing Proof of Claim on or before _______________, 201__, on all creditors whose claim was scheduled as disputed, contingent, or unliquidated in the Schedules and/or Amended Schedules (ECF No ____; and it is further

ORDERED: The Debtor shall serve the attached Notice of Disputed, Contingent, or Unliquidated Claim and Notice of Deadline for Filing Proof of Claim on all affected parties by first class mail, postage prepaid on or before _____________, 201__ and it is further

ORDERED: The Debtor shall file a Certificate of Service indicating compliance with this order on or before _____________, 201__.

Dated at ___________________, Connecticut this ____ day of ______________, 201__.

NOTICE OF DISPUTED, CONTINGENT, OR UNLIQUIDATED CLAIM
<u>AND NOTICE OF DEADLINE FOR FILING PROOF OF CLAIM</u>

To: Claimant(s) Address(es)

Scheduled Claim Amount(s): $____________________________
Claim(s) Scheduled as: [disputed, contingent, or unliquidated, as applicable]

[Note: *All Claimants should be listed here, or an exhibit may be used to list each claimant, with their respective address and the amount of the claim scheduled as disputed, contingent, or unliquidated]*

1. The Debtor scheduled your claim as indicated above. Any creditor whose claim is scheduled as disputed, contingent, or unliquidated in the Debtor's Schedules filed on ________________________, 201__ (ECF No. _), and/or the Amended Schedules filed on ________________________, 201__ (ECF No. _), must file a proof of claim by ________________________, 201__. Pursuant to Federal Rule of Bankruptcy Procedure 3003(c)(2), any creditor required to file a proof of claim who fails to do so shall not be treated as a creditor with respect to such a claim for the purposes of voting on the Debtor's Plan and for distributions to creditors.

2. Creditors who have already filed claims need not file them again.

3. A proof of claim form is enclosed with this notice.

4. Counsel to the Debtor shall file this completed notice listing all those creditors whose claim was not scheduled or whose claim was scheduled as disputed, contingent, or unliquidated in the Schedules and Amended Schedules (ECF Nos._) on or before ________________________, 201__. Counsel to the Debtor shall also serve this notice on all affected parties by First Class Mail, postage prepaid on or before ________________________, 201__. Counsel to the Debtor shall file a Certificate of Service indicating such compliance on or before ________________________, 201__.

APPENDIX L

LIST OF GOVERNMENT AGENCY ADDRESSES

Attorney General of the United States
U.S. Department of Justice
950 Pennsylvania Avenue
Washington, DC 20530-0001

Civil Process Clerk
United States Attorney's Office
157 Church Street, 25th Floor
New Haven, CT 06510

Office of the Attorney General
State of Connecticut
55 Elm Street
Hartford, CT 06106

Connecticut Department of Revenue Services
Collections Unit – Bankruptcy Team
450 Columbus Boulevard, Suite 1
Hartford, CT 06103

APPENDIX M

MOTIONS THAT DO NOT FOLLOW CONTESTED MATTER PROCEDURE

- Motion for 2004 Examination
- Motion to Expedite Hearing
- Motion to Extend the Automatic Stay
- Motion to Limit Notice/Service
- Motion for Sanctions
- Motion for Contempt
- Motion for Exemption from Electronic Filing
- Motion to Appear Pro Hac Vice
- Application to Pay Filing Fee in Installments
- Motion to Waive Filing Fee
- Motion to Return Fee
- Motion to Convert Chapter 7 to 11/12/13 by Debtor
- Motion to Dismiss Chapter 13 Case by Debtor
- Motion to Convert Chapter 13 to Chapter 7 by Debtor
- Motion to Terminate Wage Deduction Provision in Confirmation Order
- Motion to Alter or Amend/Modify pursuant to Fed.R.Bankr.P. 9023
- Motion for Relief from Judgment or Order/Reconsider/Vacate Pursuant to Fed.R.Bankr.P. 9024
- Motions for Extension of Time ***See***, D .Conn. L. Civ. R. 7(b)
- Motion to Delay Entry of Discharge
- Motion for Authority to Operate Business
- Any Motion/Application/Pleading filed in an Appeal
- Any Motion/Application/Pleading filed in an Adversary Proceeding
- Objection to Claim, ***See***, Notice of Objection to Claim Form, Connecticut Local Form 420B
- Stipulations Addressing a Pending Motion/Application/Pleading

APPENDIX N

EXCEPTIONS TO THE CONTESTED MATTER PROCEDURE

- Motion to Compromise pursuant to Fed. R. Bankr. P. 9019
- Motion to Redact
- Motion to Seal
- Motion under § 363 for Cash Collateral/Sale
- Motion under § 364 Borrowing/Financing
- Motion to Dismiss/Convert Chapter 11 by Debtor
- Motion to Dismiss/Convert any case/chapter filed by party other than Debtor
- Motion to Extend Time to File a § 523/727 complaint without consent
- Motion under § 365 to Assume, Assign, or Reject Executory Contract or Unexpired Lease
- Motion to Extend Exclusivity or Time to Confirm a Plan in Chapter 11/12/13
- Motion for Joint Administration/Substantive Consolidation
- Application for Final Decree in Chapter 11
- Application to Employ
- Fee Applications
- Disclosure Statement
- Chapter 11/12/13 Plan Confirmation
- Motion to Modify 11/12/13 Plan after Confirmation
- Trustee's Objection to Debtors Claim of Exemption

Dr. Deborah Thorne, University of Idaho
Co-principle Investigator: Consumer Bankruptcy Project

Studying Consumer Bankruptcy, Twenty Years In: Observations and Ponderings

Most Compelling Findings from the Consumer Bankruptcy Project

- ▸ Consistently, the leading causes of bankruptcy are job loss (decline in income) and medical expenses
- ▸ Households typically struggle for years in the "sweatbox" before they file bankruptcy
- ▸ Bankruptcy is not a low socioeconomic status phenomenon—mostly homeowners with some college
- ▸ Chronic issues—inadequate income, health struggles, and being old—make the fresh start unlikely

Specific to Today's Chat

- ▸ The age distribution of filers is shifting to the right—folks getting older

Bankruptcy Filing Rates per 1,000 U.S. Population, By Age Cohorts

	1991	2001	2007	2013-16	Relative percentage change: 1991-2016
	------------------------(rate)-----------------------------				
Age group					
18-24	3.9	3.7	1.7	0.9	-77.8%
25-34	10.2	12.7	5.8	3.7	-63.8%
35-44	9.3	14.4	6.7	5.6	-39.6%
45-54	7.3	11.4	5.8	7.1	-2.4%
55-64	3.5	5.5	4.9	5.8	+66.2%
65-74	1.2	3.1	2.9	3.6	+203.9%
75+	0.3	2.3	1.3	1.3	+345.1%
65+	*n/a*	*n/a*	2.5	2.8	
<65	*n/a*	*n/a*	5.2	4.8	

Notes: This table shows the estimated filing rate per 1,000 persons, extrapolating the CBP data across the country using U.S. Census data. The 2007 and 2013-16 estimates are from national random samples and are directly computed. The 1991 and 2001 figures are taken from Thorne, Warren & Sullivan (2009). Estimates include an adjustment for the number of joint filings in each database.

Percent of U.S. Bankruptcy Filers by Age Cohort

Age group	1991	2001	2007	2013-2016	Relative percentage change: 1991-2016
	----------------------------(percent) -----------------------				
18-24	8.7	5.3	4.2	2.1	-75.8%
25-34	36.7	26.1	21.9	15.5	-57.7%
35-44	30.6	33.7	28.1	20.4	-33.4%
45-54	15.8	23.2	23.6	28.3	+79.3%
55-64	6.1	7.2	14.7	21.5	+252.1%
65-74	1.8	3.0	5.3	8.9	+392.6%
65+	2.1	4.5	7.6	12.2	+478.9%
75+	0.3	1.5	2.3	3.3	+996.9%

Notes: The percentages are based on total number of filers, not number of petitions. Thus, a joint bankruptcy petition from a married couple results in two filers.

Financial Characteristics of Younger and Older Bankruptcy Filers, and Older Non-Bankrupt Americans

	Bankrupt 65 and Over	Non-Bankrupt 65 and over
Total debt	$202,592 ($101,560)	$50,231 ($1,000)
Secured debt	$158,616* ($70,047)*	
Homeownership	66.4%*	83.2%
Total assets	$186,928* ($90,476)*	$899,721 ($252,500)
Unsecured debt (incl. priority debt)	$43,989* ($32,713)*	
Pretax annual income	$42,544* ($30,575)	$76,403 ($36,523)
Total debt/income	4.94 (3.20)*	0.78 (0.03)

Notes: Medians are shown in parentheses. The bankruptcy data are from the 2013-16 CBP. Nonbankruptcy data are from the Survey of Consumer Finances.

Elder Reasons for Filing

Medical expenses = 64%
Missed work for medical reasons = 40%
▸BOTH medical expenses and missed work = 70%

▸ Decline in income = 69%

▸ Financially help out family or friends = 36%

▸ Debt collection attempts = 72%

What In the World Is Going On—From the Perspective of a Social Scientist?

The 1980s and 1990s were the "Golden Years" of retirement

► Social Security provided 40% of pre-retirement income
► 65 was the age for full Social Security benefits
► Medicare coverage was good—out-of-pocket expenses were approximately12% of income
► Defined benefit (DB) plans (62%) and post-retirement health insurance were common

Great Risk Shift – beginning in 1980s

A situation whereby "a myriad of risks that were once managed and pooled by government and private corporations shifted onto individuals and families" (Hacker 2006).

► DB plans (17%) have been replaced with DC plans – investment decisions left to individuals
► Full retirement age for Social Security has increased to 70
► Inadequate coverage from Medicare—out-of-pocket has increased to 20% of income, $250,000 post-retirement (1995: Newt Gingrich: "Let it wither on the vine.")
► Employers are dropping retirees' post-retirement healthcare

Given these shifts, increases in elder filings are predictable

Implications of the risk shifts for older folks:

► Obviously, increased rates of filing bankruptcy

► Their wealth is being stripped. At the time of their bankruptcies, older folks had *negative* wealth of $17,390.

► Many **emptied their retirement accounts** to repay their debts.
The wealth that should have been there to sustain them until they die is gone; it has been transferred to the health care industry and the lending industry.

► Emotional and physical distress

So much research still needed to be done!

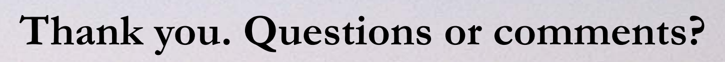
► We need to drill down to explore exactly what is behind the decline in income.
►We need to drill down to explore exactly which medical costs are unmanageable.
► At what age did they retire? If at 62, may have run out of money way too soon.
►We need to conduct longitudinal research and follow older filers to determine if the bankruptcy was beneficial. Did it provide them breathing room? Truth be told, they will never financially recover completely. They are too old for that.
► We need research to determine if older folks who file sooner, rather than later, are in better financial shape? Post-bankruptcy, do they have more wealth left to carry them for the rest of their lives?
► We need additional research to study what the stress of the debt and bankruptcy does to the older filers, physically and emotionally? From the stories, it appears that many of them experience severe medical and emotional problems due to the worry.
► We need to study the gendered element of elder bankruptcy. Given that women generally outlive their husbands, and we know that they are very likely to live in poverty, are they over-represented in bankruptcy?

The research on older folks and bankruptcy is heavy, disheartening, and frightening.

► What they are experiencing, at the ends of their lives, is tragic.
► The current political tone does not suggest that our country will move back toward shared risk anytime soon. Individuals will be left to manage on their own.
►Each of us, almost without exception, will be in the same precarious circumstances when we are old. Just one economic downturn or one medical crisis….

So what is to be done? Elder bankruptcy should be rare.
Increases were the result of policy decisions. Decreases will occur for the same reasons.

Non-wealthy elders were frequently shunted off to poorhouses, which were “dreary, vermin-infested, and laden with human waste” (Fleming, Evans and Chutka 2003:916). Elderly poor were regarded as “a burden on the local taxes” and were “despised and often treated as outcasts” (Fleming, Evans and Chutka 2003:914). In some communities, despite their advanced age, they were auctioned off for farm labor. Toward the end of the nineteenth century, contempt for older Americans peaked—old age was considered a disease and old people were obsolescent.


Thank you. Questions or comments?

2018 CONNECTICUT BANKRUPTCY CONFERENCE

UCC ARTICLE 9 SALES AS ALTERNATIVE TO BANKRUPTCY CODE SECTION 363 SALES

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OUTLINE ON LAW AND STRATEGIC CONSIDERATIONS

A. **Issue**: As a mechanism for disposing of distressed assets, Bankruptcy Code section 363 sales have become relatively expensive and time consuming and are subject to risks and lack of flexibility when compared to other possible methods of disposition.

1. Expense—bankruptcy professionals (debtor's counsel and committee professionals), US Trustee fees (now 1% of quarterly disbursements above $1 million)—cost of middle market case ($50 million revenue debtor) six months to close on sale and 1 year to close of case may be well in excess of $500,000.

2. Time—Difficult to obtain court approval and close in less than 120 to 180 days.

3. Risks—business failure, competitive bidding, opposition by creditor constituencies, court decision.

4. Lack of flexibility—fiduciary duties imposed on debtor and debtor's management that do not exist outside of bankruptcy.

B. **Other methods of disposition may not be or are not available**: no ABC statute in Connecticut, receivership statute and practice not well developed as in Rhode Island. Lender may be unwilling to take less than par payoff in refinance. Liquidation or foreclosure likely generates less value and destroys going concern.

C. **Nuts and Bolts of Article 9 Sale**

1. Sale as a Remedy

a. Default by borrower triggers secured party's statutory remedies under Uniform Commercial Code ("UCC") Article 9. UCC 9-601(a).

b. Secured party's remedy under Article 9 after default is disposition. One method of disposition is foreclosure sale under UCC 9-610(a).

2. Commercial Reasonableness—9-627

a. "Every aspect" of disposition must be "commercially reasonable." UCC 9-610(b).

b. Whether a sale is commercially reasonable is a question of fact.

c. Several factors determine whether a sale was commercially reasonable: the relationship of the price obtained to the recognized market price; the conformity of the sale to commercially accepted standards; the utilization of a recognized market in the sale; and the overall reasonableness of the means and methods of disposition under the circumstances

3. Mechanics

a. Public vs Private Sale—9-610

i. Public sale generally required if lender wants to purchase collateral.

ii. Private sale does not require marketing because public does not participate in the sale process. Buyer does not risk being outbid, but potential risks.

b. Notice—9-611, 9-612, 9-613

i. Must be reasonable with respect to timing, manner and content. Timeliness a question of fact, but 10 day safe harbor. 9-612

ii. Must go to debtor, any secondary obligor (guarantor), and other secured parties.

iii. Debtor and secondary obligor may waive notice, must be after default. 9-611(a)(2), 9-624

iv. Contents and form of notice. 9-613

c. Warranties—9-610(e), (d), (f)

4. Buyer Takes Free and Clear—9-617

i. But see cases on successor liability, fraudulent conveyance, unjust enrichment, aiding and abetting.

ii. Foreclosing party's lien and subordinate liens discharged.

D. **Considerations for Debtor/Obligor, Secured Party and Buyer**

1. Benefits

a. Speed—private sale may take place in matter of days. Preserve enterprise value.

b. Cost—low, very low compared to bankruptcy sale.

c. Certainty/control—control stays with secured lender, debtor and buyer. No court, US Trustee, committee, competing buyer, etc. No third party exercising independent judgment over the transaction.

d. Flexibility as a result of lack of fiduciary duty constraints—to, for example, deal with release of guaranties, employment of key people—which may be critical to both debtor and buyer.

e. Fiduciary duties of DIP not present.

f. Free and clear—but see cases on successor liability, fraudulent conveyance, unjust enrichment, aiding and abetting.

g. No competitive bidding (buyer).

h. Any challenges come after the fact.

2. Risks/Disadvantages

a. Successor liability, fraudulent conveyance, unjust enrichment, aiding and abetting. **But**—these cases are very difficult to recover on. May get past the summary judgment stage, but issues as to value, collectability, etc.

b. Transfer of real property.

c. Assignment of leases and contracts.

d. Only assets on which lender holds security interest.

e. Does not deal with the claims of unsecured creditors.

f. May not bring the highest price—though may be able to go through quick sale process.

g. Involuntary bankruptcy.

h. No court "free and clear" order.

SELECTED CASES

Commercial Reasonableness

Gaynor v. Union Trust Co., 216 Conn. 458, 478 (1990)

Connecticut Bank & Trust Co., N.A. v. Incendy, 207 Conn. 15 (1988)

Pirrotti v. Respironics, Inc., 2013 U.S. Dist. LEXIS 11137, [*43] (D. Conn. 2013)

- Every aspect of disposition, including method, manner, time, place and terms must be commercially reasonable.

- Burden is on secured party to establish the fair market value of the collateral at the time of sale by presenting evidence of the value other than the price received.

- Requires evidence of such things as the amount of advertising done, the number of people contacted, normal commercial practices in disposing of the particular collateral, the length of time between repossession and the sale, whether any deterioration in the collateral has occurred, the number of bids received, and the price obtained.

- Price received at sale of collateral is important and one of the relevant factors in determining whether sale was commercially reasonable, alone it is insufficient to establish that the sale was commercially reasonable or to establish the reasonable value of the collateral sold. It is only where the sale is conducted according to the requirements of Article 9 that the amount received or bid at a sale of collateral is evidence of its true value.

- Reasonableness is question of fact.

Successor Liability

Call Ctr. Techs., Inc. v. Grand Adventures Tour, 635 F.3d 48 (2nd Cir. 2011)

Pirrotti v. Respironics, Inc., 2013 U.S. Dist. LEXIS 11137, [*43] (D. Conn. 2013)

Greystone Community Reinvestment Ass'n, Inc. v. Berean Capital, Inc., 638 F.Supp.2d 278 (D.Conn. 2006)

Chamlink Corp. v. Merritt Extruder Corp., 96 Conn.App. 183 (Conn.App. 2006)

Ed Peters Jewelry Co. v. C&J Jewelry Co., 124 F.3d 252 (1st Cir. 1997)

- General rule—corporation which purchases all of the assets of another company does not become liable for the debts and liabilities of its predecessor unless (1) the purchase agreement expressly or impliedly so provides; (2) there was a merger or consolidation of the two firms; (3) the purchaser is a "mere continuation of the seller; or (4) the transaction is entered into fraudulently for the purpose of escaping liability.

- "De facto" merger where (1) continuation of the enterprise of the seller corporation so that there is a continuity of management, personnel, physical location, assets and general business operations; (2) continuity of shareholders; (3) seller corporation ceases its ordinary business operations, liquidates, and dissolves as soon as legally and practically possible; (4) purchasing corporation assumes those liabilities and obligations of the seller ordinarily necessary for the uninterrupted continuation of normal business operations of the seller corporation. All four factors need not be present, court applies balancing test.

- "Mere continuation" looks to whether there is continuity of enterprise as opposd to continuity of ownership. May be applicable where successor maintains same business, with same employees doing the same jobs, under the same supervisors, working conditions, and production processes, and produces the same products for the same customers.

- Successor liability under foregoing theories a question of fact.

- Purchase via Article 9 sale does not necessarily protect from successor liability claim.

Fraudulent Conveyance

Pirrotti v. Respironics, Inc., 2013 U.S. Dist. LEXIS 11137, [*43] (D. Conn. 2013)

Sourcing Management v. Simclair, Inc., 118 F.Supp. 899 (N.D. Tex. 2015)

In re Comprehensive Power, Inc., 578 B.R. 14 (Bankr. D. Mass. 2017)

- Actual fraud claims.

- Constructive Fraud claims.

- Transfer cannot be considered fraudulent if at the time of the transfer the transferred property is encumbered by valid liens exceeding the property's value.

- Purchase via Article 9 does not necessarily protect from fraudulent conveyance claim.

Fiduciary Duties

Master-Halco, Inc. v. Scillia, Dowling & Natarelli, 739 F.Supp. 2d 100 (D. Conn. 2010)

Baker & Taylor, Inc. v. AlphaCraze.com Corp., 2011 U.S. Dist. LEXIS 87801 (D. Conn. 2011)

Wells Fargo Bank, N.A. v. Konover, 2011 U.S. Dist. LEXIS 32079 (D. Conn. 2011)

Hyundai-Wai Machine Am. Corp. v. Rouette (In re Rouette), 500 B.R. 670 (Bankr. D. Conn. 2013).

- Outside of bankruptcy, whether a corporation is solvent or insolvent, officers and directors do not owe a fiduciary duty to creditors.

Smart World Technologies, LLC v. Juno Online Services (In re Smart World Technologies, LLC), 423 F.3d 166 (2nd Cir. 2005)

In re Signature Apparel Group, 577 B.R. 54 (Bankr. S.D.N.Y. 2017)

- DIP has fiduciary duty to estate—same fiduciary duty as a trustee to the creditors and the estate. Fiduciary obligations also fall upon the officers and directors who conduct the debtor in possession's affairs.

- Fiduciary obligations include obligation to refrain from self-dealing, to avoid conflicts of interest and the appearance of impropriety, to treat all parties to the case fairly, and to maximize the value of the estate.

Warranties

Ulbrich v. Groth, 310 Conn. 375 (2013)

- Disclaimers by bank of warranties of any kind not sufficient to disclaim implied warranty of title.

STATUTORY PROVISIONS

42a-9-610

(a) After default, a secured party may sell, lease, license or otherwise dispose of any or all of the collateral in its present condition or following any commercially reasonable preparation or processing.

(b) Every aspect of a disposition of collateral, including the method, manner, time, place and other terms, must be commercially reasonable. If commercially reasonable, a secured party may dispose of collateral by public or private proceedings, by one or more contracts, as a unit or in parcels, and at any time and place and on any terms.

(c) A secured party may purchase collateral:

(1) At a public disposition; or

(2) At a private disposition only if the collateral is of a kind that is customarily sold on a recognized market or the subject of widely distributed standard price quotations.

(d) A contract for sale, lease, license or other disposition includes the warranties relating to title, possession, quiet enjoyment and the like which by operation of law accompany a voluntary disposition of property of the kind subject to the contract.

(e) A secured party may disclaim or modify warranties under subsection (d):

(1) In a manner that would be effective to disclaim or modify the warranties in a voluntary disposition of property of the kind subject to the contract of disposition; or

(2) By communicating to the purchaser a record evidencing the contract for disposition and including an express disclaimer or modification of the warranties.

(f) A record is sufficient to disclaim warranties under subsection (e) if it indicates "There is no warranty relating to title, possession, quiet enjoyment or the like in this disposition" or uses words of similar import.

42a-9-611

(a) In this section, "notification date" means the earlier of the date on which:

(1) A secured party sends to the debtor and any secondary obligor an authenticated notification of disposition; or

(2) The debtor and any secondary obligor waive the right to notification.

(b) Except as otherwise provided in subsection (d), a secured party that disposes of collateral under section 42a-9-610 shall send to the persons specified in subsection (c) a reasonable authenticated notification of disposition.

(c) To comply with subsection (b), the secured party shall send an authenticated notification of disposition to:

(1) The debtor;

(2) Any secondary obligor; and

(3) If the collateral is other than consumer goods:

(A) Any other person from which the secured party has received, before the notification date, an authenticated notification of a claim of an interest in the collateral;

(B) Any other secured party or lienholder that, ten days before the notification date, held a security interest in or other lien on the collateral perfected by the filing of a financing statement that:
(i) Identified the collateral;

(ii) Was indexed under the debtor's name as of that date; and

(iii) Was filed in the office in which to file a financing statement against the debtor covering the collateral as of that date; and

(C) Any other secured party that, ten days before the notification date, held a security interest in the collateral perfected by compliance with a statute, regulation or treaty described in subsection (a) of section 42a-9-311.
(d) Subsection (b) does not apply if the collateral is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market.

(e) A secured party complies with the requirement for notification prescribed by subparagraph (B) of subdivision (3) of subsection (c) of this section if:

(1) Not later than twenty days or earlier than thirty days before the notification date, the secured party requests, in a commercially reasonable manner, information concerning financing statements indexed under the debtor's name in the office indicated in subparagraph (B) of subdivision (3) of subsection (c) of this section; and

(2) Before the notification date, the secured party:

(A) Did not receive a response to the request for information; or

(B) Received a response to the request for information and sent an authenticated notification of disposition to each secured party or other lienholder named in that response whose financing statement covered the collateral.

42a-9-612

(a) Except as otherwise provided in subsection (b), whether a notification is sent within a reasonable time is a question of fact.

(b) In a transaction other than a consumer transaction, a notification of disposition sent after default and ten days or more before the earliest time of disposition set forth in the notification is sent within a reasonable time before the disposition.

42a-9-613

Except in a consumer-goods transaction, the following rules apply:

(1) The contents of a notification of disposition are sufficient if the notification:

(A) Describes the debtor and the secured party;

(B) Describes the collateral that is the subject of the intended disposition;

(C) States the method of intended disposition;

(D) States that the debtor is entitled to an accounting of the unpaid indebtedness and states the charge, if any, for an accounting; and

(E) States the time and place of a public disposition or the time after which any other disposition is to be made.

(2) Whether the contents of a notification that lacks any of the information specified in subdivision (1) are nevertheless sufficient is a question of fact.

(3) The contents of a notification providing substantially the information specified in subdivision (1) are sufficient, even if the notification includes:

(A) Information not specified by that subdivision; or

(B) Minor errors that are not seriously misleading.

(4) A particular phrasing of the notification is not required.

(5) The following form of notification and the form appearing in subdivision (3) of section 42a-9-614, when completed, each provides sufficient information:

NOTIFICATION OF DISPOSITION OF COLLATERAL

To: .... (Name of debtor, obligor or other person to which the notification is sent)

From: .... (Name, address and telephone number of secured party)

Name of Debtor(s): .... (Include only if debtor(s) are not an addressee)

(For a public disposition:)

We will sell (or lease or license, as applicable) the .... (describe collateral) (to the highest qualified bidder) in public as follows:

Day and Date: ....

Time: ....

Place: ....

(For a private disposition:)

We will sell (or lease or license, as applicable) the .... (describe collateral) privately sometime after .... (day and date).

You are entitled to an accounting of the unpaid indebtedness secured by the property that we intend to sell (or lease or license, as applicable) (for a charge of $ ....). You may request an accounting by calling us at .... (telephone number).

42a-9-617

(a) A secured party's disposition of collateral after default:

(1) Transfers to a transferee for value all of the debtor's rights in the collateral;

(2) Discharges the security interest under which the disposition is made; and

(3) Discharges any subordinate security interest or other subordinate lien.

(b) A transferee that acts in good faith takes free of the rights and interests described in subsection (a), even if the secured party fails to comply with this article or the requirements of any judicial proceeding.

(c) If a transferee does not take free of the rights and interests described in subsection (a), the transferee takes the collateral subject to:

(1) The debtor's rights in the collateral;

(2) The security interest or agricultural lien under which the disposition is made; and

(3) Any other security interest or other lien.

42a-9-624

(a) A debtor or secondary obligor may waive the right to notification of disposition of collateral under section 42a-9-611 only by an agreement to that effect entered into and authenticated after default.

(b) A debtor may waive the right to require disposition of collateral under subsection (e) of section 42a-9-620 only by an agreement to that effect entered into and authenticated after default.

(c) Except in a consumer-goods transaction, a debtor or secondary obligor may waive the right to redeem collateral under section 42a-9-623 only by an agreement to that effect entered into and authenticated after default.

42a-9-625

(a) If it is established that a secured party is not proceeding in accordance with this article, a court may order or restrain collection, enforcement or disposition of collateral on appropriate terms and conditions.

(b) Subject to subsections (c), (d) and (f), a person is liable for damages in the amount of any loss caused by a failure to comply with this article. Loss caused by a failure to comply may include loss resulting from the debtor's inability to obtain, or increased costs of, alternative financing.

(c) Except as otherwise provided in section 42a-9-628:

(1) A person that, at the time of the failure, was a debtor, was an obligor or held a security interest in or other lien on the collateral may recover damages under subsection (b) for its loss; and

(2) If the collateral is consumer goods, a person that was a debtor or a secondary obligor at the time a secured party failed to comply with this part may recover for that failure in any event an amount not less than the credit service charge plus ten per cent of the principal amount of the obligation or the time-price differential plus ten per cent of the cash price.

(d) A debtor whose deficiency is eliminated under section 42a-9-626 may recover damages for the loss of any surplus. However, a debtor or secondary obligor whose deficiency is eliminated or reduced under section 42a-9-626 may not otherwise recover under subsection (b) for

noncompliance with the provisions of this part relating to collection, enforcement, disposition or acceptance.

(e) In addition to any damages recoverable under subsection (b), the debtor, consumer obligor, or person named as a debtor in a filed record, as applicable, may recover five hundred dollars in each case from a person that:

(1) Fails to comply with section 42a-9-208;

(2) Fails to comply with section 42a-9-209;

(3) Files a record that the person is not entitled to file under subsection (a) of section 42a-9-509;

(4) Fails to cause the secured party of record to file or send a termination statement as required by subsection (a) or (c) of section 42a-9-513; or

(5) Fails to comply with subsection (b) of section 42a-9-616.

(f) A debtor or consumer obligor may recover damages under subsection (b) and, in addition, five hundred dollars in each case from a person that, without reasonable cause, fails to comply with a request under section 42a-9-210. A recipient of a request under section 42a-9-210 which never claimed an interest in the collateral or obligations that are the subject of a request under that section has a reasonable excuse for failure to comply with the request within the meaning of this subsection.

(g) If a secured party fails to comply with a request regarding a list of collateral or a statement of account under section 42a-9-210, the secured party may claim a security interest only as shown in the list or statement included in the request as against a person that is reasonably misled by the failure.

42a-9-626

(a) In an action arising from a transaction, other than a consumer transaction, in which the amount of a deficiency or surplus is in issue, the following rules apply:

(1) A secured party need not prove compliance with the provisions of this part relating to collection, enforcement, disposition or acceptance unless the debtor or a secondary obligor places the secured party's compliance in issue.

(2) If the secured party's compliance is placed in issue, the secured party has the burden of establishing that the collection, enforcement, disposition or acceptance was conducted in accordance with this part.

(3) Except as otherwise provided in section 42a-9-628 , if a secured party fails to prove that the collection, enforcement, disposition or acceptance was conducted in accordance with the provisions of this part relating to collection, enforcement, disposition or acceptance, the liability of a debtor or a secondary obligor for a deficiency is limited to an amount by which the sum of the secured obligation, expenses and attorney's fees exceeds the greater of:

(A) The proceeds of the collection, enforcement, disposition or acceptance; or

(B) The amount of proceeds that would have been realized had the noncomplying secured party proceeded in accordance with the provisions of this part relating to collection, enforcement, disposition or acceptance.

(4) For purposes of subparagraph (B) of subdivision (3) of this subsection, the amount of proceeds that would have been realized is equal to the sum of the secured obligation, expenses and attorney's fees unless the secured party proves that the amount is less than that sum.

(5) If a deficiency or surplus is calculated under subsection (f) of section 42a-9-615 , the debtor or obligor has the burden of establishing that the amount of proceeds of the disposition is significantly below the range of prices that a complying disposition to a person other than the secured party, a person related to the secured party or a secondary obligor would have brought.
(b) The limitation of the rules in subsection (a) to transactions other than consumer transactions is intended to leave to the court the determination of the proper rules in consumer transactions. The court may not infer from that limitation the nature of the proper rule in consumer transactions and may continue to apply established approaches. Notwithstanding subsection (b) of section 42a-9-627 , those approaches may apply principles of existing statutory and case law, including laws concerning the determination of a deficiency or surplus, that apply to analogous consumer transactions in similar goods under part XI of chapter 669 1 and under other law of this state.

42a-9-627

(a) The fact that a greater amount could have been obtained by a collection, enforcement, disposition or acceptance at a different time or in a different method from that selected by the secured party is not of itself sufficient to preclude the secured party from establishing that the collection, enforcement, disposition or acceptance was made in a commercially reasonable manner.

(b) A disposition of collateral is made in a commercially reasonable manner if the disposition is made:

(1) In the usual manner on any recognized market;

(2) At the price current in any recognized market at the time of the disposition; or

(3) Otherwise in conformity with reasonable commercial practices among dealers in the type of property that was the subject of the disposition.

(c) A collection, enforcement, disposition or acceptance is commercially reasonable if it has been approved:

(1) In a judicial proceeding;

(2) By a bona fide creditors’ committee;

(3) By a representative of creditors; or

(4) By an assignee for the benefit of creditors.

(d) Approval under subsection (c) need not be obtained, and lack of approval does not mean that the collection, enforcement, disposition or acceptance is not commercially reasonable.

(e) Notwithstanding the provisions of subsection (b), in a consumer transaction the determination of a deficiency or surplus is subject to the court determination of the proper rule that applies to a consumer transaction under subsection (b) of section 42a-9-626.

EXAMPLE FORMS

SECURED PARTY SALE AGREEMENT

This Secured Party Sale Agreement (the **"Agreement"**) is entered into as of ______ __, 201_, by and between ____________ Bank (in such capacity, the **"Seller"**), and ____________________, a _________________ corporation (the **"Purchaser"**).

<u>WITNESSETH</u>

WHEREAS, Seller has a duly perfected security interest in and lien on substantially all of the assets of __________________, a Corporation (the **"Company"**), to secure all liabilities, obligations and indebtedness owing by the Company under that certain Loan Agreement dated as of _________ __, 201_ (as amended prior to the date hereof, the **"Loan Agreement"**), by and among, among others, the Seller and the Company, and the documents and instruments entered into in connection therewith (collectively, the **"Loan Documents"**);

WHEREAS, as of the date hereof, the Company is indebted to the Seller in an aggregate outstanding principal amount of $_____________ plus accrued and unpaid interest thereon, as provided in the Loan Agreement and the other Loan Documents;

WHEREAS, certain Events of Default (as defined in the Loan Agreement) have occurred and are continuing;

WHEREAS, as a result of such Events of Default and contemporaneously with the execution and delivery hereof, Seller is conducting a private sale to Purchaser pursuant to Section 9-610 of the UCC (as defined below) of Seller's interest in certain of the assets of the Company; and

WHEREAS, the parties desire to memorialize the terms and conditions under which Seller will sell to Purchaser, and Purchaser will purchase from Seller, Seller's interest in certain of the assets of the Company.

NOW THEREFORE, in consideration of the mutual covenants and agreements hereinafter set forth, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties agree as follows:

ARTICLE 1
THE TRANSACTIONS; CLOSING

1.1. Purchase and Sale of Purchased Assets. Subject to the terms and conditions of this Agreement, at the Closing (as hereinafter defined), the Seller, in its capacity as a secured creditor conducting a secured party sale pursuant to Section 9-610 of the UCC, shall sell, transfer, assign and deliver to the Purchaser, and Purchaser shall purchase from the Seller, all of Seller's interest in the assets of the Company that are subject to the Seller's perfected security interest and described on <u>**Schedule 1.1**</u> hereto (all of such assets being referred to herein as the **"Purchased Assets"**).

1.2. Excluded Assets. Notwithstanding anything to the contrary contained in this Agreement, the Purchased Assets do not include any assets of or relating to the Company in which Seller does not have a perfected security interest.

1.3. Certain Definitions. For purposes of this Agreement, the following terms shall have the meanings indicated below:

(a) "Affiliate" means, with respect to any specified Person, any other Person directly or indirectly controlling, controlled by or under common control with such specified Person.

(b) "Person" means an individual, a corporation, a partnership, a limited liability company, a trust, an unincorporated association, a governmental entity or any agency, instrumentality or political subdivision of a governmental entity, or any other entity or body.

(c) "UCC" means the Uniform Commercial Code as in effect from time to time in the State of Connecticut. Section references herein with respect to the UCC are to Article 9 of the Uniform Commercial Code as in effect from time to time in the State of Connecticut.

1.4. Consideration. The purchase price (the **"Purchase Price")** for the Purchased Assets shall be $_____________, which shall be paid in immediately available funds via wire transfer to the Seller in accordance with wire instructions to be provided by the Seller at or prior to the Closing.

1.5. Closing. The transactions contemplated hereby (the **"Transactions")** shall take place at a closing (the **"Closing")** to be held on ________ __, 201_, such other date as agreed to in writing by the Seller and the Purchaser (the **"Closing Date"),**

1.6. Terms of Sale.

(a) Subject to the terms and conditions set forth in this Agreement, the parties agree that the purchase and sale of the Purchased Assets (the "Sale") shall constitute a private secured party sale under Sections 9-610 *et seq.* of the UCC, other applicable law and the Loan Documents, of all of the Seller's interest in and to all of the Purchased Assets.

(b) Buyer previously requested information concerning financing statements indexed under the Company's name in the office in which to file a financing statement against the Company covering the Collateral (as defined in the Loan Agreement) as of such date. Buyer has determined that the only parties to whom notices of disposition (the "Notice of Disposition") are required to be sent with respect to the Sale contemplated hereby under Section 9-611(c) of the UCC are (i) the Company, as debtor, and (ii) ________________, as secondary obligor.

(c) NEITHER SELLER NOR PURCHASER IS ASSUMING AND NEITHER SHALL BE LIABLE FOR ANY DEBT, OBLIGATION, RESPONSIBILITY OR LIABILITY OF THE COMPANY OR OF ONE ANOTHER, WHETHER KNOWN OR UNKNOWN, CONTINGENT OR ABSOLUTE OR OTHERWISE AND WHETHER RELATING TO THE PURCHASED ASSETS, THE EXCLUDED ASSETS OR OTHERWISE, INCLUDING, WITHOUT LIMITATION, ANY DEBT, OBLIGATION, RESPONSIBILITY OR LIABILITY WITH RESPECT TO EQUIPMENT LEASES, REAL PROPERTY LEASES OR CONTRACTS. IN FURTHERANCE AND NOT IN LIMITATION OF THE

FOREGOING, PURCHASER DOES NOT ASSUME ANY LIABILITY UNDER ANY EQUIPMENT LEASE, REAL PROPERTY LEASE OR OTHER CONTRACT QNLESS PURCHASER AFFIRMATIVELY ASSUMES SUCH LIABILITY IN WRITING, WHICH MAY OCCUR AT OR FOLLOWING THE CLOSING IN THE SOLE DISCRETION OF PURCHASER.

(d) Upon payment in full of the Purchase Price, Seller shall deliver to Purchaser a fully executed copy of the Secured Party Bill of Sale in the form attached as Exhibit A hereto (the **"Bill of Sale").** If there is any conflict between this Agreement and the Bill of Sale with respect to the transfer of the Purchased Assets, the Bill of Sale shall control.

1.7. Liabilities and Liens Remain Outstanding. Except to the extent of the Purchase Price received from Purchaser, which shall be applied by Seller to the obligations of the Company under the Loan Documents in such manner as it determines in its sole and absolute discretion, the obligations of the Company under the Loan Documents shall remain outstanding, and Seller does not release any, but instead specifically reserves: (i) all rights to recover any deficiency against the Company under the Loan Documents, and (ii) all rights against the Company under the Loan Documents and otherwise. The parties do not intend the Transactions to be (nor shall the Transaction be deemed to be) a "strict foreclosure" or "acceptance of collateral in full satisfaction of any secured obligation" as described in § 9-620 of the UCC. Seller reserves each and every such right described above.

ARTICLE2

DISCLAIMER OF WARRANTIES BY SELLER

2.1. No Other Representations or Warranties. Purchaser acknowledges that neither the Seller nor any of its directors, officers, stockholders, employees, consultants, agents or advisors makes or has made any representation or warranty to Purchaser, its Affiliates or its financing sources, and that Seller's interests in and to the Purchased Assets are being conveyed to Purchaser "as-is and where-is," in each case. Seller disclaims any and all warranties of title, possession, quiet enjoyment and the like. There is no warranty relating to title, possession, quiet enjoyment or the like in this disposition. There is no warranty regarding the priority of Seller's liens and security interests in and to the Purchased Assets.

ARTICLE3
CONDITIONS TO CLOSING

3.1. Conditions to Obligations of the Purchaser. Unless waived in writing by the Purchaser, the obligation of the Purchaser hereunder to consummate the Transactions is subject to the satisfaction at or prior to the Closing of the following conditions:

(a) Deliveries By Seller. At the Closing, Seller shall deliver, or cause to be delivered, to Purchaser, the following:

(i) a duly executed Bill of Sale, together with a transfer statement (as defined in the UCC) signed by Seller;

Purchase Price;

(ii) a receipt duly executed by Seller evidencing payment of the

(iii) such other instruments or documents as Purchaser reasonably may request to fully effect the transfer of the Purchased Assets and to confer upon Purchaser the benefits contemplated by this Agreement.

3.2. Conditions to Obligations of the Seller. Unless waived in writing by the Seller, the obligation of the Seller hereunder to consummate the Transactions is subject to the satisfaction at or prior to the Closing of the following conditions:

(a) Deliveries By Purchaser. At the Closing, Purchaser shall deliver, or cause to be delivered, to Seller, the following:

(i) the Purchase Price in immediately available funds via wire transfer in accordance with instructions to be provided by Seller at or prior to Closing;

(ii) A countersigned Bill of Sale; and

(iii) such other instruments or documents as Seller reasonably may request to fully effect the transfer of the Purchased Assets and to confer upon Seller the benefits contemplated by this Agreement.

(b) Consent of Company and Guarantor. Seller shall have received a fully executed copy of the Acknowledgment and Consent to this Agreement in the form attached hereto as Exhibit B executed by the Company and Guarantor (as defined therein).

ARTICLE4
MISCELLANEOUS

4.1. Governing Law; Forum. This Agreement shall be governed by and construed in accordance with the internal laws of the State of Connecticut. Any judicial proceeding arising out of or relating to this Agreement shall be brought in the courts of the State of Connecticut, and, by execution and delivery of this Agreement, each of the parties to this Agreement accepts the exclusive jurisdiction of such courts, and irrevocably agrees to be bound by any judgment rendered thereby in connection with this Agreement.

4.2. Amendments, Waivers. This Agreement may be amended or modified only with the written consent of the Purchaser and the Seller. No waiver of any term or provision hereof shall be effective unless in writing signed by the party waiving such term or provision. No failure to exercise or delay in exercising any right, power or remedy hereunder shall operate as a waiver thereof; nor shall any single or partial exercise of any right, power or remedy hereunder preclude any other or further exercise thereof or the exercise of any other right, power or remedy. The rights provided hereunder are cumulative and not exclusive of any rights, powers or remedies provided by law.

4.3. Expenses. Except as otherwise expressly set forth herein, all legal and other costs and expenses incurred in connection with this Agreement and the Transactions contemplated hereby shall be paid by the party incurring such costs and expenses.

4.4. Successors and Assigns. This Agreement, and all provisions hereof, shall be binding upon and inure to the benefit of the respective successors and assigns of the parties hereto, provided that this Agreement may not be assigned by any party without the prior written consent of the other parties.

4.5. Entire Agreement. This Agreement, the attached exhibits and schedules, and the other agreements, documents and instruments contemplated hereby contain the entire understanding of the parties, and there are no further or other agreements or understandings, written or oral, in effect between the parties relating to the subject matter hereof unless expressly referred to herein.

4.6. Counterparts. This Agreement may be executed in one or more counterparts, and with counterpart facsimile or electronic signature pages, each of which shall be an original, but all of which when taken together shall constitute one and the same Agreement.

4.7. Headings. The headings of Articles and Sections herein are inserted for convenience of reference only and shall be ignored in the construction or interpretation hereof.

4.8. Further Assurances. Following the Closing, the parties will execute and deliver such documents and take such other actions as may be reasonably requested from time to time by the Purchaser or the Seller in order to fully consummate the Transactions.

4.9. Third Party Beneficiaries. Nothing in the Agreement shall be construed to confer any right, benefit or remedy upon any Person that is not a party hereto or a permitted assignee of a party hereto, except as otherwise expressly set forth in this Agreement.

4.10. No Strict Construction. The parties hereto have participated jointly in the negotiation and drafting of this Agreement and the other agreements and documents contemplated herein. In the event an ambiguity or question of intent or interpretation arises under any provision of this Agreement or any other agreement or documents contemplated herein, this Agreement and such other agreements or documents shall be construed as if drafted jointly by the parties thereto, and no presumption or burden of proof shall arise favoring or disfavoring any party by virtue of authoring any of the provisions of this Agreement or any other agreements or documents contemplated herein.

4.11. Schedules and Exhibits. All Schedules and Exhibits to this Agreement are an integral part of this Agreement and are incorporated herein by reference in this Agreement for all purposes of this Agreement. No information set forth on any Schedule shall be deemed to broaden in any way the scope of the Seller's representations and warranties. Neither the specification of any dollar amount in the representations and warranties contained in this Agreement nor the inclusion of any item on a Schedule is evidence of or intended to imply the materiality of such item for purposes of the Agreement, or that such item

is a disclosure required under the Agreement. Any description of any agreement, document, instrument, plan, arrangement or other item set forth in a Schedule is a summary only and is qualified in its entirety by the terms of such agreement, document, instrument, plan, arrangement or item, copies of which have been made available to the Purchaser. No disclosure in any Schedule relating to any possible breach or violation of any agreement, law or regulation shall be construed as an admission or indication that any such breach or violation exists or has actually occurred, or shall constitute an admission of liability to any third party.

4.12. Waiver of Jury Trial. EACH PARTY HERETO ACKNOWLEDGES AND AGREES THAT ANY CONTROVERSY WHICH MAY ARJSE UNDER THIS AGREEMENT IS LIKELY TO INVOLVE COMPLICATED AND DIFFICULT ISSUES, AND THEREFORE IT HEREBY IRREVOCABLY AND UNCONDITIONALLY WAIVES ANY RJGHT IT MAY HAVE TO A TRJAL BY JURY IN RESPECT OF ANY LITIGATION DIRECTLY OR INDIRECTLY ARJSING OUT OF OR RELATING TO THIS AGREEMENT AND ANY OF THE AGREEMENTS DELIVERED IN CONNECTION HEREWITH OR THE TRANSACTIONS CONTEMPLATED HEREBY OR THEREBY.

4.13. Severability. This Agreement shall be interpreted in such a manner as to be effective and valid under applicable law, but if any provision hereof shall be prohibited or invalid under any such law, such provision shall be ineffective to the extent of such prohibition or invalidity, without invalidating or nullifying the remainder of such provision or any other provisions of this Agreement. If any one or more of the provisions contained in this Agreement shall for any reason be held to be excessively broad as to duration, geographical scope, activity or subject, such provisions shall be construed by limiting and reducing it so as to be enforceable to the maximum extent permitted by applicable law.

4.14. Certain Taxes. All transfer, documentary, sales, use, real property gains, stamp, registration, and other such Taxes and fees incurred in connection with this Agreement shall be paid by the Purchaser when due.

[Signature page follows]

IN WITNESS WHEREOF, the parties hereto have executed and delivered this Agreement as a sealed instrument as of the date first above written.

SELLER:

By: ______________________________

Name:
Title:

PURCHASER:

By: ____

Name: Title:

Notices of Private Disposition of Collateral

April 8, 2013
VIA CERTIFIED MAIL NO.
REGULAR U.S. MAIL AND EMAIL:
____ Corp.
_____ Washington Avenue
St. Louis, MO 63103
Attn:

NOTICE OF PRIVATE DISPOSITION OF COLLATERAL UNDER SECTION 9-611 OF THE UNIFORM COMMERCIAL CODE

Names of Debtors: (collectively, the "**Debtors**", and each separately, a "**Debtor**")
Bank of _______, N.A. is the Administrative Agent for the Lenders (collectively, the "**Secured Party**") under that certain Credit Agreement dated August 30, 2010 with ____ Corp. (as amended, the "**Credit Agreement**"). Pursuant to that certain Guaranty and Collateral Agreement dated August 30, 2010 (as amended, the "**Security Agreement**"), each Debtor granted the Secured Party a security interest in all of its Collateral (as defined in the Security Agreement). The Debtors are in default of their obligations under the Credit Agreement and the Security Agreement.

This notice is being sent to you pursuant to Section 9-611 of the Uniform Commercial Code (the "**UCC**"). The Secured Party intends to foreclose upon its security interest in the Collateral described on Exhibit A hereto (the "**Sale Collateral**") by private sale of the Sale Collateral conducted on or after April 18, 2013 (the "**Sale**"). The Secured Party reserves the right to sell the Sale Collateral in a single lot or in multiple lots, by way of one or more contracts, and on such terms and conditions as are agreed upon between the Secured Party and any purchaser of the Sale Collateral. The Secured Party reserves the right to add to, withdraw or otherwise modify or amend in any respect whatsoever all or any portion of the Sale Collateral listed in Exhibit A as being subject to the Sale, for any reason whatsoever.

You are entitled to an accounting of the unpaid indebtedness secured by the property that the Secured Party intends to sell. The Secured Party's charge for an accounting shall be in an amount equal to its costs and expenses (including attorney fees) incurred as a result of providing such accounting. You may request an accounting by calling ______________ at (XXX) XXX-XXXX.

Except to the extent that such right is waived, the Debtors, any secondary obligor, or any other secured party or lienholder has the right to redeem the Sale Collateral at any time before the Secured Party has disposed of the Sale Collateral or entered into a contract for its disposition by tendering payment of all indebtedness secured by the Sale Collateral as well as any expenses reasonably incurred by the Secured Party in retaking, holding and preparing the Sale Collateral for disposition, in arranging for the Sale, and, to the extent provided in the Security Agreement and not prohibited by law, the Secured Party's reasonable attorneys' fees and legal expenses. If

the proceeds of the Sale are less than the amount owed to Secured Party by the Debtors, the Secured Party will seek to recover such amount from the Debtors and/or any secondary obligators in accordance with applicable law.

By selling and purchasing the Sale Collateral pursuant to the private Sale referenced herein, neither the Secured Party nor any purchaser of the Sale Collateral shall assume any liability or obligation whatsoever regarding any debts, expenses or liabilities of the Debtors or any other person or entity, and all such debts, expenses and liabilities shall not be assumed or deemed to be assumed by the Secured Party or any purchaser. Neither the Secured Party nor any purchaser shall be, or shall be deemed to be, a "successor" of or to any Debtor any other person or entity for any purpose.

The Secured Party reserves all of its rights and remedies, of any and every type or nature whatsoever, against the Debtors and all other persons and entities for any and all deficiencies under any obligations remaining due to the Secured Party after the Sale. The private Sale referenced herein is not intended to be, nor shall it be deemed to be, a "strict foreclosure" or "acceptance of collateral in full or partial satisfaction of obligation" as set forth in Section 9-620 of the UCC.

___________ OF AMERICA, N.A., as Administrative Agent for the Lenders

By:

____

Its Attorney

Copy to:

VIA CERTIFIED MAIL NO.

<u>REGULAR U.S. MAIL AND EMAIL:</u>

<u>EXHIBIT A</u> (Description of Sale Collateral)

All "equipment" (as that term is defined in Section 9-102(a)(33) of the UCC) located in the United States and Puerto Rico.

All "fixtures" (as that term is defined in Section 9-102(a)(41) of the UCC) located in the United States and Puerto Rico.

All "general intangibles" (as that term is defined in Section 9-102(a)(42) of the UCC).

All "inventory" (as that term is defined in Section 9-102(a)(48) of the UCC) located in the United States and Puerto Rico.

Abundant Splits in Consumer and Reorganization Law

1st Annual Connecticut
Bankruptcy Conference
Westbrook, Connecticut
October 4, 2018

Bill Rochelle • Editor-at-Large
American Bankruptcy Institute
bill@abi.org • 703. 894.5909
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Supreme Court

Decided Last Term

Intermediate transfers to financial institutions do not trigger the safe harbor.

Supreme Court Narrowly Interprets the Safe Harbor, Overrules the Majority of Circuits

Resolving a split of circuits, the Supreme Court ruled unanimously today in *Merit Management Group LP v. FTI Consulting Inc.* that the so-called safe harbor under Section 546(e) only applies to “the transfer that the trustee seeks to avoid.” In other words, using a bank as an escrow agent does not preclude a trustee from recovering a constructively fraudulent transfer under Section 548(a)(1)(B), when the trustee is seeking to recover from the ultimate recipient of the transfer but not from an intermediary bank.

The Supreme Court had been asked to resolve a split of circuits and decide whether the safe harbor applies when a financial institution is only a “mere conduit.” Instead, the unanimous opinion by Justice Sonia Sotomayor decided the case on a different and broader ground. The opinion may lead to a rethinking of safe harbor cases and might open the door to suits that previously were believed to rest comfortably within the safe harbor.

The Seventh Circuit Opinion

The case came to the Supreme Court from the Seventh Circuit, where a bankruptcy trustee had sued a selling shareholder in the leveraged buyout of a non-public company. The transaction was structured so that the purchase price for the stock initially came from an investment bank and was transferred to a commercial bank acting as escrow agent. As escrow agent, the bank paid a total of $16.5 million to the selling shareholder. The trustee sued the selling shareholder for receipt of a constructively fraudulent transfer.

The district court granted a motion to dismiss, reasoning that the safe harbor applied because the transfer included both a transfer from an investment bank and a transfer to a commercial bank, before the funds ended up in the hands of the selling shareholder.

On appeal, the Seventh Circuit reversed, in an opinion by Chief Circuit Judge Diane P. Wood. *FTI Consulting Inc. v. Merit Management Group LP*, 830 F.3d 690 (7th Cir. July 28, 2016).

The Seventh Circuit opinion stands for the proposition that routing consideration for an LBO of a non-public company through a financial institution cannot preclude a fraudulent transfer attack if it turns out that the seller was rendered insolvent.

Since the purchaser was buying stock, it was clear to the Seventh Circuit that the transfers were either a settlement payment or a payment in connection with a securities contract. The appeals

court said it was therefore only necessary to decide whether the safe harbor protects transactions "simply [because they were] conducted through financial institutions."

The Seventh Circuit refused to "interpret the safe harbor so expansively that it covers any transaction involving securities that uses a financial institution or other named entity as a conduit for funds." Instead, the appeals court said "it is the economic substance of the transaction that matters."

The Chicago-based appeals court therefore reversed the district court, which had utilized the safe harbor to dismiss the trustee's suit.

The Seventh Circuit opinion deepened an existing circuit split because the Second, Third, Sixth, Eighth and Tenth Circuits have invoked the safe harbor when a financial institution is nothing more than a conduit. The Eleventh Circuit was aligned with the Seventh, requiring the financial institution to be more than a conduit.

The defendant-selling shareholder filed a petition for *certiorari*, which the Supreme Court granted in May 2017. Oral argument was held on Nov. 6.

The Unanimous Opinion

The seeds for Justice Sotomayor's opinion were sown in an exchange at oral argument between Justice Anthony M. Kennedy and former Solicitor General Paul D. Clement, counsel for the trustee. Justice Kennedy asked whether the opinion should be qualified to require that the financial institution have an "equity participation" before the safe harbor applies.

Clement said he had a "simpler way to write the opinion[: by just looking] to the transfer that the trustee seeks to avoid." And that's what Justice Sotomayor did.

Laying out the statute in full text in her opinion, Justice Sotomayor traced the many amendments to the safe harbor, saying Congress "each time expand[ed] the categories of covered transfers or entities."

In pertinent part, Section 546(e) provides that a trustee "may not avoid a transfer" that is a "settlement payment . . . made by or to (or for the benefit of) a . . . financial institution" or that "is a transfer made by or to (or for the benefit of) a . . . financial institution . . . in connection with a securities contract . . . ."

Justice Sotomayor framed the question as whether the safe harbor applied because the transfer was "'made by or to (or for the benefit of) a . . . financial institution.'" She said that asking whether the bank had a beneficial interest in the transferred property "put the proverbial cart before the horse."

Before deciding whether the transfer was made to a covered entity, "the court must first identify the relevant transfer," she said.

Justice Sotomayor devoted the bulk of her opinion to explaining why the "language of Section 546(e)," the "specific context in which that language is used, and the broader statutory structure all support the conclusion that the relevant transfer for purposes of the Section 546(e) safe-harbor inquiry is the overarching transfer that the trustee seeks to avoid." She said the trustee properly identified the transfer as the sale of stock by the seller to the buyer, not intermediate transfers involving investment or commercial banks.

Uttering a phrase that will be cited countless times in the future, Justice Sotomayor cautioned that a trustee "is not free to define the transfer it seeks to avoid in any way it chooses."

Justice Sotomayor devoted the final third of her 19-page opinion to refuting the selling shareholder's arguments. The last part of her opinion arguably broadens the scope of the holding and makes the safe harbor more narrow than it is now generally understood to be.

She said that the addition of "(or for the benefit of)" in 2006 was only intended for the scope of the safe harbor to match the scope of the avoiding powers, where similar language is used. She rejected the selling shareholder's contention that the language was intended to bar avoidance if the financial institution was an intermediary without a financial interest in the transfer.

Next, the selling shareholder mounted an argument based on the inclusion of a securities clearing agency as one of the entities covered by the safe harbor.

If the relevant transfer is from the buyer to the seller, Justice Sotomayor said, "the question then becomes whether the transfer was 'made by or to (or for the benefit of)' a covered entity," such as a clearing agency.

Answering her own question, Justice Sotomayor said, "If the transfer that the trustee seeks to avoid was made 'by' or 'to' a securities clearing agency . . . , then Section 546(e) will bar avoidance, and it will do so without regard to whether the entity acted only as an intermediary."

On the next page, Justice Sotomayor acknowledged there was "good reason to believe that Congress was concerned about transfers '*by* an industry hub.'" [Emphasis in original.]

She went on to say that the safe harbor protects securities transactions "'made by or to (or for the benefit of)' covered entities. See Section 546(e). Transfers 'through' a covered entity, conversely, appear nowhere in the statute."

What exactly did the justice mean by her statements?

It was generally understood, at least before today's opinion, that a trustee could not recover a fraudulent transfer resulting from the sale of stock in a publicly held company, because the payoff to the selling shareholder would have been made through a "covered entity," like a clearing agent. Does today's opinion mean that a trustee for a public company can recover from selling shareholders but, of course, not from a clearing agent?

It had also been held that the LBO of a privately held company was protected by the safe harbor, if the sale of the stock utilized a bank somewhere in the stream of payments. It seems reasonably clear that an LBO of a privately held is no longer protected, unless the transferee is a financial institution.

However, what results if the transfer ends up in the coffers of a bank that held a lien on the stock being sold? May the trustee recover only from the beneficial owner of the stock but not from the bank where the money ended up?

The meaning of *Merit Management* will be debated in other contexts. For instance, the Second Circuit held in *Note Holders v. Large Private Beneficial Owners (In re Tribune Co.)*, 818 F.3d 98 (2d Cir. 2016), that the safe harbor bars suits by creditors under state law to recover payments made in securities transactions.

In *Tribune*, the Second Circuit concluded that Congress intended broad protection for securities markets, even to the extent of barring creditors from prosecuting claims that belong to them and not to bankruptcy trustees. Does *Merit Management* undercut the Second Circuit's notion that the safe harbor broadly immunizes any transaction involving securities whenever there has been a bankruptcy?

The opinion is *Merit Management Group LP v. FTI Consulting Inc.*, 16-784 (Sup. Ct.).

Some justices are critical of the existing test for ruling on non-statutory insider status.

Supreme Court Says Insider Status Is Reviewed for Clear Error Under Existing Test

The Supreme Court used a bankruptcy case to elucidate the standard of review when an appellate court confronts a mixed question of law and fact. According to Justice Elena Kagan, who wrote the March 5 opinion for the unanimous Court, clear error was the proper standard of review because the arm's-length nature of the transaction was primarily factual in nature.

In concurring opinions, four justices questioned whether the Ninth Circuit employed the proper legal test for non-statutory insider status. Implying that the dissenter in the Ninth Circuit was on the right track, they laid out a test for non-statutory insider status that would be more consonant with the statute and produce a different outcome.

At oral argument in the Supreme Court on October 31, it seemed possible that the justices might rule that review is *de novo* when the facts in the trial court were undisputed. However, the Court's opinion hewed to the traditional notion that inferences taken from undisputed facts are reviewed for clear error.

The Ninth Circuit Decision

In this chapter 11 reorganization, there were only two creditors. One was a bank with a $10 million secured claim. The other was the debtor's general partner, who had a $2.8 million unsecured claim.

The bank opposed the plan and could have defeated confirmation for lack of an accepting class, because the insider's vote could not be counted under Section 1129(a)(10) in cramming down the plan on the bank.

To create an accepting class and open the door to confirmation via cramdown, the insider sold her claim for $5,000 to a very close friend. The plan provided a $30,000 distribution on the unsecured claim.

The bankruptcy judge ruled that the buyer automatically became an insider by purchasing the insider's claim. The Bankruptcy Appellate Panel reversed and was upheld by the Ninth Circuit in a 2-1 opinion.

All three circuit judges agreed that the purchaser did not automatically become an insider by purchasing the insider's claim. The majority then said that status as an insider entails a "factual

inquiry that must be conducted on a case-by-case basis." To be a non-statutory insider, the appeals court laid out a two-part test. A claim buyer "must have a close relationship with the debtor and negotiate the relevant transaction at less than arm's length."

The Ninth Circuit did not remand the case to the bankruptcy court because the bankruptcy judge had ruled that the buyer purchased the insider's claim in an arm's-length transaction. Since the purchaser bought the claim at arm's length, the second prong of the test had not been met, leading the majority on the Ninth Circuit to rule that the purchaser was not a non-statutory insider.

The majority on the circuit court therefore upheld the appellate panel because the bankruptcy judge's findings of fact on insider status were not clearly erroneous.

Circuit Judge Richard R. Clifton dissented in part. It was "clear" to him that the buyer should have been deemed an insider. In his view of the facts, the sale was not negotiated at arm's length.

The Petition for *Certiorari*

The bank filed a petition for *certiorari*, which was granted in March 2017. The Court limited its review to the appellate standard of review. The U.S. Solicitor General, who had opposed granting *certiorari*, submitted a merits brief on the side of the debtor and argued that the Ninth Circuit properly applied the clear-error standard of appellate review. The Solicitor General did not take a position on whether the bankruptcy judge committed clear error.

The Unanimous Opinion

In her 11-page opinion for the unanimous court, Justice Kagan said that courts have developed standards for non-statutory insiders that "are not entirely uniform." Many, she said, focus on whether the transaction was conducted at arm's length.

The buyer and seller were in a romantic relationship but lived apart and kept their finances separate. Despite the close relationship, the bankruptcy judge had found that the sale of the claim was negotiated at arm's length.

Justice Kagan said that the bankruptcy court had correctly applied the Ninth Circuit's two-part test. The Supreme Court, however, did not include a review of the test within the grant of *certiorari*. Instead, the Court only agreed to review the proper appellate standard for a ruling on non-statutory insider status.

Parsing the standards of appellate review, Justice Kagan said that findings of historical fact — such as "what, when or where, how or why" — are reviewable for clear error.

On the other hand, whether historical facts satisfy the test for non-statutory insider status is a mixed question of law and fact, Justice Kagan said. She then said that mixed questions "are not all alike."

Pinpointing the standard of review for mixed questions "all depends," she said, on whether the work of the appellate court is "primarily legal or factual."

Deciding whether the sale of the claim was "conducted as if the [buyer and seller] were strangers to each other" was "about as factual sounding as any mixed question gets," Justice Kagan said. Indeed, she said, applying the Ninth Circuit's two-part test amounts to what the Court "previously described as 'factual inferences[] from undisputed facts."

Justice Kagan said that the bankruptcy court had the "closest and the deepest understanding of the record" from hearing the witnesses and presiding over the presentation of evidence.

The appellate standard of review was therefore for clear error because the appellate court was called on to perform "[p]recious little" legal work in applying the Ninth Circuit's two-part test.

Approaching the issue from a different direction, Justice Kagan said that even a *de novo* review "will not much clarify legal principles or provide guidance to other courts resolving other disputes."

The Concurring Opinions

Justice Sonia Sotomayor wrote a seven-page concurring opinion joined by Justices Anthony M. Kennedy, Clarence Thomas, and Neil M. Gorsuch.

Justice Sotomayor said it "is not clear to me" that the two-prong test in the Ninth Circuit "is consistent with the plain meaning of the term 'insider' as it appears in [Section 101(31) of] the Code."

The enumerated statutory insiders in Section 101(31) do not lose that status, Justice Sotomayor said, by negotiating at arm's length. Therefore, she said, "it is not clear why the same should not be true of non-statutory insiders."

Finding shortcomings in the Ninth Circuit's test, Justice Sotomayor proceeded to offer two other tests.

First, the court could focus on "commonalities" between enumerated insiders and "characteristics of the alleged non-statutory insider." Second, the court might consider "other aspects of the parties' relationship" if the transaction was negotiated at arm's length.

Had the trial court applied one of her proposed tests, Justice Sotomayor said it "is conceivable" that the standard for review might have been different.

In the penultimate paragraph of her concurrence, Justice Sotomayor said that the facts of the case as applied to one of her two alternative tests may have resulted in a finding that the purchaser was an insider, even if the clear-error test were applied.

In a signal that she and her three colleagues were dissatisfied with the Ninth Circuit's existing test, Justice Sotomayor ended her opinion by imploring courts "to grapple with the role that an arm's-length inquiry should play in a determination of insider status."

Justice Kennedy wrote a separate two-page concurrence to emphasize that the Court's opinion should not be taken as an endorsement for the Ninth Circuit's existing two-part test. He also questioned whether the bankruptcy judge was correct in finding that the purchaser was not an insider, but said "*certiorari* was not granted on this question."

The opinion is *U.S. Bank NA v. The Village at Lakeridge LLC,* 15-1509 (Sup. Ct. March 5, 2018).

High court resolves a circuit split on Section 523(a)(2)(B) and the meaning of "financial condition."

A False Statement About One Asset **Isn't Grounds for** Nondischargeability

The Supreme Court resolved a split of circuits today by holding that a false statement about one asset must be in writing to provide grounds for rendering a debt nondischargeable under Section 523(a)(2).

The 15-page opinion by Justice Sonia Sotomayor focused primarily on the plain language of the statute and the meaning of the word "respecting." The opinion was unanimous, except that Justices Clarence Thomas, Samuel A. Alito Jr. and Neil M. Gorsuch did not join in a section of the decision where Justice Sotomayor buttressed her conclusion by relying on legislative history surrounding the adoption of the Bankruptcy Code in 1978.

The case pitted courts' aversion to those who lie against the statutory language and its history. In a sense, the result is akin to *Law v. Siegel*, 134 S. Ct. 1188 (2014), where the Supreme Court ruled that the bankruptcy court does not have a "roving commission" to do equity. In *Law*, the high court barred the imposition of sanctions by invading property made exempt by statute, even though the debtor persistently committed fraud.

A ruling the other way would have led to anomalous results. If a smaller lie about one asset could result in nondischargeability, a bigger lie about a debtor's entire net worth would provide no grounds for nondischargeability unless it were in writing.

While courts may not be favorably inclined toward debtors who lie orally to obtain credit, Congress made a decision in Section 523(a)(2)(B) that a materially false statement "respecting the debtor's . . . financing condition" must be in writing to provide grounds for nondischargeability of the related debt.

The Case Below

A client told his lawyers that he was to receive a large tax refund enabling him to pay his legal bills. The lawyers continued working, based on the oral representation.

Although the refund was smaller than represented, the client spent it on his business, falsely telling his lawyers that he had not received the refund. The lawyers continued working. Years later, they obtained a judgment they could not collect after the client filed bankruptcy.

Affirmed in district court, the bankruptcy judge held that the claim for legal fees was not discharged. The Eleventh Circuit reversed in a Feb. 15, 2017, opinion by Circuit Judge William Pryor, *Appling v. Lamar, Archer & Cofrin LLP (In re Appling)*, 848 F.3d 953 (11th Cir. Feb. 15, 2017). To read ABI's discussion of the Eleventh Circuit opinion, click here.

The creditor filed a petition for *certiorari*, which the Supreme Court granted on the recommendation of the U.S. Solicitor General, who later submitted an *amicus* brief supporting the debtor, arguing that the Eleventh Circuit was correct, and contending that an oral misstatement about one asset is a statement about "financial condition" that must be in writing before the debt can be declared nondischargeable.

The circuits were split. The Fifth and Tenth Circuit held that a false statement about one asset can result in nondischargeability, while the Eleventh Circuit had joined the Fourth in holding that a statement about any asset must be in writing to provide grounds for nondischargeability.

The justices heard oral argument on April 17.

Another 'Plain Language' Opinion

The creditor-petitioner argued that a statement about a debtor's overall financial condition is the only type of statement "respecting" financial condition that can result in nondischargeability under Section 523(a)(2)(B). According to the creditor, a lie about one asset is not about "financial condition." Rather, the law firm contended that a lie about one asset falls within the ambit of Section 523(a)(2)(A) and leads to a nondischargeable debt because it is a "false representation." Under (a)(2)(A), there is no requirement that a "false representation" be in writing before the debt can be nondischargeable.

As is her style, Justice Sotomayor was quick to the point. In the second paragraph of her opinion, she said that the "statutory language makes plain that a statement about a single asset can be a 'statement respecting the debtor's financial condition.'" If the statement was not made in writing, she said, "the associated debt may be discharged, even if the statement was false."

Justice Sotomayor said that the Bankruptcy Code does not define three critical terms: "statement," "financial condition," and "respecting." Only "respecting" was in dispute, she said.

Looking to several dictionaries, Justice Sotomayor said that "respecting" means "in view of: considering; with regard or relation to: regarding, concerning." At least in the context of the instant case, she said that "related to" does not have a "materially different meaning" than "about," "concerning," "with reference to," or "as regards." The words all have circular definitions, she said.

In the realm of statutory construction and drafting, Justice Sotomayor said that "respecting" "generally has a broadening effect" and "covers not only its subject but also matters relating to that subject." She rejected the notion that (a)(2)(B) only refers to overall financial condition, because that interpretation would read "'respecting' out of the statute."

Broadening her opinion further, she said that a statement is "respecting" financial condition "if it has a direct relation to or impact on the debtor's overall financial condition."

A narrower interpretation, according to Justice Sotomayor, "would yield incoherent results." For example, she said that a false statement, such as, "I am above water," could not result in nondischargeability unless it were in writing, while saying, "I have $200,000 in equity in my house" could lead to nondischargeability. "This, too, is inexplicably bizarre," she said.

Justice Sotomayor traced the language in the Bankruptcy Code to a phrase first adopted by Congress in 1926, which the circuits consistently interpreted to include even one of a debtor's assets. Having used the same word in the Bankruptcy Reform Act of 1978, she said that Congress "intended for it to retain its established meaning."

Justices Thomas, Alito and Gorsuch did not join in the last section of Justice Sotomayor's opinion, where she grounded the result in legislative history underpinning Section 523(a)(2)(B). She quoted from a 1995 Supreme Court decision citing the legislative history as saying that Congress drafted Section (a)(2) in a manner intended to prevent abuse by creditors who might otherwise trap debtors into making statements that could result in denial of discharge.

The opinion is *Lamar, Archer & Cofrin, LLP v. Appling*, 16-1215 (Sup. Ct. June 4, 2018).

Possible for Next Term

What did Congress mean in Sections 365(n) and 101(35A)? Is the right to use a trademark terminated when a trademark license is rejected?

'*Cert*' Petition Asks Supreme Court to Overrule *Lubrizol* on Trademark Licenses

Does the rejection of a trademark license mean that the licensee must stop using the trademark?

The circuits are split, but the Supreme Court is being given an opportunity to resolve the question and decide whether the Fourth Circuit was right or wrong in 1985 when it handed down one of most controversial bankruptcy decision of all time, *Lubrizol Enterprises Inc. v. Richmond Metal Finishers Inc.*, 756 F.2d 1043 (4th Cir. 1985).

The licensee of a rejected trademark license filed a petition for *certiorari* in the Supreme Court from the First Circuit's opinion in January in *Mission Product Holdings Inc. v. Tempnology LLC (In re Tempnology LLC)*, 879 F.3d 389 (1st Cir. Jan. 12, 2018). The petition is likely to be considered by the justices at their so-called long conference in late September. We may know as early as September 27 whether the high court will hear the case in the term to begin in October. If *certiorari* is granted, oral argument could take place in December 2018.

The Circuit Split

In *Lubrizol*, the Fourth Circuit held in 1985 that rejecting an executory contract for intellectual property bars the non-bankrupt from continuing to use patents, trademarks and copyrights. Congress responded three years later by adding Section 365(n) and the definition of "intellectual property" in Section 101(35A). Together, they provide that the non-debtor can elect to continue using patents, copyrights and trade secrets despite rejection of a license.

The amendment omitted reference to trademarks. The Senate Report said that the amendment did not mention trademarks because the issue "could not be addressed without more extensive study." In the meantime, Congress said it would "allow the development of equitable treatment of this situation by bankruptcy courts."

As a result of the omission of trademarks from the definition of "intellectual property," the lower courts were split when it comes to deciding whether rejection of a trademark license precludes the licensee from continuing to use the mark. Some courts interpreted Sections 365(n) and 101(35A) as implying a legislative adoption of *Lubrizol* when it comes to trademarks. Other lower courts disagreed.

The Seventh Circuit was the first court of appeals to weigh in when it handed down *Sunbeam Products Inc. v. Chicago American Manufacturing LLC*, 686 F.3d 372 (7th Cir. 2012). The Chicago-based court disagreed with *Lubrizol* and held that "nothing about this process [of rejection] implies that any other rights of the other contracting party have been vaporized." Holding that the right to use the trademark was not terminated by rejection, Circuit Judge Frank Easterbrook noted how *Lubrizol* has been "uniformly criticized" by scholars and commentators.

The split crystalized at the circuit level when the First Circuit handed down *Tempnology* in January. The majority in the 2/1 decision sided with *Lubrizol* and criticized *Sunbeam* for "largely [resting] on the unstated premise that it is possible to free a debtor from any continuing performance obligations under a trademark license even while preserving the licensee's right to use the trademark." The majority favored "the categorical approach of leaving trademark licenses unprotected from court-approved rejection, unless and until Congress should decide otherwise."

The licensee filed a petition for *certiorari* on June 11. Counsel for the petitioner-licensee includes Danielle Spinelli, a former Supreme Court clerk who argued on the winning side in two recent bankruptcy cases, *Czyzewski v. Jevic Holding Corp*., 137 S. Ct. 973 (2017), and *Clark v. Rameker*, 134 S. Ct. 2242 (2014).

The *Tempnology* '*Cert*' Petition

The licensee in *Tempnology* tells the justices in the *certiorari* petition that the First Circuit worsened an existing circuit split on an "openly acknowledged, and longstanding division of authority among the courts of appeals." The petitioner says that the split "is entrenched and will not resolve itself without this Court's intervention."

Arguing that the First Circuit was wrong, the petitioner adopts the approach in *Sunbeam* by contending that rejection of an "executory contract is merely a breach," as provided in Section 365(g). The Boston-based appeals court, it says, confused the power of rejection with the avoidance power.

In addition to *Sunbeam*, the petitioner finds support at the circuit level in the concurring opinion by Third Circuit Judge Thomas L. Ambro in *In re Exide Technologies*, 607 F.3d 957, 964 (3d Cir. 2010). Judge Ambro advocated the same result as the Seventh Circuit on much the same reasoning.

The *Tempnology* petition seeks high court review of a second question: Can the exclusive right to sell a product be terminated by rejection of an executory contract? In other words, is "exclusivity" an intellectual property right that is treated the same for rejection purposes as a trademark and other intellectual property?

Although the petitioner cites scholars in support of its argument that the First Circuit was wrong, there may be no circuit split. Absent a circuit split on exclusivity, the Supreme Court might grant *certiorari* but limit review to the *Lubrizol* issue.

The *certiorari* petition is *Mission Product Holdings Inc. v. Tempnology LLC*, 17-1657 (Sup. Ct.).

Petitioner contends the Second Circuit was wrong to bar arbitration in view of the Supreme Court's decision in Epic Systems.

'*Cert*' Petition Wants Discharge Violations to Be Arbitrated

Can a debtor be forced to arbitrate an alleged violation of the discharge injunction under Section 524?

That is the topic of a petition for *certiorari* filed on June 5, asking the Supreme Court to review *Credit One Bank NA v. Anderson (In re Anderson)*, 884 F.3d 382 (2d Cir. March 7, 2018). Despite an arbitration provision in a pre-bankruptcy agreement with a creditor, the Second Circuit upheld the two lower courts and refused to compel arbitration when the debtor mounted a class action contending that the creditor routinely violated the discharge injunction.

Although there is no circuit split on the arbitrability of an alleged discharge violation, the petitioner in *Anderson* contends that the Second Circuit was wrong in light of recently decided *Epic Systems Corp. v. Lewis*, 200 L. Ed. 2d 889, U.S.L.W. 4297 (Sup. Ct. May 21, 2018), where the Supreme Court compelled employees to arbitrate their wages and hours claims governed by the Fair Labor Standards Act.

Indeed, the petitioner in *Anderson* concedes that the Fourth, Fifth and Ninth Circuits agree with the Second Circuit and allow discretion to disregard an arbitration agreement when the lawsuit raises a "core" bankruptcy claim and arbitration would represent a "severe conflict" with the Bankruptcy Code.

The *Anderson* '*Cert*' Petition

Believing that the Second Circuit was wrong in view of *Epic*, the creditor-petitioner in *Anderson* interprets *Epic* to mean "that another federal statute can render an arbitration agreement unenforceable . . . only if that was Congress's clear and manifest intent." The petitioner in *Anderson* believes that "[n]othing in the Bankruptcy Code evidences a clear and manifest congressional intent to displace the Arbitration Act's command as to claims for violation of the statutory discharge injunction."

The petitioner believes that discharge violations are arbitrable because "[t]here is no indication in either [Section 524 or Section 105] . . . that Congress intended to preclude arbitration of Section 524 claims."

In other words, the petitioner believes that an arbitration clause in a pre-bankruptcy agreement can bar a debtor from resorting to bankruptcy court to enforce or seek redress for a violation of discharge. If that were true, a creditor with an otherwise enforceable arbitration agreement could dun a debtor after bankruptcy, knowing that the debtor could enforce his or her discharge only in arbitration.

If courts were to adopt the petitioner's view, many otherwise "core" proceedings in bankruptcy cases would disappear into arbitration. The standard sought by the petitioner might mean that a creditor could force a debtor to arbitrate a claim objection, an objection to the dischargeability of a debt, or even a fraudulent transfer or preference claim.

Possible Disposition of the *Anderson* Petition

Conceding there is no circuit split on the non-arbitrability of "core" claims involving a fundamental bankruptcy right, the petitioner wants the Supreme Court to put the appeals courts on the right track because "the lower courts have been flummoxed by the Bankruptcy Code, which [the Supreme Court] has never addressed for these purposes."

The petitioner well may be correct that *Anderson* cannot be squared with *Epic*, a 5/4 decision. However, the Supreme Court is not a court of error. Along with alleged violations of the U.S. Constitution, most Supreme Court cases resolve circuit splits.

Since there is no circuit split underlying *Anderson*, the petitioner forthrightly asks the Supreme Court, in the alternative, to "grant [the *certiorari* petition], vacate, and remand [to the Second Circuit] in light of its intervening decision in *Epic Systems*." A GVR, as it is called, seems more likely than a straight-up grant of *certiorari*.

The debtor-plaintiff in *Anderson* already waived its right to file a response to the petition for *certiorari*. Like *Tempnology*, the justices are likely to consider the *Anderson* petition and issue a disposition as early as September 27.

Subsequent to *Anderson* but the same day as *Epic*, a bankruptcy court in Florida reached the same result as the Second Circuit. To read ABI's discussion of *In re Bateman*, 14-5369, 2018 BL 181355 (Bankr. M.D. Fla. May 21, 2018), click here.

To read ABI's discussion of the Second Circuit decision in *Anderson*, click here. To read the Anderson *certiorari* petition, click here.

The petition is *Credit One Bank NA v. Anderson*, 17-1652 (Sup. Ct.).

Reorganization

Dismissal

The appeals court avoids ruling broadly on the ability of a golden share or blocking provision to bar a company from filing bankruptcy voluntarily.

Fifth Circuit Issues a Narrow Opinion Requiring Corporate Authority to File a Petition

On direct appeal from a bankruptcy court in Mississippi, the Fifth Circuit was being asked to hand down a blockbuster opinion saying whether a creditor or shareholder could use a so-called golden share or blocking provision to preclude a company from filing bankruptcy.

An opinion directly answering the certified questions would have allowed the New Orleans-based appeals court to adopt, reject or significantly expand the idea that no one can contract away the ability to file bankruptcy or the right to a discharge.

To avoid issuing an advisory opinion, Circuit Judge Carolyn Dineen King instead answered a narrow question closely tailored to the facts. Based on Supreme Court authority from 1945, Judge King held in her May 22 opinion for the Fifth Circuit that a bankruptcy court must dismiss a bankruptcy petition if the filing was not authorized in accordance with the corporate charter.

Judge King took pains to ensure that her opinion would not be interpreted too broadly. She said, for instance, that the result might be different if the ability to block bankruptcy were held by a creditor "with no stake in the company" or if a creditor took an equity interest as a "ruse" to guarantee payment of a debt.

The Bankruptcy Court Opinion

The debtor owned a car rental company. To finance an acquisition, the debtor received a $15 million investment from a diversified financial group. In return, the investor was given 100% of the debtor's preferred equity convertible into 49.76% of the equity. The preferred shareholder was the single largest investor in the company.

An investment bank helped arrange the acquisition. The bank was an affiliate of the preferred shareholder. The investment bank had a $3 million unpaid claim for its services. In his opinion in December, Bankruptcy Judge Edward Ellington of Jackson, Miss., said that the preferred shareholder controlled the affiliated investment bank creditor.

As part of the transaction, the debtor reincorporated in Delaware and provided in the certificate of incorporation that a majority of all classes of equity, voting separately, must approve a "liquidation event" such as bankruptcy.

Without holding a vote of common and preferred shareholders, the company filed a chapter 11 petition. The preferred shareholder responded by filing a motion to dismiss for lack of proper corporate authorization. In opposition, the debtor argued that the creditor, acting through its controlled affiliate, the preferred shareholder, could not bar a bankruptcy filing and thus realize a result it could not achieve directly.

Judge Ellison granted the dismissal motion, holding that the preferred shareholder had the "unquestioned right" to block a voluntary bankruptcy, even though it was controlled by the creditor with the $3 million disputed claim.

In January, Judge Ellison certified three questions for direct appeal to the Fifth Circuit: (1) Is a blocking provision or golden share, held by either a creditor or equity holder, invalid as a violation of public policy if it prevents a corporation from filing bankruptcy; (2) if the holder is both a creditor and shareholder, is barring bankruptcy invalid as a violation of public policy; and (3) under Delaware law, may a certificate of incorporation contain a blocking provision or golden share, and if permissible, does Delaware law impose fiduciary duties on the holder in exercising its power?

On February 8, the appeals court granted the petition and expedited the appeal. Oral argument took place on May 2.

To read ABI's report on the bankruptcy court's decision and the certified question, click here.

Judge King's Cautious, Narrow Opinion

Addressing the concepts of golden shares and blocking provisions, Judge King said they are not identical. A blocking provision could be one of several contractual provisions a creditor might use to prevent a debtor from filing bankruptcy. In the bankruptcy context, she said that a golden share is stock that gives a creditor the right to prevent a voluntary bankruptcy.

The case on appeal did not fit within either definition, Judge King said. In any event, opining on the legality of blocking provisions or golden shares would amount to issuing an advisory opinion, which she was unwilling to do.

Instead, Judge King narrowed the question to decide whether the parties could "amend a corporate charter to allow a non-fiduciary shareholder fully controlled by an unsecured creditor to prevent a voluntary bankruptcy petition."

Judge King said that the Bankruptcy Code does not specify who has the right to file a petition for a corporation. In substance, she based her decision on *Price v. Gurney*, 324 U.S. 100, 106 (1945), where the Supreme Court held that state law determines who has authority to file a voluntary petition for a corporation.

Judge King found "no reason to depart from that general rule in this case." She also found no statute or "binding caselaw" that would allow the court "to ignore corporate foundational documents, deprive a *bona fide* shareholder of its voting rights, and reallocate corporate authority to file for bankruptcy just because the shareholder also happens to be an unsecured creditor."

Cases relied upon by the debtor were "not controlling and not to the contrary," Judge King said. They involved "creditors' attempts to appoint non-fiduciary officers and directors with the ability to prevent a bankruptcy filing."

Exploring the facts, Judge King said she *found no evidence* that the requirement for shareholder approval "was merely a ruse" to ensure that the debtor would pay the investment bank's $3 million claim, *even if the banker and the preferred shareholder were treated as a single entity.* In other words, Judge King's holding might not apply in another case where the corporate charter was being used to ensure payment of a debt.

On the other hand, the opinion also means that a creditor and shareholder theoretically can be one entity without disabling the right to vote as a shareholder.

Stressing the limited nature of the holding, Judge King said that the case entailed a *bona fide* shareholder and "goes no further." She said the case did not involve a creditor who "somehow contracted for the right to prevent a bankruptcy or where the equity interest is just a ruse."

Having determined that nothing in federal bankruptcy law precluded enforcement of the corporate charter under the facts of the case, Judge King then analyzed whether the charter was enforceable under Delaware law.

Judge King found no Delaware cases saying whether shareholders could be given the right to decide for or against filing bankruptcy. Fortunately, the debtor abandoned the argument on appeal, so she was not called on to make a so-called *Erie* guess. Therefore, Judge King assumed that Delaware law would allow such a provision.

Next, Judge King examined whether the preferred shareholder violated fiduciary duties. In the first place, the record did not establish that the preferred shareholder was a controlling shareholder and therefore did not have fiduciary duties under Delaware law.

Even if the shareholder were controlling and therefore did have fiduciary duties, Judge King found "a more fundamental defect" in the debtor's argument: The proper remedy for violation of

fiduciary duties would “not allow a corporation to disregard its charter and declare bankruptcy without shareholder consent.”

Even if the shareholder had violated fiduciary duties, “the proper remedy is not to deny an otherwise meritorious motion to dismiss the bankruptcy petition.”

“Instead,” Judge King said, the debtor “must seek its remedy under state law” if the shareholder has “breached a fiduciary duty.”

Judge King’s opinion does not indicate whether a bankruptcy court through some procedural construct would have jurisdiction to determine whether a shareholder had violated a fiduciary duty and thus enable a company to file bankruptcy voluntarily without corporate authorization. For example, it is not clear one way or another whether a company could file a petition and answer a motion to dismiss by contending that the shareholder was violating fiduciary duties.

The opinion is *Franchise Services of North America Inc. v. U.S. Trustee (In re Franchise Services of North America Inc.)*, 18-60093 (5th Cir. May 22, 2018).

Executory Contracts & Leases

***First Circuit follows the Fourth Circuit's* Lubrizol *and rejects the Seventh Circuit's* Sunbeam.**

Circuit Split Deepens on Rejection of Trademark Licenses

Pointedly disagreeing with the Seventh Circuit, the First Circuit deepened an existing split by adopting the Fourth Circuit's conclusion in *Lubrizol* and holding that rejection of a trademark license agreement precludes the licensee from continuing to use the license.

The 2/1 opinion from the First Circuit on Jan. 12 reversed the Bankruptcy Appellate Panel, which, to the contrary, had followed Circuit Judge Frank Easterbrook's decision in *Sunbeam Products Inc. v. Chicago American Manufacturing LLC*, 686 F.3d 372 (7th Cir. 2012). In *Sunbeam,* the Seventh Circuit rejected the Fourth Circuit's rationale in *Lubrizol Enterprises Inc. v. Richmond Metal Finishers Inc.*, 756 F.2d 1043 (4th Cir. 1985).

In simple terms, the First Circuit's decision means that the licensee of patents can continue using the technology after rejection as a consequence of Section 363(n), but the same licensee cannot continue using trademark licenses that went along with the technology.

The Genesis of Section 365(n)

In *Lubrizol*, the Fourth Circuit ruled in 1985 that rejection of an executory contract licensing intellectual property halted the non-bankrupt's right to use patents, trademarks and copyrights. Three years later, Congress responded by adding Section 365(n), which, in conjunction with the definition of "intellectual property" in Section 101(35A), provides that the non-debtor can elect to continue using patents, copyrights and trade secrets despite rejection of a license.

The amendment conspicuously omitted reference to trademarks. The Senate Report said that the amendment did not deal with trademarks because the issue "could not be addressed without more extensive study." According to the report, Congress decided to postpone action "to allow the development of equitable treatment of this situation by bankruptcy courts."

Since then, courts have split into two camps. One group takes a negative inference from the omission of trademarks from Section 365(n) by holding that rejection terminates the right to use a trademark, although the licensee could elect to continue using patents covered by the same agreement.

In *Sunbeam*, the Seventh Circuit split with the Fourth in 2012. Judge Easterbrook acknowledged that Section 365(n) does not preserve the right to use trademarks, but at the same

time does not prescribe the consequences of rejection. Judge Easterbrook instead relied on Section 365(g), which teaches that rejection "constitutes a breach" of contract.

Judge Easterbrook reasoned that a licensor's breach outside of bankruptcy would not preclude the licensee from continuing to use a trademark. He ruled that rejection converted the debtor's unfulfilled obligations into damages. He said that "nothing about this process implies than any other rights of the other contracting party have been vaporized." He added that *Lubrizol* has been "uniformly criticized" by scholars and commentators.

The First Circuit Case

Before bankruptcy, the debtor in the case before the First Circuit had granted the licensee a non-exclusive, irrevocable, fully paid, transferrable license to its intellectual property including patents. However, the irrevocable license excluded the debtor's trademarks.

Separately, the license agreement granted a non-exclusive, non-transferable, limited license to use the debtor's trademarks.

The day after filing a chapter 11 petition, the debtor filed a motion to reject the trademark and patent licenses as executory contracts under Section 365(a). During the ensuing litigation, the debtor conceded that Section 365(n) allowed the licensee to retain its rights in the intellectual property and patents, but not the trademarks.

Ultimately, the bankruptcy court ruled that Section 365(n) did not preserve the licensee's rights in the trademarks. The bankruptcy judge believed that the omission of trademarks from the definition of intellectual property in Section 101(35A) meant that Section 365(n) does not protect rights in trademarks.

On the first appeal, the BAP followed *Sunbeam* and reversed the bankruptcy court, calling *Lubrizol* "draconian" and saying that rejection does not "vaporize" trademark rights. To read ABI's report on the BAP opinion, click here.

With regard to trademarks, Circuit Judge William J. Kayatta, Jr. reversed the BAP in a 2/1 opinion, holding that the right to use trademarks did not survive rejection.

Judge Kayatta said that *Sunbeam* "largely rests on the unstated premise that it is possible to free a debtor from any continuing performance obligations under a trademark license even while preserving the licensee's right to use the trademark." That premise, he said, is wrong because "effective licensing of a trademark" requires the licensor to continue monitoring and exercising control over the quality of the goods sold under the mark.

Sunbeam is wrong, in Judge Kayatta's view, because it "entirely ignores the residual enforcement burden it would impose on the debtor just as the Code otherwise allows the debtor to free itself from executory burdens" and "invites further degradation of the debtor's fresh start options."

Judge Kayatta therefore favored "the categorical approach of leaving trademark licenses unprotected from court-approved rejection, unless and until Congress should decide otherwise."

The Dissent

Circuit Judge Juan R. Torruella dissented with regard to trademarks. Like *Sunbeam*, he would have held that rights in a trademark "did not vaporize" as a result of rejection.

Judge Torruella based his dissent in large part on the legislative history surrounding the adoption of Sections 363(n) and 101(35A). He saw Congress as allowing courts to use their equitable powers to protect trademark licensees.

Rather than eviscerating the licensee's trademark rights, Judge Torruella said he instead would "be guided by the terms of the [license agreement], and non-bankruptcy law, to determine the appropriate equitable remedy of the functional breach of contract."

Distribution Rights

The litigation in bankruptcy court also involved the debtor's license of distribution rights. Affirmed by the BAP, the bankruptcy court had ruled that rejection cut off distribution rights too.

On appeal in the circuit, the licensee mounted several creative arguments aimed at showing that distribution rights were an adjunct to the patents and technology and therefore should survive.

Judges Kayatta and Torruella agreed that rejection cut off distribution rights.

The Next Steps

If the licensee does not throw in the towel, the next step will be a petition for rehearing *en banc* or a petition for *certiorari*. The circuit split pits not only the First Circuit against the Seventh. In his concurrence in *In re Exide Technologies*, 607 F.3d 957, 964 (3d Cir. 2010), Third Circuit Judge Thomas L. Ambro reached the same result as the Seventh Circuit on much the same reasoning.

The opinion is *Mission Product Holdings Inc. v. Old Cold LLC (In re Old Cold LLC)*, 879 F.3d 376 (1st Cir. Jan. 12, 2018).

Do free and clear sales confer interests that are entitled to adequate protection?

Seventh Circuit Opens a Can of Worms on Bankruptcy Sales and Adequate Protection

In a highly theoretical opinion, the Seventh Circuit said that an out-of-the-money creditor in a free and clear bankruptcy sale *might* be entitled to some sale proceeds, thus reducing the recovery by the senior lender even if the lender is not being paid in full.

How's that possible? The Chicago-based appeals court *theorized* that the ability to sell free and clear *might* create an interest in property for which a subordinate creditor *could* be entitled to an adequate protection payment.

Before you panic and conclude that everything you know about bankruptcy sales is about to change, keep in mind that the Seventh Circuit based its July 9 opinion on an assumption that may prove to be wrong when the question arises again.

The Underwater Sales

The circuit court decided two consolidated appeals, both involving an Illinois bulk sale law designed to aid the state in collecting taxes. If state taxes are not paid, the bulk purchaser of a business becomes liable for the taxes under state law.

In parallel bankruptcies, the debtors owed $1.4 million and $600,000, respectively, in state taxes. In sales free and clear of liens and claims under Section 363(f), the properties fetched $5.2 million and $2 million, respectively. However, banks held first liens on the properties for $14 million and $4 million, respectively.

In other words, the first lien lenders would recover only a fraction of their secured claims even if they received all sale proceeds.

The state opposed distribution of the sale proceeds to the senior lenders, contending the state was entitled to be paid in full because the bulk sale law permits collection of the tax debts from purchasers. More cogently, the state argued that its successor liability claims under the bulk sale law amounted to an "interest" in property that was entitled to adequate protection under Section 363(e).

Because the senior lenders were underwater, the bankruptcy judges in Chicago both ruled that the state was entitled to no recovery from the sales.

On appeal, two different district judges remanded for the bankruptcy judges to develop the record by making two findings: (1) what the state would have recovered if the property had not been sold free and clear, and (2) how the state could be compensated for its "interest" given that the lenders had senior liens.

On remand, both bankruptcy judges again denied the state any recovery, ruling that the state's realizable interest was effectively zero. The appeals court allowed direct appeals on both cases.

The Circuit Opinion, Based on an Assumption

Circuit Judge Ilana K. Rovner authored a 29-page opinion upholding the results in the bankruptcy courts, albeit on different grounds that some in the bankruptcy community may find unsettling.

Judge Rovner explained that the Illinois bulk sale law does not affect lien priorities. Indeed, the law does not apply in foreclosure, where the state cannot assert a successor liability claim against a purchaser.

In bankruptcy, however, the state contends that the ability to hold purchasers personally liable has "real value" that is entitled to adequate protection. More specifically, the state claims that a purchaser will pay a higher price because a bankruptcy sale relieves the purchaser of liability for state taxes. Developing the theory further, the state postulates that the purchaser would pay more to avoid the expense and loss of value to the business that would result from foreclosure, where the tax liability would disappear.

Judge Rovner therefore framed the question as whether the state was entitled to adequate protection when the properties were sold free and clear in bankruptcy court.

Significantly, Judge Rovner's entire opinion rests on a critical assumption. Without deciding, she assumed that the state's ability to impose successor liability was an "interest" in the debtor's property that would invoke the concept of adequate protection under Sections 363(e) and 361(1). She made the assumption because the bankruptcy courts had made the same assumption, and the issue was litigated or decided below.

Judge Rovner's own opinion contains language undercutting the assumption. She said that a buyer's inclination to pay a premium for a sale free and clear "is attributable to [the state law] rather than any asset of the estate." If that is true, a sale free and clear would be cutting off a state law right against a purchaser, not an interest in estate property deserving of adequate protection.

Judge Rovner said she was “dubious of the notion” that the state could have recovered all outstanding taxes. She also recognized that allowing the state to recover even a portion of the taxes “would, in a real sense, permit [the state] to jump the queue of creditors and grant [the state] monetary protection for its interest at the expense of other creditors.”

Judge Rovner therefore analyzed several hypotheticals to decide what the state “realistically could have recovered from the purchaser.” Even if a purchaser might pay more, the bank, she said, “surely would not be indifferent” if the state were to receive some of the proceeds when the secured lender was not being paid in full. The lender could foreclose, she said, to cut off the tax claims.

Nevertheless, “foreclosure comes with significant costs and can ultimately reduce the net recovery of a bank,” Judge Rovner said.

In a settlement to avoid foreclosure, a bank might accept somewhat less if the state were to take less than full payment. Judge Rovner said that compromises between the bank and the state “are more than an abstract possibility.” On the other hand, she quoted one of the district judges who said that an interest otherwise entitled to adequate protection “may be worth nothing, in practical terms, in which case the interest holder is entitled to no compensation pursuant to Section[s] 363(e) and 361(1).”

Focusing adequate protection “is where the wheels come off the wagon of [the state’s] argument,” Judge Rovner said, because “Section 361(1) directs us to consider how much the value of [the state’s] interest decreased as a result of the bankruptcy court’s free and clear orders.” In that regard, she said, “we are still faced with the problem of valuation.”

Regardless of whether the trustee or the state bore the burden of proof, she said there was “no evidence as to what [the state] likely would have collected from the purchaser but for the bankruptcy court’s Section 363(f) free-and-clear order.” In the absence of evidence about how much the state’s interest was diminished, Judge Rovner held that the “bankruptcy courts therefore did not err in valuing [the state’s] interest at zero for purposes of its right to adequate protection.”

What Does the Opinion Mean?

Judge Rovner’s opinion has set the stage for the next case where the state and the trustee will present expert witnesses about the incremental value in a bankruptcy sale as opposed to foreclosure.

It has always been this writer’s belief that a bankruptcy sale is more valuable than foreclosure for several reasons. Nonetheless, would the state be entitled to the incremental value, rather than the lender who is not being paid in full?

A lender's ability to liquidate collateral in bankruptcy court could be viewed as a right held by a secured creditor, not value inherent in the collateral itself to which adequate protection rights might attach. Likewise, the bulk sale laws could be seen as creating only a claim against a purchaser, not an interest in the bankrupt seller's property warranting adequate protection.

In a different context, the Ninth Circuit said in *Pinnacle Restaurant at Big Sky LLC v. CH SP Acquisitions LLC (In re Spanish Peaks Holdings II LLC)*, 862 F.3d 1148 (9th Cir. July 13, 2017), that a bankruptcy sale can be the rough equivalent of mortgage foreclosure, in which case the state's tax claims would be extinguished altogether. To read ABI's discussion of *Spanish Peaks*, click here.

In any event, courts in the Seventh Circuit are now taxed with deciding whether the Illinois bulk sale law creates an interest in property entitled to adequate protection. It is by no means clear, however, that the outcome will affect only Illinois.

Most states have laws that confer rights on creditors to pursue claims against purchasers who do not follow procedures required by bulk sale laws. It is also not evident why the issue is confined to bulk sale laws, because subordinate secured creditors could argue that sales free and clear of their liens enhance the purchase price.

The opinion is *Illinois Department of Revenue v. Hanmi Bank*, 17-1575 (7th Cir. July 9, 2018).

For swaps, the Section 560 safe harbor overrides the anti-*ipso facto** *provisions in the Bankruptcy Code.

Flip Clauses in Swaps Held Enforceable by District Judge in New York

In a broadly worded opinion, District Judge Lorna G. Schonfield of Manhattan ruled that a so-called flip clause in a swap agreement is enforceable under the exception to the automatic stay in Section 560 of the Bankruptcy Code.

Judge Schonfield affirmed a June 2016 opinion by Bankruptcy Judge Shelley C. Chapman and in the process disagreed with former Bankruptcy Judge James M. Peck, who had held in a pair of opinions in 2010 and 2011 that a flip clause is an *ipso facto* clause that is not enforceable under Sections 365(e)(1), 541(c)(1)(B) and 363(l) of the Bankruptcy Code.

The Lehman Flip Clauses

Lehman Brothers Holdings Inc. and its subsidiaries had thousands of swaps in their portfolios when they began filing for chapter 11 protection in September 2008. Some included so-called flip clauses that came into play when Lehman was "in the money" at the outset of bankruptcy and stood to recover from termination of the swaps.

Briefly stated, the flip clauses provided that collateral securing the swaps ordinarily would go first to Lehman subsidiary Lehman Brothers Special Financing Inc. (known as LBSF) as the swap counterparty in an ordinary maturity or termination.

If the Lehman parent or LBSF were to file bankruptcy and thus cause an event of default, the swap counterparty could terminate the swap prematurely. If the Lehman parent or LBSF were the defaulting party, the flip clause would kick in and direct the collateral proceeds first to noteholders, not to LBSF. Since the noteholders were never paid in full, LBSF got nothing when the flip clauses were invoked, even though LBSF would have been in the money were there are an ordinary maturity.

In 2010, Lehman sued 250 defendants in bankruptcy court, contending that the flip clauses violated the anti-*ipso facto* provisions in Sections 365(e)(1), 541(c)(1)(B) and 363(l) of the Bankruptcy Code. Lehman contended that flip clauses were invalid because those subsections provide that contractual provisions are unenforceable if they become effective on insolvency or bankruptcy.

In different adversary proceedings involving different counterparties, Judge Peck wrote decisions in 2010 and 2011 where he agreed with Lehman and concluded that flip clauses violated the anti-*ipso facto* statutes. He also decided that Section 560 did not apply. Neither of those decisions went up on appeal.

When Judge Peck left the bench, Judge Chapman took over the Lehman bankruptcy, including litigation over the flip clauses. The defendants filed motions to dismiss. Judge Chapman granted the motions in her opinion in June 2016, prompting Lehman to appeal. To read ABI's discussion of Judge Chapman's opinion, click here.

Judge Schonfield's Opinion

In her 16-page opinion on March 14, Judge Schonfield did not keep the reader in suspense. After laying out the facts and Judge Chapman's decision, she went to the heart of the case and said that flip clauses "do not violate the Bankruptcy Code" because they are protected by the safe harbor in Section 560.

Section 560 provides that "any contractual right of a swap participant . . . to cause the liquidation, termination or acceleration [of a swap agreement] shall not be stayed, avoided, or otherwise limited by operation of any provision" in the Bankruptcy Code. Citing legislative history, Judge Schonfield said that the "purpose of Section 560 is to protect securities markets."

The purpose of Section 560 in mind, Judge Schonfield said that "the most sensible literal reading of Section 560 applies to the distributions in this case." Enforcing a flip clause, she said, is the "'exercise of [a] contractual right . . . to cause the liquidation [or] termination'" of a swap.

Judge Schonfield rejected Lehman's argument that "liquidation" as used in Section 560 only refers to the calculation of amounts owed, not to the actual distribution of funds.

Because the safe harbors in the Bankruptcy Code must be "interpreted based on their plain meaning," Judge Schonfield said that Lehman's argument was "nonsensical because it would nullify any protection Section 560 provides to swap agreements." The "mere calculation" of a swap, she said, would provide "no security to swap participants."

Next, Lehman contended that the trustees who held the collateral were the only parties entitled to enforce the flip clauses. Since the trustees were not swap participants, according to Lehman, their actions were not protected by the Section 560 safe harbor.

Although she found no authority on the topic, Judge Schonfield said that Lehman's "argument is incorrect and contrary to the plain language of the statute." Section 560, she said, "only requires the exercise 'of' a swap participant's contractual right, but that right need not be exercised 'by'

the swap participant." Therefore, when the trustees terminated the swaps, she said "they exercised the rights 'of'" the swap participants.

Lehman also made claims under state law for unjust enrichment, constructive trust, money had and received, replevin and breach of contract. Those claims were properly dismissed, Judge Schonfield said, because the distributions were not improper given that the flip clauses "were not unenforceable *ipso facto* clauses."

Judge Schonfield also upheld dismissal of Lehman's fraudulent transfer claims based on the notion that the swap participants did not give fair consideration. Since the payments "indisputably" were repayments of a debt owning to the swap participants, they gave fair consideration, thus barring any fraudulent transfer claims.

Judge Schonfield specifically declined to follow Judge Peck's decisions from 2010 and 2011, saying that they were not binding authority.

The opinion is *Lehman Brothers Special Financing Inc. v. Bank of America NA (In re Lehman Brothers Holdings Inc.)*, 17-1224 (S.D.N.Y. March 14, 2018).

Sales

Section 363(m) allows an appeal if the remedy won't upset the sale itself, Third Circuit says.

Third Circuit Explains When Sale Orders Are Not Automatically Moot

On an issue under Section 363(m) where the circuits are split, the Third Circuit is in the minority, aligned with the Sixth and Tenth Circuits by holding that an appeal from an order approving a sale to a good faith purchaser is not automatically moot.

In an opinion on Oct. 24, the Third Circuit fleshed out the circumstance in which an appeal will not be moot, even though the bankruptcy court approved the lease or sale of property and there was no stay pending appeal.

The sale was contentious and factually complex, but for the purpose of analysis, the circumstances were not unusual. A chapter 7 trustee was selling the estate's claims against insiders. The first bid of $125,000 came from a group of creditors. In addition to paying the purchase price, they agreed to contribute proceeds from lawsuits to the estate for distribution to all creditors.

After the insiders submitted a competing bid, the bankruptcy court authorized the trustee to hold an auction. The creditors submitted a bid of $180,000 and won the auction. In conjunction with their opposition to approval of the sale to the insiders, the insiders offered as much as $220,000.

The bankruptcy court approved the sale to the creditors for $180,000, theorizing that the creditors' offer was higher because they would contribute recoveries to the estate and because the insiders had not complied with auction rules.

On appeal, the district court dismissed the insiders' appeal as moot under Section 363(m). That section provides that reversal or modification of an order approving a sale or lease "does not affect the validity" of the sale or lease "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."

Circuit Judge Kent A. Jordan synthesized the Third Circuit's precedent on Section 363(m) in a 37-page opinion upholding the lower courts and declaring that the appeal was moot. He explained that the section is designed to promote finality of sales and thereby attract investors and "effectuate debtor rehabilitation." If the section "is to have teeth," Judge Jordan said, "any reasonably close question" should be resolved in favor of finding the appeal to be moot.

Previously, the Third Circuit had held that an appeal will be moot if three conditions are met: (1) There was no stay pending appeal, (2) reversal would affect the validity of the sale, and (3) the sale was to a good faith purchaser.

Judge Jordan found "no clear error" in the bankruptcy court's findings that the parties were in good faith because there was no collusion; the creditors followed the auction rules; and there was no evidence to "suggest that the bidding took place at less than arm's length."

Having found that the sale was conducted in good faith, Judge Jordan then addressed the other two issues, first confirming there was no stay pending appeal. Before dismissing the appeal as moot, the pivotal issue became the ability of the appellate court to modify or reverse without affecting the validity of the sale.

Judge Jordan said that appellate rights are preserved "only in those rare circumstances where collateral issues not implicating a central or integral element of a sale are challenged."

The insiders argued that they were not challenging the validity of the sale, only the ability of the creditors to pursue claims of the estate. Agreeing with the trustee's contention, Judge Jordan said it would have made no sense for the creditors to purchase the estate's claims if they could not pursue them.

Judge Jordan therefore dismissed the appeal as moot, because the circuit court could not give the creditors a remedy "without affecting the validity of the sale."

Of significance, the ability of the creditors to prosecute the estate's claims was not resolved either in the sale order or by dismissal of the appeal, because the sale did not obviate any of the insiders' defenses. Back in bankruptcy court, the insiders were moving to dismiss the creditors' suit against them on the theory that the creditors were not entitled to prosecute estate claims. The bankruptcy court held the dismissal motion in abeyance pending the outcome of the appeal.

For ABI's discussion of a recent Sixth Circuit opinion widening the split on Section 363(m), click here.

The opinion is *Schepis v. Burtch (In re Pursuit Capital Management LLC)*, 874 F.3d 124 (3d Cir. Oct. 24, 2017).

Estate Property

Jewel has now been formally rejected in New York and California. Washington, D.C., is next.

California Supreme Court Kills the *Jewel* Doctrine on a Certified Question

The handwriting was on the wall, but now it's official in California, and probably everywhere else: Profits earned on unfinished hourly business after a law firm dissolves are *not* property of the "old" firm and can be retained by the new firm that completes the work.

Answering a certified question from the Ninth Circuit, the California Supreme Court held on March 5 that "a dissolved law firm's property interest in hourly fee matters is limited to the right to be paid for the work it performs before dissolution." A "narrow" exception allows the old firm to collect for work performed before dissolution and to be paid for preserving and transferring hourly fee matters to new counsel of the client's choice.

The state's high court did not rest its conclusion on a tortured analysis of the Revised Uniform Partnership Law or impressive-sounding legal mumbo jumbo. Instead, the state Supreme Court relied on logical conclusions based on common experience and longstanding principles. For instance, the court said that the dissolved firm cannot claim "a legitimate interest in the hourly matters on which it is *not* working — and on which it cannot work." [Emphasis in original.]

The result emanated principally from two value judgments: The law should not intrude "without justification on clients' choice of counsel" nor limit "lawyers' mobility postdissolution."

The Heller Ehrman Liquidation

A firm that once had 700 lawyers, Heller Ehrman LLP was liquidated in chapter 11. The confirmed plan created a trust that sued 16 firms for income that lawyers from the liquidated firm earned at their new firms in completing hourly matters originated at Heller Ehrman. All but four firms settled. The bankruptcy court granted summary judgment in favor of the trustee and against the four firms.

The bankruptcy court based its decision on *Jewel v. Boxer*, a 1984 decision by an intermediate California appellate court, which said that profits earned on unfinished business belong to the "old" firm. The *Jewel* court allowed the new firm to recover only its overhead and rejected arguments based on clients' rights to select attorneys of their choice. *Jewel* had been followed in one other California appellate decision, but the issue had not previously reached the state's highest court.

Jewel was attractive for trustees in law firm bankruptcies because asserting the principle brought in settlements generating assets that otherwise would be few and far between.

After the Heller Ehrman bankruptcy court ruled in favor of the trustee, District Judge Charles R. Breyer of San Francisco withdrew the reference. Reviewing the bankruptcy court's rulings *de novo*, he granted summary judgment for the law firms. The trustee appealed.

After hearing oral argument in June 2016, the Ninth Circuit issued an order the next month certifying the question to the California Supreme Court. The Ninth Circuit pointed out that California's highest court has never directly addressed the *Jewel* issue. The appeals court also alluded to *Jewel* litigation in New York.

On a certified question from the Second Circuit, the New York Court of Appeals held in July 2014 that *Jewel* is not the law in New York. The New York court ruled that there is no property interest in hourly unfinished business because it is "too contingent in nature and speculative to create a present or future property interest." The New York decision stemmed from the bankruptcies of Coudert Brothers LP and Thelen LLP.

In addition to citing the New York decision, the Ninth Circuit pointed out that California revised its partnership law in 1996, 12 years after *Jewel*.

Judge Breyer was not the only district judge to undermine *Jewel*. Granting an interlocutory appeal, District Judge James J. Donato of San Francisco reversed the bankruptcy court and held in favor of lawyers who went to new firms. He ruled that they could retain what they bill at their new firms.

Judge Donato issued his decision in the liquidation of Howrey LLP. On appeal, the Ninth Circuit certified the question to the District of Columbia Court of Appeals in February because the case turns on D.C. law, not California law.

The California Court's Analysis

The certified question was argued in the state's high court in December 2017. The March 5 opinion by Justice Mariano-Florentino Cuéllar went to the heart of the issue immediately. He said that a dissolved law firm has "no property interest in legal matters handled on an hourly basis, and therefore, no property interest in the profits generated by its former partners' work on hourly fee matters pending at the time of the firm's dissolution."

There is no property interest, he said, because the old firm "has no more than an expectation" that "may be dashed at any time by a client's choice to remove its business." He explained that the "mere possibility of unearned, prospective fees . . . cannot constitute a property interest."

Rather than tease the result from the Revised Uniform Partnership Act, or RUPA, Justice Cuéllar based the decision on a "sensible interpretation" of state law and "practical implications" to conclude that "the dissolved firm's property interest here is quite narrow."

Policy implications were paramount. The outcome should "protect the client's choice of counsel" and comport "with our policy of encouraging labor mobility while minimizing firm instability." He said that neither previous cases nor "specific statutory provisions . . . resolve the question before us."

In the law firm context, a property interest is grounded on a "sufficiently strong expectation." That expectation "requires a legitimate, objectively reasonable assurance rather than a mere unilaterally-held presumption."

The old firm, Justice Cuéllar said, claims an "interest in the hourly matters on which it is *not* working — and on which it cannot work" and "seeks remuneration for work that someone else must undertake." [Emphasis in original.] Given that neither clients nor lawyers would share that view, he said that the old firm's "expectation is best understood as essentially unilateral." He went on to add that the old firm's "hopes were speculative, given the client's right to terminate counsel at any time, with or without cause. As such, they do not amount to a property interest."

Again focusing on policy considerations, Judge Cuéllar recognized that former partners in a dissolved firm "may face limited mobility in bringing unfinished business to replacement firms." Similarly, recognizing a property interest in unfinished business "would also risk impinging on the client's right to discharge an attorney at will." He therefore affirmed the principle "that client matters belong to the clients, not the law firms."

Judge Cuéllar said that the principle in *Jewel* was unnecessary to prevent lawyers from jumping ship prematurely because the California Supreme Court had upheld the enforceability of a law partnership's noncompetition agreement.

Rather than basing the conclusion on RUPA, Judge Cuéllar said that "[n]othing else in RUPA cuts against our holding."

Judge Cuéllar pointedly declined to say whether overruling *Jewel* with regard to hourly matters would also apply to contingencies.

The opinion is *Heller Ehrman LLP v. Davis Wright Tremaine LLP*, S236208 (Cal. Sup. Ct. March 5, 2018).

Jurisdiction & Power

Filing bankruptcy won't divest a district court of maritime jurisdiction, and a bankruptcy court can't adjudicate maritime lien rights.

Automatic Stay Doesn't Apply to Enforcement of Maritime Liens, Ninth Circuit Says

A bankruptcy filing cannot divest a district court of preexisting maritime jurisdiction over a vessel; the automatic bankruptcy stay does not apply to maritime lien rights, and the bankruptcy court does not have jurisdiction to adjudicate maritime liens, the Ninth Circuit said in a lengthy opinion by Circuit Judge Jacqueline H. Nguyen.

A vessel exploded, injuring a seaman who was unable to work as a result of his injuries. The seaman filed a verified complaint in admiralty in district court against the vessel, the corporation that owned the vessel and the individual who owned the corporation.

In her March 28 opinion for the three-judge panel, Judge Nguyen said the defendants never objected to admiralty jurisdiction, giving the district court *in rem* jurisdiction over the vessel. The seaman was seeking "maintenance and cure," maritime terms for an injured seaman's food, lodging and medical care while unable to work. None of the defendants had insurance to cover the seaman's maintenance and cure.

Fifteen months into the maritime suit, on the eve of trial to determine the amount of maintenance and cure, the individual defendant and the corporate owner of the vessel filed chapter 13 and 7 petitions, respectively. The district court stayed the maritime suit altogether, citing the Section 362 automatic stay.

Later, the bankruptcy court partially modified the automatic stay to allow the district court to determine the extent and validity of the seaman's maritime lien against the vessel but specifically barred enforcement of the lien.

Sua sponte, the district judge then dismissed the maritime suit, believing the court lost maritime jurisdiction because the seaman had not verified an amended complaint. Next, the bankruptcy court approved a sale of the vessel "free and clear." The seaman appealed dismissal of the maritime suit and the loss of his maritime lien rights.

Judge Nguyen reversed in 44-page opinion, making significant pronouncements about the intersection of bankruptcy and maritime jurisdiction.

Important for maritime law but not so much with regard to bankruptcy law, Judge Nguyen held that the failure to verify the amended complaint did not divest the district court of maritime jurisdiction because the defendants never objected to maritime jurisdiction in 15 months of litigation. She therefore reversed the dismissal of the maritime claim for lack of *in rem* jurisdiction over the vessel.

The defendants argued that the appeal nonetheless was moot because the bankruptcy court in the meantime had sold the vessel free of liens. The argument, Judge Nguyen said, assumes that the bankruptcy court had jurisdiction to dispose of the seaman's maritime lien. She held, "It did not."

The district court had ruled that the Section 362 stay enjoined the seaman from enforcing his maritime liens. Again, Judge Nguyen reversed.

Judge Nguyen relied on *U.S. v. ZP Chandon*, 889 F.2d 233, 238 (9th Cir. 1989), for the proposition that the automatic stay in bankruptcy court does not apply to a maritime lien for a seaman's wages. She reasoned that the principle in *Chandon* applies equally to a maritime lien for maintenance and cure, because maritime liens are "sacred liens" when owed to seamen as a consequence of their service. She cited 1893 Supreme Court authority as saying that a seaman's sacred liens are entitled to protection "as long as a plank of the ship remains."

Judge Nguyen held that "Congress would not have overruled this 'sacred' principle of admiralty law in the Bankruptcy Act *sub silentio*." Therefore, she said, the "bankruptcy stay did not apply to [the seaman's] efforts to enforce his maritime lien for maintenance and cure."

Next, Judge Nguyen held that the "bankruptcy court lacked jurisdiction to adjudicate [the seaman's] maritime lien because the admiralty court had already obtained jurisdiction over the [vessel]." To that point, she cited authority saying that "the court which first obtains jurisdiction is entitled to retain it without interference."

Consequently, the chapter 7 petition by the corporate owner of the vessel "could not have vested the bankruptcy court with the same jurisdiction," Judge Nguyen said.

Judge Nguyen said commentators are not sure whether a bankruptcy court has power to sell a vessel free of maritime liens. Regardless of the answer to that question, she held that "a maritime lien cannot be extinguished except through application of maritime law." Even if a bankruptcy court has jurisdiction to release a maritime lien, it "should be required to do so pursuant to maritime law" because priorities are different under the Bankruptcy Code and maritime law. For example, she said, seamen are in a "preferred position."

Judge Nguyen's opinion concluded with another extraordinary holding with regard to the seaman's motions for summary judgment, which had been denied below. Ordinarily, denial of a motion for summary judgment cannot be appealed.

Because she saw the decision below as manifestly incorrect, Judge Nguyen issued a writ of *mandamus* directing the district court to grant maintenance at a rate of $34 a day, subject to upward modification after trial. In that respect, the opinion is a useful survey of the law regarding *mandamus*.

The opinion is *Barnes v. Sea Hawaii Rafting LLC*, 16-15023 (9th Cir. March 28, 2018).

A bankruptcy court's in rem jurisdiction overrides a claim of sovereign immunity.

Delaware's Judge Sontchi Writes a Seminal Opinion on Sovereign Immunity

In a scholarly opinion, Chief Bankruptcy Judge Christopher S. Sontchi of Delaware explained when there is or is not a waiver of sovereign immunity allowing a debtor to sue a state or local government in bankruptcy court for a tax refund. The opinion could be applied in other contexts when a state or local government raises a sovereign immunity defense.

Judge Sontchi's intricate dissection of the law features the triumvirate of Supreme Court opinions where the justices quickly backtracked in two later cases after having insinuated earlier in *dicta* that the waiver of sovereign immunity in Section 106(a) is unconstitutional. Were it not for the two later Supreme Court decisions coupled with astute analysis like Judge Sontchi's, bankruptcy courts might lack the power to adjudicate the amount of a state's claim against a debtor or to discharge a state tax claim.

The Facts in Judge Sontchi's Case

In his 66-page opinion on July 25, Judge Sontchi carefully laid out the factual and procedural history of the claims for real estate tax refunds made by a trust created under a confirmed chapter 11 plan. He also minutely described the procedures a debtor must follow under California state law, as a predicate for seeking a refund in state court or bankruptcy court.

For the sake of understanding his conclusions, however, the essential facts are simple: Before bankruptcy, the debtor paid several years of real estate taxes on its electric generating plant. Also before bankruptcy, the debtor initiated proceedings before the California State Board of Equalization, or SBE, claiming refunds because the assessments were allegedly too high.

After confirmation, the creditors' trust in substance filed suit against the SBE and the county, asking Judge Sontchi to value the property, reduce the assessments, and direct the county to pay refunds based on lower assessments. The SBE made the equivalent of a motion to dismiss, contending that sovereign immunity left the bankruptcy court without jurisdiction to lower the assessments.

Judge Sontchi agreed and dismissed the proceedings against the SBE seeking to lower the assessments.

The Statutory Waiver of Sovereign Immunity

The creditors' trust sued under Section 505(a), which provides that bankruptcy courts, under certain circumstances, "may determine the amount or legality of any tax, . . . whether or not previously assessed, whether or not paid, and whether or not contested before and adjudicated by a judicial or administrative tribunal of competent jurisdiction."

The Third Circuit, according to Judge Sontchi, has held that Section 505(a) is a jurisdictional statute that was enacted "to clarify the bankruptcy court's jurisdiction over tax claims."

The Third Circuit also held that a sovereign immunity defense is jurisdictional in nature. Thus, the Bankruptcy Code may confer jurisdiction through Section 505(a), but the court will have no jurisdiction if the government has a sovereign immunity defense. The state's sovereign immunity (or lack of it) therefore comes to the fore.

Facially, however, Section 106(a)(1) by its terms abrogates sovereign immunity with respect to claims under Section 505. Judge Sontchi therefore analyzed whether Section 106(a)(1) withstood constitutional scrutiny to waive sovereign immunity for the trust's suit under Section 505.

Governing Supreme Court Authority

In the Supreme Court's seminal decision on sovereign immunity, *Seminole Tribe of Florida v. Florida*, 517 U.S. 44 (1996), the majority in the 5/4 decision used a footnote to describe a dissenter as interpreting the majority opinion to prohibit federal jurisdiction to enforce bankruptcy laws against the states. The majority said that the dissent's conclusion was "exaggerated." *Id*. at 72.

Two years later, the Third Circuit nonetheless applied *Seminole Tribe* to hold that Section 106(a) is "unconstitutional to the extent that it purports to abrogate state sovereign immunity in federal court." *Sacred Heart Hospital v. Dept. of Public Welfare (In re Sacred Heart Hospital)*, 133 F.3d 237, 245 (3d Cir. 1998). According to Judge Sontchi, most but not all circuits agree.

In bankruptcy cases, the Supreme Court later began to backtrack, else discharge, fresh start and reorganization might become unattainable for some debtors.

In *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440 (2004), the high court was asked to decide whether Section 106(a) was unconstitutional.

The high court ducked the larger issue in *Hood* by holding that the dischargeability of a student loan was not a suit against the state in terms of Eleventh Amendment sovereign immunity. Rather, the Court said, discharge was an *in rem* proceeding where "the bankruptcy court's jurisdiction over

the *res* is unquestioned." *Id*. at 448. The Court went on to say that "the exercise of its *in rem* jurisdiction to discharge a debt does not infringe state sovereignty." *Id*.

Ducking the larger question again two years later, the Supreme Court held in *Central Valley Community College v. Katz*, 546 U.S. 356 (2006), that the power to avoid and recover a preference operates "free and clear of the State's claim of sovereign immunity," since the preference power has been a "core aspect" of bankruptcy "since at least the 18th century." *Id*. at 373.

In *Katz*, Judge Sontchi said that the Supreme Court "refused to abide by the *dicta*" in *Seminole Tribe*.

Waiver by Consent

Although the Supreme Court twice undermined *Seminole Tribe* in the bankruptcy arena, Judge Sontchi said he remained bound by the Third Circuit's opinion in *Sacred Heart* and could not rely on Section 106(a) to override the SBE's claim of sovereign immunity.

The creditors' trust nonetheless argued several theories of waiver. Judge Sontchi held that the SBE had not waived sovereign immunity by having previously participated in preliminary stages of litigation in bankruptcy court over the refund claim. The state, he said, had neither filed a claim nor "joined any causes of action" that would constitute waiver.

The trust, however, gained more (but not enough) traction with the waiver of sovereign immunity by consent arising from the states' ratification of the U.S. Constitution and the Bankruptcy Clause. Still, Judge Sontchi said, every law labeled "bankruptcy" may not impinge on sovereign immunity.

Cobbling together the notion of consent by ratification of the Constitution with *Katz* and *Hood*, Judge Sontchi said that sovereign immunity will not bar "proceedings that effectuate the *in rem* jurisdiction of bankruptcy courts." He proceed to analyze whether the tax refund claims invoked the court's *in rem* jurisdiction.

"[M]erely because the estate may have a claim for a tax refund is not enough to invoke the *in rem* jurisdiction of the bankruptcy court," Judge Sontchi said. Essentially, he concluded that assessing the value of the plant would not invoke *in rem* jurisdiction over estate property when the claim for a refund pertained to taxes already paid, because ruling on the value of the plant would "not actually affect rights in the Facility."

On the other hand, Judge Sontchi said there would be *in rem* jurisdiction to value the property had the refund claim pertained to post-petition payments or if the state were lodging a claim for unpaid taxes.

The case at hand, according to Judge Sontchi, "is nothing more than a state law claim for a sum of money. To disallow a sovereign immunity defense in this situation would . . . allow a wholesale suit for money damages."

Judge Sontchi capped off his decision by finding no ancillary jurisdiction to sidestep sovereign immunity.

In substance, Judge Sontchi held that sovereign immunity left the court without jurisdiction to determine the proper assessment with respect to taxes that already had been paid, but there would be jurisdiction if the taxes had not been paid because the state would be seeking to collect taxes from estate property.

The trust was not left without a remedy, however, because the trust could utilize the California courts to contest the assessments. Once the assessments were determined, Judge Sontchi's opinion indicates there would be no sovereign immunity bar to proceedings seeking the payment of tax refunds.

The opinion is *In re La Paloma Generating Co. LLC*, 17-12700 (Bankr. D. Del. July 25, 2018).

Delaware bankruptcy judge disagrees with district court on final adjudicatory power to include third-party releases in confirmation orders.

Bankruptcy Court Finds Constitutional Power to Grant Releases in Confirmation Orders

On remand from the district court in *Millennium Lab Holdings*, Bankruptcy Judge Laurie Selber Silverstein of Delaware decided that a bankruptcy court has constitutional power to enter a final order granting non-consensual, third-party releases of non-bankruptcy claims as part of a chapter 11 confirmation order.

Written with a passion suggesting it may be the most important decision of her career, Judge Silverstein's 69-page opinion on Oct. 3 concludes that the limitations on the constitutional power of a bankruptcy court under *Stern v. Marshall* are altogether inapplicable to granting third-party releases because a confirmation order exclusively implicates questions of federal bankruptcy law and raises no issues under state or common law.

Ordering remand in March, District Judge Leonard P. Stark of Delaware implied, without explicitly holding, that a bankruptcy court should only make proposed findings and conclusions when granting third-party releases as part of a chapter 11 confirmation order. Sending the case back to Judge Silverstein, he told her to consider the question of constitutional power and also decide whether the appellant had waived *Stern* objections.

In her Oct. 3 opinion, Judge Silverstein persuasively ruled that the appellant had waived *Stern* objections by never raising the issue during the confirmation process. If there is another appeal, Judge Stark and even the Third Circuit could uphold confirmation just on the issue of waiver and never reach the broader *Stern* questions given the principle that courts should not make constitutional rulings when a case can be decided on another ground.

Consequently, *Millennium Lab Holdings* may leave the constitutional issue undecided at the appellate level. Until the question is starkly raised and decided, parties will proceed at their peril if they consummate plans with releases based only on the bankruptcy court's confirmation order.

The Facts

The chapter 11 debtor, Millennium Lab Holdings II LLC, obtained a $1.825 billion senior secured credit facility and used $1.3 billion of the proceeds before bankruptcy to pay a special dividend to shareholders.

Indebted to Medicare and Medicaid for $250 million that it could not pay, Millennium filed a chapter 11 petition along with a prepackaged plan calling for the shareholders to contribute $325 million in return for releases of any claims that could be made by the lenders. The plan did not allow the lenders to opt out of the releases.

Before confirmation, a lender holding more than $100 million of the senior secured debt filed suit in district court in Delaware against the shareholders and company executives who would receive releases under the plan. The suit alleged fraud and RICO violations arising from misrepresentations inducing the lenders to enter into the credit agreement.

Over objection, Judge Silverstein confirmed the plan and approved the third-party releases. The dissenting lender appealed.

Having consummated the plan, Millennium filed a motion to dismiss the appeal on the ground of equitable mootness, because the plan had been consummated in the absence of a stay pending appeal.

District Judge Stark's Remand

Arguably for the first time, the objecting lender contended on appeal that the bankruptcy court lacked constitutional power to enter a final order granting third-party releases. Although the bankruptcy court had clearly found "related to" jurisdiction to impose the releases, District Judge Stark concluded that the bankruptcy court had not been called on to decide whether it had power under *Stern* to enter a final order including the releases.

To most readers, Judge Stark's decision in March implied, without holding, that granting the releases was beyond the bankruptcy court's constitutional power. Among other things, Judge Stark said that the objecting lender was entitled to an Article III adjudication because the releases were "tantamount to resolution of those claims on the merits against" the lender.

Rather than rule on a constitutional issue that had not been developed in the lower court, Judge Stark remanded the case for Judge Silverstein to decide whether she had final adjudicatory authority, either as a matter of constitutional law or as a consequence of the lender's waiver. If there were no power to make a final order, Judge Stark said that Judge Silverstein could submit proposed findings and conclusions or strike the releases from the confirmation order.

To read ABI's discussion of Judge Stark's opinion, click here.

Granting Releases Is a 'Core' Bankruptcy Power

Ruling after remand, Judge Silverstein didn't keep the reader in suspense. On the second page of her opinion, she said there is constitutional power to grant releases in a confirmation order. To

rule otherwise, she said, would go "far beyond the holding of any court" and "dramatically change the division of labor between the bankruptcy and district courts."

Judge Silverstein found circuit court support for her conclusion. She cited post-*Marathon Pipeline* but pre-*Stern* decisions from the Seventh and District of Columbia Circuits finding constitutional power to grant third-party releases in a confirmation order.

Post-*Stern*, Judge Silverstein found support from two Third Circuit opinions for the proposition that a bankruptcy court can issue a final order on a core issue that has preclusive effect on a third party's lawsuit: *In re Lazy Days' RV Center Inc.*, 724 F.3d 418 (3d Cir. 2013), and *In re Linear Electric Co.*, 852 F.3d 313 (3d Cir. March 20, 2017). She emphasized a statement in *Lazy Days'* that *Stern* is "plainly inapposite" where the debtor sought relief "based on a federal bankruptcy law provision with no common law analogue."

More recently, Judge Silverstein cited bankruptcy court decisions from Boston and White Plains, N.Y., finding constitutional power to grant third-party releases in confirmation orders.

Adopting even the broadest interpretation of *Stern*, Judge Silverstein said that confirming a plan with releases "does not rule on the merits of the state law claims being released." Therefore, she said, "*Stern* is inapplicable as confirmation of a plan is not a state law claim of any type."

To the contrary, Judge Silverstein said, a bankruptcy court has final adjudicatory power because the court "is applying a federal standard" to ensure that the releases "comply with applicable provisions of the Bankruptcy Code."

In short, there is no contravention of *Stern* because the bankruptcy court is making a determination on confirmation based entirely on federal bankruptcy law, where there is statutory core power under 28 U.S.C. § 157(b)(2)(L). The fact that confirmation bars a creditor's state law claims against a third party is merely incidental.

Indeed, the incidental effect on third-party claims is the gist of the issue. Judge Silverstein pointed out the consequences of making *Stern* applicable to plans with third-party releases.

If there were no final adjudicatory power in the confirmation context, Judge Silverstein said that bankruptcy courts could no longer make Section 363 sale orders insulating buyers from successor liability. Similarly, bankruptcy courts would lack power, she said, to order substantive consolidation, bar annual shareholders' meetings, recharacterize debt as equity, or subordinate claims.

On the question of the waiver of *Stern* objections under *Wellness International*, Judge Silverstein thoroughly analyzed the record to conclude that the objecting lender never raised the constitutional question during or even after the confirmation process.

Her original ruling on confirmation did not deal with final adjudicatory power because any reference to *Stern* was so oblique that neither the court nor the parties understood that a constitutional issue was afoot. Citing the *Wellness International* prohibition of sandbagging, Judge Silverstein said that the lender could not lie in the weeds and raise constitutional infirmities for the first time on appeal.

On the ground of waiver alone, Judge Silverstein found that she was entitled to enter a final order.

The opinion is *In re Millennium Lab Holdings II LLC,* 15-12284, 575 B.R. 252 (Bankr. D. Del. Oct. 3, 2017).

Makewhole Premiums

Third Circuit says that New York bankruptcy court's* MPM *decision was wrong.

Third Circuit Splits with New York by Allowing Makewhole Premiums in Chapter 11

Parting company with decisions from New York, the Third Circuit in Philadelphia reversed the lower courts in Delaware and ruled that so-called makewhole premiums must be paid to bondholders, at least when prepayment is voluntary in chapter 11 and the language of the indenture is not to the contrary.

In a Nov. 17 decision in the wake of the reorganization of electric energy giant Energy Future Holdings Corp., the Third Circuit distinguished a Second Circuit decision and eviscerated a New York bankruptcy court opinion that favored large corporate debtors by holding that makewhole premiums are not owing if the debt was automatically accelerated by a bankruptcy filing. The Third Circuit opinion is important because that court makes law governing Delaware, where many of the country's largest reorganizations are filed.

Litigation in the Lower Courts

Energy Future needed bankruptcy relief but also had designs on using chapter 11 to refinance secured bonds bearing interest rates well above the current market. However, more than $400 million in makewhole premiums on first and second lien bonds would be due in refinancings outside of bankruptcy.

A makewhole premium is a payment required in some indentures to compensate lenders for being forced to reinvest at lower interest rates when bonds are paid before maturity.

Immediately after the chapter 11 filing in Delaware, Energy Future refinanced the debt with court approval, leaving open the question of whether makewhole premiums were owing. Later, the bankruptcy court ruled that the premiums were not owing. The decisions by the bankruptcy court were upheld this year by a district judge in Delaware.

Reversal in the Third Circuit

Writing for the appeals court, Circuit Judge Thomas Ambro reversed the lower courts and reinstated the liability to pay the makewhole premiums. According to Judge Ambro, the result turned on the language of the indentures. His decision cannot be understood as a blanket ruling on makewhole premiums generally in bankruptcy, except to the extent that indentures have the same language.

For the first lien bondholders, pivotal Section 3.07 of the indenture, entitled "Optional Redemption," said that the company could "redeem" the notes by paying the principal and accrued interest "plus the Applicable Premium."

The bankruptcy court disallowed the makewhole premium, focusing on another provision in the indenture, Section 6.02, which automatically accelerated the notes in the event of bankruptcy. The bankruptcy judge reasoned that no premium was due in bankruptcy because the acceleration clause made no mention of the premium.

Judge Ambro said that Section 3.07 raised three questions: (1) was there a redemption; (2) was it optional; and (3) did it occur before the specified date? He answered all three questions in the affirmative.

First, Judge Ambro cited governing New York law for the proposition that a redemption includes "both pre- and post-maturity repayments." Next, he said the "redemption was very much optional" because the debtor could have reinstated the debt in a chapter 11 plan, even though the acceleration was automatic.

Judge Ambro therefore concluded that Section 3.07, "on its face," required paying the premium.

In opposition, the debtor relied on a 2013 Second Circuit decision in the American Airlines reorganization. Judge Ambro made short shrift of that argument by pointing to language in the indenture in the American Airlines case explicitly saying that no premium was due in an acceleration resulting from bankruptcy.

Rebutting the bankruptcy court's reliance on Section 6.02, Judge Ambro said "it surpasses strange to hold that silence in Section 6.02 supersedes Section 3.07's simple script."

Judge Ambro Rejects *MPM Silicones*

The second lien indenture was similar but not identical. In it, Section 6.02 said that bankruptcy automatically accelerated all principal "and premium, if any."

To escape the seemingly explicit requirement to pay the premium in bankruptcy, the Delaware bankruptcy court followed a 2014 New York bankruptcy court decision called *MPM Silicones*, which involved a similar indenture. There, the judge in Manhattan said that the reference to "premium" was not adequately specific to invoke the "Applicable Premium," which was the defined term for a makewhole premium.

With respect to the second lien bonds, Judge Ambro reversed the bankruptcy court because the words "premium, if any" left "no doubt" that a makewhole was required.

Further undercutting *MPM Silicones* and cases that adopted its reasoning, Judge Ambro used the remainder of his opinion to explain why the New York bankruptcy court misinterpreted New York law, which governed the indentures. He said that the Manhattan court stretched a New York Court of Appeals decision "beyond its language." The Delaware bankruptcy court, he said, adopted the same misinterpretation of New York law.

Judge Ambro said the New York Court of Appeals decision, called *Northwestern*, reflected a "policy concern that lenders should not be permitted 'to recover prepayment premiums after default and acceleration'" outside of bankruptcy. In the *Energy Future* case, he said the noteholders "did not seek immediate payment." Indeed, the noteholders attempted to deaccelerate and reinstate the debt.

By refusing to enforce Section 3.07 after acceleration, Judge Ambro said that the bankruptcy court "ran afoul of New York authority by failing to enforce a contract provision" that was "not affected by acceleration."

Judge Ambro was a bankruptcy lawyer before ascending to the circuit bench in 2000.

The opinion is *Delaware Trust Co. v. Energy Future Intermediate Holding Co. LLC (In re Energy Future Holdings Corp.)*, 842 F.3d 247 (3d Cir. Nov. 17, 2016).

***Till** doesn't apply in fixing cramdown interest rates in major corporate reorganizations, circuit says.*

Second Circuit Splits with Third on Makewholes Occasioned by Bankruptcy

Handing down an opinion almost a year in making, the Second Circuit made four significant pronouncements pertinent to major corporate reorganizations. In an opinion on Oct. 20 by Circuit Judge Barrington D. Parker, the appeals court abandoned the so-called *Till* formula for calculating the rate of interest paid to secured creditors in a chapter 11 cramdown.

Instead, the circuit court said that the interest rate on a crammed-down debt obligation must reflect the higher market rate, if one exists.

Although the cramdown ruling was favorable to lenders, Judge Parker's second holding was favorable to debtors because he held that a so-called makewhole premium is not earned on debt that was automatically accelerated by bankruptcy. The Second Circuit's opinion on that issue is starkly in conflict with the Third Circuit's *Energy Future* opinion from November 2016 holding precisely the opposite.

In a third ruling, again favorable to creditors, Judge Parker refused to dismiss the appeal under the doctrine of equitable mootness because the lenders had made every conceivable effort at obtaining a stay pending appeal.

Finally, the appeals court arguably engaged in appellate fact-finding in upholding the lower court's conclusion regarding contractual subordination.

The MPM Silicones Chapter 11 Plan

Bond indentures often contain provisions calling for yield maintenance, or makewhole premiums, to compensate bondholders for having to reinvest at lower interest rates if the loan is repaid before maturity. The provisions are designed as disincentives to refinance when interest rates drop.

Indentures are not crystal clear on whether the makewhole is due if prepayment occurs in chapter 11 cases when the debt is accelerated automatically on bankruptcy. And so it was with MPM Silicones LLC, also known as Momentive Performance, when the company was confirming its chapter 11 plan in 2014.

In confirming the plan over the objection of secured lenders claiming entitlement to a makewhole, the bankruptcy court issued four major rulings: (1) The secured lenders were not entitled to a makewhole; (2) In being given a new debt obligation in cramdown, the secured lenders were not entitled to a market rate of interest under the Supreme Court's *Till* decision from 2004; (3) The appeal was not equitably moot, and (4) Subordinated notes were indeed subordinated to second-lien debt and were therefore not entitled to any distribution under the plan.

The secured lenders deprived of the makewhole and the subordinated lenders took appeals, but the district court upheld the bankruptcy court in May 2015. The bankruptcy and district courts denied stays pending appeal, and the Second Circuit denied a stay for lack of appellate jurisdiction.

The ensuing appeal in the Second Circuit was argued on Nov. 9, 2016. A week later, the Third Circuit handed down *Delaware Trust Co. v. Energy Future Intermediate Holding Co. LLC (In re Energy Future Holdings Corp.)*, 842 F.3d 247 (3d Cir.). Written by Circuit Judge Thomas Ambro, *Energy Future* reversed the two lower courts in Delaware, ruled that the makewhole was owing, distinguished a leading Second Circuit case denying a makewhole, eviscerated the bankruptcy court's *MPM Silicones* opinion, and said that makewholes are owing under typically written indentures.

As a consequence of *Energy Future*, filing a major chapter 11 case in Delaware is a nonstarter if there is potential liability for a makewhole. On the other hand, New York is an attractive venue after *MPM Silicones*.

Although there is a split of circuits, the makewhole issue is not a likely case for the Supreme Court to grant *certiorari*, because the outcome turns on interpretation of an ambiguous contract governed by state law. Consequently, the split will endure unless New York State's highest court opines on that state's law and functionally decides whether makewholes are earned after bankruptcy, an outcome as to which Judge Ambro made an educated guess on state law.

Makewholes

In ruling that no prepayment premium was owing, Judge Parker described the bankruptcy and district courts as construing the indenture to mean that makewholes are "due only in the case of an 'optional redemption' and not in the case of an acceleration brought about by a bankruptcy filing." Judge Parker said, "We agree too."

His ruling in that respect was cabined by the Second Circuit's decision in *In re AMR Corp.*, 730 F.3d 88 (2d Cir. 2013), where, Judge Parker said, the appeals court upheld denial of a makewhole and "rejected nearly identical arguments."

To overcome the effect of automatic acceleration that was the key to denial of a makewhole, the creditors contended that they should have been permitted to deaccelerate the debt. Judge Parker

rejected that argument too, saying that "the automatic stay barred rescission of the acceleration of the notes."

Judge Parker gave the Third Circuit's *Energy Future* opinion nothing more than a "but see" citation, without discussion of where Judge Ambro went wrong. Where the Third Circuit based its conclusion in large part on New York law, Judge Parker had no similarly detailed discussion.

Till Inapplicable in Major Chapter 11s

In *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004), a plurality of the justices on the Supreme Court said that the interest rate to be paid to a secured lender being crammed down in chapter 13 on a subprime auto loan is the prime rate plus an upward adjust of 1% to 3% to cover the time-value of money, inflation and risk. The plurality rejected the notion of pegging the interest rate to market rates, because there usually is none for that type of consumer loan.

Employing *Till*, the bankruptcy court gave two issues of secured debt interest rates of 4.1% and 4.85%, based on a prime rate of 2.1%, to which the judge added 2.0% and 2.75%, respectively, for risk.

In footnote 14 in *Till*, the plurality said that the chapter 13 formula may not be suited to chapter 11, where there may be a market for similar loans to large bankrupt companies. Judge Parker adopted the approach of the Sixth Circuit in *In re American HomePatient Inc.*, 420 F.3d 559 (6th Cir. 2005), by departing from the *Till* formula if there is an "efficient market" for similar loans to companies in chapter 11. He said that *American HomePatient* "best aligns with the Code and relevant precedent."

Preparing for the confirmation of its plan, MPM Silicones scoured the market because the company would have been required to cash out the secured lenders had they accepted a plan that offered them no makewhole. The lenders argued that they should be entitled to interest on crammed-down debt of between 5% and 6%, reflecting offers the company had received for loans to finance confirmation.

Without intimating what the result should be, Judge Parker remanded the case for the bankruptcy court to "ascertain if an efficient market rate exists and, if so, apply that rate, instead of the formula rate." He said the lower courts erred "in categorically dismissing the probative value of market rates of interest."

Equitable Mootness

The debtor argued that the appeals court should dismiss the appeal on the ground of equitable mootness, because the plan had long since been implemented. Citing *In re Chateaugay Corp.*, 988 F.2d 322 (2d Cir. 1993), Judge Parker said that the "chief consideration" is whether the "appellant

sought a stay of confirmation." If a stay was sought, the circuit will allow relief on appeal if it is "at all feasible" without knocking the props out from under the plan.

Because raising the interest rate to the level sought by the creditor would only increase the reorganized company's costs by $32 million spread over seven years, Judge Parker said that the appeal was not equitably moot.

In that regard, like the issue we discuss next, the appeals court may have engaged in appellate fact-finding by concluding that a higher interest rate would not cripple the reorganized company financially. Some might contend that Judge Parker should have remanded the case for the bankruptcy court to decide whether the interest rate could be raised without disrupting the reorganized company's finances.

Contractual Subordination

Plan confirmation precipitated an intercreditor dispute regarding the contractual subordination of one debt issue that turned on the definition of "senior debt." The erstwhile subordinated lenders constructed a sophistic but not frivolous argument to relieve themselves of the burden of subordination. Had they prevailed, they would have been entitled to a distribution under a plan that otherwise offered them nothing.

Finding the indenture to be unambiguous, the two lower courts agreed that the debt indeed was subordinated. Judge Parker reached the same conclusion, but he said the indenture was ambiguous.

In contract or statutory interpretation, courts search for a meaning that renders nothing superfluous. Any interpretation of the indenture, Judge Parker said, would result in making some words superfluous. "Where, as here, varying interpretations render contractual language superfluous, we are not obligated to arbitrarily select one as opposed to another," the judge said.

The differing reasonable interpretations made the indenture "ambiguous as a matter of law," Judge Parker said.

When a contract is ambiguous, courts look to extrinsic evidence. Judge Parker then cited the numerous instances of SEC filings and other public statements before bankruptcy where the debtor said that the debt was subordinated. In what arguably amounts to appellate fact-finding, he said it "was widely understood in the investment community that the Second-Lien Notes had priority."

Judge Parker rejected another argument that, he said, would result in an "irrational outcome." That argument was based on the notion that the granting of a security interest to the senior debt resulted in taking away senior status.

Upholding the lower courts on a different theory, Judge Parker had "little trouble concluding that extrinsic evidence establishes that the most reasonable interpretation of the indenture is that" the notes qualify as senior debt.

Evidently, Judge Parker believed that the record supported only one conclusion and that any other finding by the bankruptcy court would have been clearly erroneous. Perhaps it would have been better had he said so, to avoid the accusation of appellate fact-finding.

Regardless of whether the record led to any other plausible conclusion, relying on public filings is akin to making a decision on an ambiguous statute based on legislative history. Led by the Supreme Court, the use of legislative history is out of fashion, because statements by legislators are not necessarily in tune with the statute.

Similarly, public filings can represent the debtor's unilateral view about a complex transaction. Conceivably, a company could attempt to achieve a result by making SEC filings that it was unable to achieve in negotiating the transaction originally. Nonetheless, purchasers of securities in the secondary market are presumably aware of the issuer's subsequent description of the transaction.

This feature of the opinion will add a significant new wrinkle to the business of buying distressed debt based a novel interpretation of an ambiguous provision in the deal documents. With the Second Circuit telling lower courts they can or perhaps should interpret creditors' rights based on the debtor's public statements, courts may be unlikely adopt interpretations that run afoul of the issuer's pronouncements.

The Circuit Split

The Second and Third Circuits are now split on entitlement to a makewhole given language commonly used in some indentures. Unless the Second Circuit reverses course on a motion for rehearing or rehearing *en banc*, the split will persist.

The losing side in the Third Circuit had filed a motion for rehearing *en banc*, which was being held in abeyance by the appeals court pending the Second Circuit's opinion in *MPM Silicones*. In the meantime, however, the parties settled; the rehearing motion was withdrawn; and the *Energy Future* decision became final.

Although the Second Circuit is loath to grant rehearing *en banc*, a motion for reconsideration by the entire circuit bench would not be a surprise. As occurred in the Fifth Circuit in *Janvey v. Golf Channel Inc.*, 834 F.3d 570 (5th Cir. Aug. 22, 2016), the lenders pursuing a makewhole might ask on rehearing that the appeals court certify the underlying state law issue to the New York Court of Appeals, that state's highest court.

However, state law was not so much a focus of Judge Parker's decision as it was the Third Circuit's *Energy Future* opinion, where the losing side was seeking certification to the state tribunal before the parties settled.

The opinion is *BOKF NA v. Momentive Performance Materials Inc. (In re MPM Silicones LLC)*, 874 F.3d 787 (2d Cir. Oct. 20, 2017).

Plans & Confirmation

A secured creditor making the 1111(b) election is not automatically entitled to a due-on-sale clause paying the claim in full if the property is sold after confirmation.

Ninth Circuit Holds that One Accepting Class in Joint Plan Is Sufficient

In a case of first impression among the courts of appeals, the Ninth Circuit held that Section 1129(a)(10) does not require every debtor in a joint plan to have an accepting impaired class. On the question of whether there must be an accepting class on a "per plan" or a "per debtor" basis, the appeals court agreed with a bankruptcy court in New York but disagreed with a bankruptcy court in Delaware.

The Ninth Circuit also held in its Jan. 25 opinion that confirmation of a "cramdown" plan does not require the plan to include a due-on-sale clause when a secured lender has taken the Section 1111(b)(2) election.

Even though Section 1129(a)(10) by itself does not require each debtor in a multi-debtor plan to have an accepting class, one circuit judge insinuated in a concurring opinion that a secured creditor could defeat confirmation by claiming that a consolidated plan must comply with the standards for substantive consolidation.

The Tortured History of Transwest Resort Properties

Five debtors owned a hotel in a vertical ownership structure. The chapter 11 cases were not substantively consolidated. One lender held both the mortgage debt on the operating entity that owned the real estate and the mezzanine debt secured by the mezzanine borrower's ownership interest in the operating company.

For the mortgage in the original principal amount of $209 million, the plan gave the lender a new $247 million note due in 21 years, paying interest only with a balloon payment on maturity. Although the mortgage originally had no due-on-sale clause, the new mortgage contained a due-on-sale clause.

If the buyer sold the project between the fifth and fifteenth years, the plan provided that the due-on-sale clause would not apply. Instead, a buyer in the 10-year gap would take ownership subject to the mortgage created at confirmation.

The joint plan for all five debtors had 10 classes of creditors. Five accepted the plan. The secured lender voted both claims against the plan and elected under Section 1111(b)(2) to have the entire mortgage claim treated as secured.

Because the mezzanine lender had the only claim against two mezzanine borrowers, the lender contended that cramdown requirements were not met because those two debtors had no accepting class. Contending that the 10-year gap in the due-on-sale clause depressed the value of the Section 1111(b)(2) election, the lender also argued that Section 1111(b)(2) requires a plan to have a due-on-sale clause.

The plan was sponsored by a purchaser who invested $30 million to acquire the equity.

The bankruptcy judge confirmed the plan in December 2011. Chief District Judge Raner C. Collins of Tucson, Ariz., dismissed the lender's original appeal on the ground of equitable mootness, because the plan had been consummated in the absence of a stay and the buyer had made its investment. Over a vigorous dissent, the Ninth Circuit held in September 2015 that a buyer who actively participates in reorganization is not protected by equitable mootness should a creditor appeal but not obtain a stay preventing consummation of the plan. *JPMCC 2007-C1 Grasslawn Lodging LLC v. Transwest Resort Properties Inc.* (*In re Transwest Resort Properties Inc.*), 801 F.3d 1161 (9th Cir. Sept. 15, 2015).

Denying a motion for rehearing *en banc*, the circuit remanded the case to Judge Collins, who upheld confirmation on the merits in June 2016. He ruled that one accepting class per plan is sufficient and that Section 1111(b) does not require a due-on-sale clause. To read ABI's discussion of Judge Collins' opinion, click here.

The lender appealed a second time, resulting in the Ninth Circuit's new opinion on Jan. 25 upholding confirmation and rejecting both of the lender's arguments.

Due-on-Sale Not Required on an 1111(b) Election

When a secured lender is undersecured, Section 1111(b) allows the lender to "elect to have its entire claim treated as a secured claim," Circuit Judge Milan D. Smith said in his opinion for the Ninth Circuit. The lender urged the appeals court to rule that a mortgage modified under a plan must include a due-on-sale clause to protect the value of the Section 1111(b) election.

Judge Smith said that the argument "finds no support in the text of the statute, nor does the language of the statute implicitly require the inclusion of such a clause." He added that the "broader statutory context of chapter 11 further undermines the lender's position."

Judge Smith said that Section 1123(b)(5) allows modification of a secured lender's claim, while Section 1129(b)(2)(A)(i)(I) "expressly allows a debtor to sell the collateral to another entity

so long as the creditor retains the lien securing its claims, yet the statute does not mention any due-on-sale requirement . . . .”

Judge Smith found support from the Seventh Circuit, which had held that a due-on-sale clause is not a lien that must be retained for the court to confirm a plan. *In re Airadigm Communications Inc.*, 519 F.3d 640 (7th Cir. 2008).

He therefore held “that Section 1111(b)(2) does not require that a plan involving an electing creditor contain a due-on-sale clause.”

One Accepting Class Per Plan Is Enough

Judge Smith said that the “plain language” of Section 1129(a)(10) “supports the ‘per plan’ approach.” He said the section “requires that one impaired class ‘under the plan’ approve ‘the plan.’”

The statute, the judge said, does not distinguish between single-debtor and multi-debtor plans: “[O]nce a single impaired class accepts a plan, Section 1129(a)(10) is satisfied as to the entire plan.”

Judge Smith found fault with the rationale in *In re Tribune Co.*, 464 B.R. 126, 182–83 (Bankr. D. Del. 2011), where a bankruptcy judge in Delaware held that each debtor must have an accepting class in a multi-debtor plan. Although he did not cite the case, a bankruptcy court in New York had held that one accepting class is sufficient in a joint plan for several debtors. *JPMorgan Chase Bank N.A. v. Charter Communications Operating, LLC (In re Charter Communications)*, 419 B.R. 221, 264–66 (Bankr. S.D.N.Y. 2009).

In his opinion for the court, Judge Smith alluded to a shortcoming in the lender’s litigation strategy that the concurring opinion developed. Judge Smith said that the lender did not object to confirmation by arguing that the joint plan amounted to substantive consolidation.

The Concurring Opinion

Circuit Judge Michelle T. Friedland wrote a concurring opinion where she agreed that Section 1111(b)(2) does not require a due-on-sale clause.

Finding the statute “somewhat ambiguous,” Judge Friedland also agreed that the “better reading” of Section 1129(a)(10) leads to the conclusion that one acceptance per plan, not one per debtor, is sufficient.

Judge Friedland wrote a concurring opinion to say that objecting to the plan as *de facto* substantive consolidation may have enabled the lender to block confirmation. She said that the

"problem" was "that the plan effectively merged the debtors without an assessment of whether consolidation was appropriate" under Ninth Circuit standards.

Judge Friedland said the lender did not object to confirmation by raising the issue of substantive consolidation and thus was barred from raising the theory on appeal.

Judge Friedland's opinion does not cite any authority for the proposition that substantive consolidation standards must be applied to multi-debtor plans. If joint plans could be confirmed only when substantive consolidation was proper, few multi-debtor plans would ever be approved.

Judge Friedland did not mention that Section 1129(a) contains several protections for dissenting creditors in a joint plan, such as the requirement that the plan must give the dissenter at least what it would receive in a liquidation. There was apparently no issue that the plan satisfied the best interests test for the dissenting mezzanine lender.

The opinion is *JPMCC 2007-C1 Grasslawn Lodging LLC v. Transwest Resort Properties Inc.* (*In re Transwest Resort Properties Inc.*), 16-16221 (9th Cir. Jan. 25, 2018).

To warrant 'designation,' a claim purchaser must have an 'ulterior motive' beyond self-interest.

Buying Just Enough Unsecured Claims to Defeat Confirmation Is Ok, Ninth Circuit Says

Buying barely enough unsecured claims to defeat confirmation of a plan is not reason in itself for barring a secured creditor from voting the purchased claims against confirmation of a chapter 11 plan, according to the Ninth Circuit.

In *Figter Ltd. v. Teachers Ins. & Annuity Association of America (In re Figter)*, 118 F.3d 635, 639 (9th Cir. 1997), the Ninth Circuit ruled that a secured creditor was entitled to vote unsecured claims against confirmation of a chapter 11 plan when the lender had purchased all the claims in the class. In his June 4 opinion, Ninth Circuit Judge N. Randy Smith expanded *Figter* by ruling emphatically that a secured creditor is not in bad faith by purchasing just enough claims to defeat confirmation, thereby adversely affecting other creditors.

Owed about $4 million, the secured creditor spent $13,000 on advice of counsel to purchase just over half in number of the chapter 11 debtor's unsecured claims. The purchased claims represented only 10% of the unsecured class in amount.

The lender's counsel testified that the client made no attempt at purchasing all unsecured claims. The client's motivation, the lawyer said, was to acquire a blocking position and do what was best for the lender.

Although the debtor had the required two-thirds vote in amount in the unsecured class to confirm the plan, the debtor was facing defeat because a majority in number of unsecured creditors were not voting in favor of the plan as required by Section 1126(c). The plan would pay unsecured creditors in full in a few months.

The debtor moved to "designate" the unsecured claims purchased by the lender under Section 1126(e), which provides that the court "may designate any entity whose acceptance or rejection of such plan was not in good faith . . . ." In substance, "designate" means to disallow voting.

The bankruptcy court designated the claims and later confirmed an amended version of the plan. Judge Smith said that the bankruptcy court based designation on just two facts: (1) the lender did not offer to purchase all unsecured claims, and (2) voting the purchased claims against the plan would give the lender an "unfair advantage" and would be "highly prejudicial" to other creditors.

The district court affirmed, but the Ninth Circuit reversed.

Judge Smith said that the Bankruptcy Code does not define “good faith” as used in Section 1126(e). *Figter*, he said, defined “bad faith” as an attempt to “secure some untoward advantage over other creditors for some ulterior purpose.” Judge Smith quoted *Figter* as holding that designation applies to creditors who were “‘not attempting to protect their own proper interests, but who were, instead, attempting to obtain some benefit to which they were not entitled.’”

According to *Figter*, “bad faith explicitly does not include ‘enlightened self-interest, even if it appears selfish to those who do not benefit from it,’” Judge Smith said. Therefore, purchasing claims to obtain a blocking provision and to protect a creditor’s own claim “does not demonstrate bad faith or an ulterior motive,” *Figter* held.

Purchasing all unsecured claims was only one factor prompting the *Figter* court to find good faith, Judge Smith said. He cited Second Circuit authority for the proposition that purchasing claims to block a plan is not bad faith in itself.

Judge Smith faulted the bankruptcy court for not analyzing the lender’s motivation and failing to identify an “ulterior motive.” Citing *Figter*, he said that self-interest and ulterior motive are not identical. Ulterior motive is attempting to obtain a benefit to which the creditor is not entitled, Judge Smith said, again citing *Figter*.

Examples of bad faith, according to Judge Smith, include purchasing a claim to block a lawsuit against the purchaser or buying claims to destroy a competitor’s business. “There must be some evidence beyond negative impact on other creditors,” Judge Smith said.

In sum, the bankruptcy court erred by making no findings about the lender’s motivation and by considering the effect on other creditors without evidence of bad faith.

The opinion is *Pacific Western Bank v. Fagerdala USA-Lompoc Inc. (In re Fagerdala USA-Lompoc Inc.)*, 16-35430 (9th Cir. June 4, 2018).

Eighth Circuit insulates parishes and church schools from substantive consolidation.

Non-Bankrupt Nonprofit Entities Are Not Subject to Substantive Consolidation

Because substantive consolidation is the equivalent of involuntary bankruptcy, Section 303(a) precludes a bankruptcy court from ordering substantive consolidation with non-bankrupt nonprofit schools, churches and charitable organizations, the Eighth Circuit ruled on April 26, affirming two lower courts.

The appeal arose in the chapter 11 reorganization of the Archdiocese of St. Paul and Minneapolis, where the church is dealing with claims of clergy sexual abuse.

To expand the pool of assets available for abuse claimants, the official creditors' committee filed a motion seeking substantive consolidation of the archdiocese with about 200 non-bankrupt schools, parishes, and other nonprofit organizations controlled by the church. The committee said that the non-bankrupt church entities owned the majority of the assets in the archdiocese.

As described in the decision for the appeals court authored by Circuit Judge Michael J. Melloy, the committee's complaint alleged in detail how the archdiocese exercised direct and virtually total control of even minute activities by the parishes and schools, including the forced consolidation of parishes over opposition from the parishes themselves, the parishioners, and the parish priests.

Bankruptcy Judge Robert J. Kressel of Minneapolis granted the archdiocese's motion to dismiss without reaching the First Amendment or the Religious Freedom Restoration Act. He dismissed because substantive consolidation would be the equivalent of an involuntary petition against the nonprofit schools and parishes. The district court affirmed, as did Judge Melloy.

Judge Melloy explained that substantive consolidation "is an equitable remedy grounded in the broad powers" of Section 105(a), which gives the bankruptcy court authority to issue "any order" that is "necessary or appropriate to carry out the provisions of" the Bankruptcy Code. He described substantive consolidation as combining "the consolidated entities' assets and liabilities to satisfy creditors from a combined pool of assets."

Although the circuits allow substantive consolidation among debtors, Judge Melloy said that only the Ninth Circuit has permitted consolidation with non-bankrupt entities. However, no circuit has authorized consolidation with a nonprofit non-bankrupt entity.

Analyzing the propriety of the rulings below, Judge Melloy began with *Law v. Siegel*, 134 S. Ct. 1188, 1194 (2014), where the Supreme Court taught that the equitable powers in Section 105(a) cannot "override explicit mandates of other sections of the Bankruptcy Code."

Judge Melloy then turned to Section 303(a), which effectively prohibits the filing of an involuntary petition against "a corporation that is not a moneyed, business, or commercial corporation." Surveying state law governing the incorporation of religious entities, he said that the parishes, schools, and other non-bankrupt entities in the archdiocese were nonprofit corporations falling within the ambit of Section 303(a).

Judge Melloy agreed with Judge Kressel's conclusion that substantive consolidation "would necessarily pull non-profit entities into bankruptcy involuntarily in contravention of Section 303(a)." Again agreeing with Judge Kressel, Judge Melloy held there was no legal authority to order substantive consolidation because doing so "would override an explicit statutory protection in the Bankruptcy Code."

Judge Melloy went on to say that "Section 303(a) prevents the use of Section 105(a) to force truly independent non-profit entities into involuntary bankruptcy."

By using the words "truly independent," Judge Melloy left the door open to allegations that consolidation may be proper if the nonprofit entity is an *alter ego* under state law or was part of a fraudulent scheme, such as a Ponzi scheme.

However, Judge Melloy was careful to say that "isolated incidents of lack of corporate formality or commingling," as alleged in the committee's complaint, "fall far short of the requirement of *alter ego* status under Minnesota law." Moreover, Judge Melloy said that the committee's theory "would effectively nullify" Minnesota law, which gives the archbishop "effective control" over the affiliated entities.

In sum, Judge Melloy said that "global consolidation of all entities in the archdiocese is not authorized by the Bankruptcy Code."

To read ABI's report on the district court opinion, click here. To read the report on Judge Kressel's opinion, click here.

The opinion is *Official Committee of Unsecured Creditors v. Archdiocese of St. Paul and Minneapolis* (*In re Archdiocese of St. Paul and Minneapolis),* 17-1079 (8th Cir. April 26, 2018).

New York and Delaware judges disagree on third party releases by non-voting creditors.

Non-Voting Creditors' Consent to Third Party Releases Can't Be Inferred

Disagreeing with some of his colleagues in New York and Delaware, Bankruptcy Judge Stuart M. Bernstein ruled that he had neither jurisdiction nor statutory power to issue a release of claims against non-debtor third parties held by creditors who did not vote on the confirmed chapter 11 plan of SunEdison, Inc., a renewable energy developer.

Although he gave the debtors an opportunity to submit a modified release that he would approve, SunEdison might be unable to comply with the rigorous standards that Judge Bernstein imposed.

The SunEdison Plan

Although no one objected, Judge Bernstein said at the confirmation hearing in late July that he had questions about the propriety of the broadly worded third party releases contained in the plan. Judge Bernstein called for further briefing on the releases but went ahead and confirmed the plan, because the debtors and affected parties were willing to accept the risk that the judge would knock out the releases later.

In his Nov. 8 opinion, Judge Bernstein said that the claims to be released and the parties benefitting from the releases were equally broad. The releases bound not only creditors who voted for the plan but also creditors who did not vote at all. He said that non-voting creditors "would release a largely unidentified group of non-debtors from liability based on pre-petition, post-petition and post-confirmation (*i.e.*, future) conduct occurring through the plan's future effective date that related in any way to their clams or those bankruptcy cases."

Deemed Consent

First, Judge Bernstein analyzed whether non-voting creditors impliedly consented to the releases, much like the Supreme Court in *Wellness International Network, Ltd. v. Sharif*, 135 S. Ct. 1932, 191 L. Ed. 2d 911, 4337 (2015), said that creditors' inaction can result in implied consent to the bankruptcy court's authority to issue a final order.

Rather than focus on constitutional principles, Judge Bernstein analyzed contract law to decide whether non-voting creditors were deemed to consent to the releases, because they were warned in the disclosure statement that inaction might be taken as consent.

Judge Bernstein began from the proposition that silence does not constitute consent, absent a duty to speak. He cited the New York Court of Appeals for saying that silence operates as an estoppel "only when it has the effect to mislead."

Judge Bernstein disagreed with several New York and Delaware bankruptcy court decisions holding that non-voting creditors were deemed to consent to third party releases. He agreed, however, with other Delaware cases holding that third party releases only bound creditors who voted for the plan.

Explaining why he reached that conclusion, Judge Bernstein said that the debtors did not "identify" the source of the creditors' "duty to speak." Despite the warning in the disclosure statement that silence may equal consent, he said the debtors failed to show how the non-voting creditors' "silence was misleading or that it signified their consent."

Observing that the plan only provided a recovery of less than 3% for unsecured creditors, Judge Bernstein left the door open to the possibility of inferring consent if the dividend were meaningful.

Jurisdiction

Having decided that consent could not be implied, Judge Bernstein turned to the question of whether the court had jurisdiction and statutory authority to enjoin creditors' unasserted claims against third parties. Assuming there were jurisdiction, he said that third party releases "are proper only in rare and unique circumstances," citing *Deutsche Bank AG v. Metromedia Fiber Network, Inc. (In re Metromedia Fiber Network, Inc.)*, 416 F.3d 136 (2d Cir. 2005).

The debtors argued that the court had jurisdiction because claims against the third parties would give rise to indemnification obligations running in favor of officers, directors, employees and agents. Judge Bernstein conceded that potential indemnification claims would give rise to a "conceivable effect" on the estate, thus giving the court jurisdiction to enjoin.

However, he said, the proposed releases were "much broader than the indemnification obligations." He also said that the releases were not "limited to the potential indemnified parties listed by the debtors."

Consequently, Judge Bernstein said that the debtors "failed to sustain their burden of proving that the court has subject matter jurisdiction to approve the Release in its current form." He also said that the releases were not "appropriate" under *Metromedia*.

A Second Bite at the Apple

Judge Bernstein refused to approve the releases contained in the plan, but he gave the debtors 30 days to submit a new form.

Nonetheless, the new releases, Judge Bernstein said, "must specify the releasee by name or readily identifiable group and the claims to be released, demonstrate how the outcome of the claims to be released might have a conceivable effect on the debtors' estates, and show that this is one of the rare cases involving unique circumstances in which the release of the claims is appropriate under *Metromedia*."

The opinion is *In re SunEdison Inc.*, 576 B.R. 453 (Bankr. S.D.N.Y. Nov. 8, 2017).

Augie/Restivo ***problems are avoided by including opt-out provisions in a substantive consolidation chapter 11 plan.***

District Court Endorses Opt-Out to Confirm Substantive Consolidation Plans

District Judge J. Paul Oetken of Manhattan endorsed a structure for chapter 11 plans to allow substantive consolidation without running afoul of *In re Augie/Restivo Baking Co.*, 860 F.2d 515 (2d Cir. 1988), where the Second Circuit ruled that substantive consolidation is only proper when (1) creditors dealt with affiliates as a single economic unit and did not rely on their separate corporate entities, and (2) the debtors' affairs are so entwined that consolidation will benefit all creditors.

In his March 28 opinion, Judge Oetken cited the Second Circuit for saying that substantive consolidation must be used "sparingly" and cannot harm creditors, although there is no requirement that it benefit creditors.

The appeal involved a holding company and an airline subsidiary that confirmed a plan based on substantive consolidation. The appealing creditor was an aircraft lessor who had a lease claim against the airline and a guarantee claim against the holding company parent arising from rejection of an aircraft lease. As a result of peculiarities in state law, the lessor contended that the claim against the parent was more valuable.

Effectuating substantive consolidation, the plan eliminated all guarantee claims. To obviate objection, the plan allowed creditors to opt out of consolidation. By opting out, a creditor would retain both its lease and guarantee claims and would receive payments as though substantive consolidation had not occurred. The plan gave the debtors the burden of proving the distributions that the creditor would have received were there no consolidation.

Despite the opt-out offer, the creditor still objected and appealed the confirmation order. The debtor put money aside in case the creditor were to prevail on appeal.

The decision by Judge Oetken in substance endorses substantive consolidation plans with opt-out provisions designed to avoid *Augie/Restivo* infirmities. The judge said that the plan did not unfairly discriminate against the lessor under Section 1123(a)(4). He also held that the bankruptcy court properly analyzed the *Augie/Restivo* factors.

The opinion has an interesting wrinkle, however. Because the opt-out option "negated any prejudice," Judge Oetken said that the lessor lacked standing to challenge substantive consolidation "because it suffered no harm from substantive consolidation."

The opinion is *In re Republic Airways Holdings Inc.*, 17-3442 (S.D.N.Y. March 28, 2018).

Committees

Priority skipping permitted as part of final approval of DIP financing.

Delaware Judge Narrows *Jevic* to Prohibit Only End-of-Case Priority Skipping

Bankruptcy Judge Kevin Gross of Delaware read *Jevic* narrowly and approved final financing in chapter 11 with a payment for general unsecured creditors but none for unsecured creditors with unpaid administrative or priority claims.

Short Bark Industries Inc., a provider of body armor and apparel for the military, filed a chapter 11 petition in July, aiming for a quick sale of the assets. The company had about $17 million in secured debt, with almost $10 million owing to the senior secured lender.

After filing, the debtor landed a so-called stalking horse bid to sell the business for $3.2 million. The official creditors' committee objected to the proposed chapter 11 financing provided by the senior secured lender.

Subject to the court's approval, the lender and the committee settled their disputes over financing. The agreement called for the lender to hold a minimum of $110,000 in sale proceeds in escrow for payment to holders of general unsecured claims but not for holders of unpaid priority or administrative claims.

The U.S. Trustee and a creditor with a disputed priority claim objected to the settlement, based on *Czyzewski v. Jevic Holding Corp.*, 15-649, 2017 BL 89680, 85 U.S.L.W. 4115 (Sup. Ct. March 22, 2017), the Supreme Court decision barring structured dismissals that "deviate from the basic priority rules."

Ruling on the objection in an opinion delivered from the bench on Sept. 11, Judge Gross said he was initially inclined to disapprove the settlement, saying that the U.S. Trustee lodged a "very strong objection." The judge said he then reread *Jevic*, noting how "it was all about a structured settlement." He quoted Justice Stephen G. Breyer's opinion proscribing "end-of-case distributions" that "would be flatly impermissible in a chapter 7 liquidation."

Judge Gross characterized Justice Breyer as disapproving *Jevic*'s priority-skipping distribution because there was no "significant, offsetting, bankruptcy-related justification."

In contrast, Judge Gross said the settlement in *Short Bark* "enables the debtors to continue with their businesses . . . and the employment of 500 plus people, while preserving the committee's right to bring actions against insiders."

Judge Gross had been told that administrative claims would be paid by using the chapter 11 financing. He said there was "little, if any, assurance" that the creditor with the disputed priority claim "would receive any distribution, were the settlement to be denied."

The decision by Judge Gross appears to limit *Jevic* to a prohibition against priority-skipping distributions occurring at the end of the case, when it is clear that priority and administrative claims will not be paid. If his rationale holds up, settlements could avoid *Jevic*'s fate by being accelerated to an earlier time in the chapter 11 case.

If Judge Gross is reversed and priority-skipping settlements are barred at all stages of reorganization, chapter 11 may devolve into an exercise only for the benefit of secured creditors.

On the other hand, bankruptcy judges could largely, but not entirely, ensure compliance with the rules of priority by using early-stage, priority-skipping settlements combined with financing orders that guarantee payment of administrative claims, leaving only priority creditors with no assured recovery. For those overlooked creditors, perhaps estate claims could be carved out in a settlement for their benefit, but the effect would look much like a chapter 11 plan having less than full compliance with Section 1129.

In *Short Bark*, estate claims were not extinguished by the financing but were preserved, leaving the possibility that priority claimants could receive proceeds from successful suits either in a chapter 11 plan or a distribution in a subsequent chapter 7 case.

If there is a flaw in *Short Bark's* logic in relation to *Jevic*, perhaps it's because the proposed financing assured the ability to continue the business and the committee's objection to financing wouldn't necessarily be fatal were there no settlement.

Justice Breyer explicitly allowed first day orders departing from the rules of priority, such as authorizations to pay prepetition wages and claims of so-called critical vendors that are designed to continue the business as a going concern. If there is an appeal, *Short Bark* will raise the question of whether priority skipping somewhat later in the case is permissible if structures are already in place assuring continuation of the business long enough to sell the assets.

For bankruptcy judges, the choice is difficult. Should they impose the Bankruptcy Code priority rules stringently, or allow an outcome that benefits the largest numbers of creditors?

In *Short Bark*, the creditors' committee was represented by Lowenstein Sandler LLP.

The opinion is *In re Short Bark Industries Inc.*, 17-11502 (Bankr. D. Del. Sept. 11, 2017).

Allowing intervention as of right, First Circuit repudiates its own prior authority as 'pure dicta.'

First Circuit Widens a Circuit Split on a Committee's Intervention Rights

Ruling on an expedited appeal involving Puerto Rico's debt restructuring, the First Circuit took sides in a circuit split and held that an official creditors' committee has an unqualified right to intervene in an adversary proceeding under F.R.C.P. 24(a)(1).

Immediately after Puerto Rico began the courtroom phase of its debt restructuring under the Puerto Rico Oversight, Management, and Economic Stability Act, or PROMESA (48 U.S.C. §§ 2161 *et. seq.*), several bond insurers initiated an adversary proceeding contending that Puerto Rico's fiscal plan violates PROMESA and the federal Constitution.

The official creditors' committee filed a motion to intervene, which the district court denied on Aug. 10.

Reversing on Sept. 22, Chief Circuit Judge Jeffrey R. Howard said that the "able district court" understandably rested her decision "exclusively" on a footnote in *Kowal v. Malkemus (In re Thompson)*, 965 F.2d 1136, 1142 n.8 (1st Cir. 1992), which says that Section 1109(b) of the Bankruptcy Code "does not afford a right to intervene under Rule 24(a)(1)."

Section 1109(b) provides that a creditors' committee "may raise and may appear and be heard on any issue in a case under this chapter." That section is among many provisions of the Bankruptcy Code incorporated into PROMESA.

Judge Howard said the footnote did not even involve a chapter 11 case and was "pure *dicta*" not binding on the circuit court.

Judge Howard said that *Thompson* relied primarily on a 1985 Fifth Circuit opinion holding that Section 1109(b) did not give a committee a right of intervention in an adversary proceeding. Two other circuits, he said, agreed with the Fifth Circuit in *dicta*.

Later, Judge Howard said, the Second and Third Circuits rejected the Fifth Circuit's approach by holding that Section 1109(b) bestows a committee with a statutory right of intervention under Rule 24(a)(1).

Not bound by *Thompson*, Judge Howard looked afresh at Section 1109(b) and observed that the language was "quite broad" by giving a committee intervention rights "on any issue in a case." Following the *Collier* treatise, he said that "any issue" subsumes adversary proceedings.

Although holding that Section 1109(b) grants a committee unconditional intervention rights, the section does not "dictate the scope of that participation," he said.

Because the district court had not reached the scope question, Judge Howard remanded the case with instructions to consider the extent of the committee's participation in the adversary proceeding. However, he said that the committee's own recommendations about limited participation "fit comfortably" within rules laid down by other courts.

The opinion is *Official Committee of Unsecured Creditors v. Assured Guaranty Corp. (In re Financial Oversight and Management Board for Puerto Rico)*, 872 F.3d 57 (1st Cir. Sept. 22, 2017).

The statute is tolled only if the creditors' committee is denied standing to sue.

Existence of a Committee Precludes Tolling the Statute for Adverse Domination

The mere existence of a creditors' committee will prevent a later trustee from invoking the doctrine of adverse domination to toll the statute of limitations, according to the Seventh Circuit.

A committee must seek and be denied the right to sue in the name of the debtor before a statute of limitations will be tolled, Circuit Judge Michael S. Kanne said in his Aug. 11 opinion.

A casino began reorganizing in 2001 when the state was in the process of revoking its gaming license. The case converted to chapter 7 in 2007, and a trustee was appointed, when revocation of the license became final. The trustee then sued officers and directors for breach of fiduciary duty and breach of contract for alleged misconduct that prompted the state to terminate the gaming license.

Relying on the state's five-year statute of limitations, the district court dismissed the fiduciary duty claims. The trustee appealed, unsuccessfully.

The trustee argued that the Illinois doctrine of adverse domination tolled the statute of limitations because the debtor in possession was not motivated to sue its own officers and directors. The existence of the chapter 11 creditors' committee doomed the argument.

The trustee noted that the committee could not sue without permission from the bankruptcy court. Judge Kanne rejected the notion that the committee was unable to sue. Although the ability to sue was "circumscribed by several requirements" such as court approval, he said "those limitations didn't render the Creditors' Committee unable to sue." In other words, "the mere existence of a potential barrier to suing did not negate the Creditors' Committee's ability 'to enforce a corporate cause of action against officers, directors, and third parties.'"

Judge Kanne said the committee would be seen as "unable to bring the claim" only "[i]f the Creditors' Committee had petitioned the bankruptcy court, and if the court had denied leave."

In a last attempt at invoking adverse domination, the trustee contended that the committee was not motivated to sue because the prospect of reorganizing in chapter 11 was more promising than suing officers and directors. Judge Kanne responded by saying that the committee "made a strategic decision not to sue." Potential plaintiffs, he said, "must live with their choice. A plaintiff

did not lack motivation to sue just because its chosen course of action proved to be unsuccessful in the end."

However, the trustee did not emerge empty-handed from the Seventh Circuit. The appeals court not only upheld a $272 million breach of contract claim against the officers and directors, but the court also ruled that the defendants should have been jointly and severally liable, not merely severally liable. In addition, the trustee had already settled with a pair of defendants for $45 million.

The opinion is *Gecker v. Estate of Flynn (In re Emerald Casino Inc.)*, 867 F.3d 743 (7th Cir. Aug. 11, 2017); rehearing and rehearing *en banc* denied Oct. 2, 2017.

Stays & Injunctions

Circuits are split on whether inaction is an ‘act’ that violates the automatic stay.

Tenth Circuit Direct Appeal to Decide Whether the Automatic Stay Is Really Automatic

The Tenth Circuit has just granted a direct appeal involving a deepening split where a minority of two circuits held that the automatic stay is not automatic.

In *WD Equipment v. Cowen (In re Cowen)*, 849 F.3d 943 (10th Cir. Feb. 27, 2017), the Tenth Circuit held that passively holding an asset of the estate, in the face of a demand for turnover, does not violate the automatic stay in Section 362(a)(3) as an act to “exercise control over property of the estate.” *Cowen* was important, because it means that debtors in chapters 7, 11, 12 and 13 cannot recover their repossessed vehicles in six states without mounting a turnover action. It also means that businesses in chapter 11 cannot immediately resume operations if property was repossessed before filing.

In substance, the Tenth Circuit held that the automatic stay is not really automatic. Latching onto the words “any act” in Section 362(a)(3), the appeals court held that inaction is not an act and thus cannot violate the automatic stay.

The Tenth Circuit in *Cowen* sided with the D.C. Circuit. The Second, Seventh, Eighth, Ninth and Eleventh Circuits hold the opposite, having ruled that a lender or owner must turn over repossessed property immediately or face a contempt citation.

The case being directly appealed to the Tenth Circuit is *Davis v. Tyson Prepared Foods Inc. (In re Garcia)*, 17-5006, 2017 BL 235622 (Bankr. D. Kan. July 7, 2017), decided in July by Bankruptcy Judge Robert E. Nugent of Wichita, Kan. Forced to rule contrary to two prior decisions of his own, Judge Nugent reluctantly held that the automatic stay did not prevent a statutory worker’s compensation lien from attaching automatically after bankruptcy to a recovery in a lawsuit. In other words, the lien attached to after-acquired property despite the policy evident in Section 552(a).

The chapter 13 trustee in *Garcia* appealed and obtained a certification of direct appeal from the district court without opposition. On Nov. 20, the Tenth Circuit granted a direct appeal.

The trustee’s petition for direct appeal said that *Cowen* “deepened an existing split in the Circuit Courts” and “has been criticized by a bankruptcy court and commentators.” The trustee cited the American Bankruptcy Institute among those who criticized *Cowen*.

The trustee in *Garcia* may mount a frontal assault on *Cowen*, but the upcoming three-judge panel in the Tenth Circuit might attempt to narrow *Cowen*. To the extent that the three judges rely on *Cowen*, they nonetheless will have laid the groundwork for an *en banc* rehearing to set aside *Cowen* entirely.

Preferably, the Tenth Circuit should address *Cowen en banc*, because attempting to narrow *Cowen* will result in increased complexity and a lack of predictability in how the Tenth Circuit might rule under slightly different circumstances.

To read ABI's discussion of *Cowen* and *Garcia*, click here and here.

The direct appeal is *Davis v. Tyson Prepared Foods Inc. (In re Garcia), (*10th Cir. 17-3247); argument Sept. 26, 2018.

Compensation

Baker Botts v. ASARCO ***doesn't prohibit retention agreements allowing fees for defense of fees, judge holds.***

Retention Agreements Allowing Defense Fees Ok in New Mexico, but Not in Delaware

A company planning a contentious reorganization should consider filing chapter 11 in Albuquerque, N.M., because a judge there will permit retention agreements allowing compensation for successful defense of professionals' fee applications.

An oil field contractor with about $5.5 million in assets and liabilities filed a chapter 11 petition and sought authority to retain counsel under an engagement agreement that included compensation for successful defense of the attorneys' fee applications. The U.S. Trustee and the creditors' committee objected to the fee-defense provision, citing *Baker Botts LLP v. Asarco LLC*, 135 S. Ct. 2158, 192 L. Ed. 2d 208, 83 U.S.L.W. 4428 (2015), and *In re Boomerang Tube Inc.*, 548 B.R. 69 (Bankr. D. Del. 2016).

In his Sept. 20 opinion, Bankruptcy Judge David T. Thuma analyzed whether *ASARCO*, which disallowed defense fees under Section 330(a)(1), also precludes the inclusion of a fee-defense provision in a retention agreement under Section 328(a). He concluded, "*ASARCO* does not hold that a fee defense provision can never be a 'reasonable term' under Section 328(a)."

ASARCO involved a case where the bankruptcy court awarded debtor's counsel $5.2 million for successfully defending its fees. The lawyers' retention was under Section 327, and the allowance of fees was governed entirely by Section 330, because the attorneys had no agreement with the debtor for payment of defense fees that might bring the case under the umbrella of Section 328.

Judge Thuma parsed *ASARCO*, a 6/3 decision, and found that Justice Clarence Thomas disallowed defense fees because the "services" benefitted only the lawyers, not the estate.

Next, Judge Thuma analyzed *Boomerang*, where Delaware Bankruptcy Judge Mary F. Walrath refused to approve a retention application requiring the debtor to compensate committee professionals for successfully defending their fees. She barred the use of Section 328 as a vehicle for paying defense costs because it, like Section 330(a), was not a "specific and explicit statute" overriding the American Rule against fee-shifting. Section 328 permits the court to approve retentions "on any reasonable terms and conditions of employment."

The *Boomerang* committee contended that the engagement agreement fell under the so-called contract exception to the American Rule, allowing parties by contract to agree that the losing side

pays everyone's lawyers. The argument was flawed, Judge Walrath said, because the debtor was not a party to the retention agreement. Even if the contract exception applied, Judge Walrath said she could not approve it because fee-defense costs would not entail any services for the committee, only benefit the lawyers themselves.

Judge Thuma disagreed with *Boomerang*. If the terms of employment have been approved by the court under Section 328(a), he said that the "professional's compensation is governed by those terms and conditions, rather than the general [reasonable compensation] language of Section 330(a)(1)(A)."

Judge Thuma noted that *ASARCO* did not involve a fee-defense provision in a retention agreement approved under Section 328(a). He then analyzed whether defense costs can be a "reasonable" term of employment.

Reasonable employment terms are not only those that benefit the client. Retention agreements, he said, will contain many provisions that benefit the lawyers as well. Even provisions that benefit lawyers also provide indirect benefit for the client because "the client obtains the services of needed, able professionals," Judge Thuma said.

Pre-*ASARCO*, Judge Thuma said that the experience in his district in paying successful defense costs had "been good for the most part," because "objections to fee applications have been limited to *bona fide* disputes, and the fee defense costs have been reasonable."

Unless *ASARCO* requires it, Judge Thuma said there "is no need to change the system," which "has worked pretty well." He did not read *ASARCO* "as mandating a change, if a properly drafted employment term is timely presented to the court and approved under Section 328(a)."

Judge Thuma ended his opinion by laying down criteria under which he would approve defense costs. Among other things, the debtor must approve them, committee counsel must be similarly protected, and fees will not be allowed for an unsuccessful defense.

The opinion is *In re Hungry Horse LLC*, 574 B.R. 740 (Bankr. D.N.M. Sept. 20, 2017).

Texas court shows antipathy to all theories seeking allowance of fees incurred in collecting fees.

ASARCO Read to Bar Fee-Defense Costs Even with a Fee-Shifting Agreement

In the wake of the Supreme Court's *ASARCO* opinion, a retained professional has virtually no chance of enforcing even a court-approved fee-shifting agreement, assuming that a decision from a district judge in Austin, Texas, was correct in upholding the denial of fees incurred in collecting fees.

The bankruptcy court approved a chapter 11 debtor's retention of an investment banker. The engagement agreement included a success fee and provided that if the success fee "is not fully paid when due," the debtor agreed "to pay all costs of collection . . . including but not limited to attorney's fees and expenses . . . ."

The debtor argued that the debt-for-equity conversion in the plan did not entitle the banker to a success fee. After the plan's effective date, the bankruptcy court disagreed and allowed the banker a $595,000 success fee. The debtor appealed but lost in both the district court and the Fifth Circuit.

After the bankruptcy court allowed the success fee, the banker moved in bankruptcy court under the fee-shifting agreement for payment of almost $200,000 in counsel fees incurred in establishing the right to collect the success fee. Bankruptcy Judge Craig A. Gargotta denied reimbursement of counsel fees.

Even though the fee-shifting agreement seemed on its face to entitle the banker to the recovery of counsel fees incurred in establishing a right to the success fee, District Judge Lee Yeakel wrote an opinion on Oct. 10 upholding Judge Gargotta on several independent grounds.

Although the bankruptcy court approved retention of the banker, Judge Yeakel ruled that the bankruptcy court must also approve attorneys hired by a court-approved professional. Since the banker's attorneys were not themselves retained with court approval, Judge Yeakel said that the banker's "claims for reimbursement of its attorney's fees and costs were properly denied."

Judge Yeakel also broadly interpreted *Baker Botts LLP v. Asarco LLC*, 135 S. Ct. 2158, 192 L. Ed. 2d 208, 83 U.S.L.W. 4428 (2015), which he construed as holding that a bankrupt estate is not responsible for a professional's time "spent litigating a fee application against the debtor in possession."

The banker argued that *ASARCO* did not apply because there was a "prevailing-party fee-shifting provision."

Judge Yeakel disagreed. The bankruptcy court properly denied reimbursement because the banker's attorney's fees and costs, "like those in *ASARCO*, were not incurred for labor performed for, or in service to," the debtor.

The result is not far removed from *In re Boomerang Tube Inc.*, 548 B.R. 69 (Bankr. D. Del. 2016), where Delaware Bankruptcy Judge Mary F. Walrath refused to approve a retention application requiring the debtor to compensate committee professionals for successfully defending their fees. In that respect, keep in mind that the bankruptcy court in the case at bar had approved fee-defense costs two years before the Supreme Court decided *ASARCO*. It is therefore questionable whether the bankruptcy court would have approved a fee-shifting agreement if *ASARCO* had already been on the books.

Judge Yeakel's decision may presage an attitude in the courts that fee-defense costs in bankruptcy will rarely if ever be reimbursed, even with a fee-shifting agreement.

The confirmed chapter 11 plan also preluded payment of the attorney's fees, according to Judge Yeakel. He focused on language in the fee-shifting agreement calling for reimbursement of the success fee were it "not fully paid when due."

The plan provided that claims would be paid on entry of a "final order," which was defined as an order no longer subject to appeal. Since the debtor promptly paid the success fee after it was upheld in the Fifth Circuit, there was no delay in payment and thus no right to recovery of attorney's fees.

The plan also included a bar date, four months after the effective date of the plan, for the filing of claims for administrative expenses. Since the bankruptcy court did not allow the claim for the success fee until after the bar date, the banker's claim for attorney's fees was untimely, Judge Yeakel said, because there were "no provisions in the plan requiring [the debtor] to pay administrative expenses that occur after the bar date."

The opinion is *Roth Capital Partners LLC v. Valence Technology Inc. (In re Valence Technology Inc.)*, 14-0949, 2017 BL 363805 (W.D. Tex. Oct. 10, 2017).

Fraudulent Transfers

Ninth Circuit criticizes the Seventh for making the sovereign immunity waiver meaningless for Section 544(b)(1) suits.

Ninth Circuit Splits with Seventh on Sovereign Immunity and Derivative Suits by a Trustee

The Ninth Circuit created a split of circuits with the Seventh by holding that the waiver of sovereign immunity under Section 106(a)(1) enables a trustee to file a derivative suit against the Internal Revenue Service for receipt of a fraudulent transfer under Section 544(b)(1).

The issue is important because the outcome determines whether a trustee can ever mount a fraudulent transfer action under state law against governmental units, in this case the IRS.

"Before the Seventh Circuit's opinion, the bankruptcy courts were unanimous in their conclusion that 106 fully waives sovereign immunity under 544(b) — hopefully the Ninth Circuit will reassure them that was the right result," Prof. Stephen J. Lubben of Seton Hall University School of Law told ABI in an email. In support of the trustee, Prof. Lubben submitted an *amicus* brief for the National Association of Bankruptcy Trustees.

The Facts

Operated as a Ponzi scheme, the debtor was a so-called subchapter S corporation that paid the IRS about $17 million on account of taxes owing by its shareholders. Under a confirmed chapter 11 plan, the trustee for a creditors' trust sued the IRS to recover the payments.

The IRS conceded that it was liable under Section 548(a)(1)(B) for receipt of fraudulent transfers amounting to about $56,000 made within two years of bankruptcy. The government acknowledged that the waiver of sovereign immunity made the IRS subject to suit for fraudulent transfer within the ambit of the Bankruptcy Code.

To recover the remainder of the $17 million, the trustee also sued under Idaho's version of the Uniform Fraudulent Transfer Act, invoking Section 544(b)(1), which requires the existence of an actual, unsecured creditor who could have sued under state law. The trustee relied on Section 544(b) because Idaho law has a four-year statute of limitations, compared with only two years under the Bankruptcy Code.

The government filed a motion for summary judgment on the Section 544(b)(1) claim, because any creditor would have been barred by sovereign immunity from suing the government for receipt of a fraudulent transfer. The district court granted the trustee's cross motion for summary

judgment, holding that Section 106(a)(1) waived sovereign immunity for derivative fraudulent transfer claims brought under Section 544(b)(1).

Section 106(a)(1) provides that "sovereign immunity is abrogated as to a governmental unit . . . with respect to" Section 544, among others.

The Ninth and Seventh Circuits Split

Upholding the district court in an Aug. 31 opinion by Circuit Judge Richard Z. Paez, the Ninth Circuit held that the Section 106 waiver permits suits under Section 544(b)(1), in the process creating a split of circuits with the Seventh Circuit in *In re Equipment Acquisition Resources Inc.*, 742 F.3d 743 (7th Cir. 2014).

In *EAR*, the Chicago-based court held that the waiver of immunity does not extend to Section 544(b)(1) suits because any actual creditor would have been barred from suing by the government's sovereign immunity. Judge Paez said he could find no other circuit decisions on the question.

Plain Language, Logic and Equity

Judge Paez relied on logic and the language of the statute, in particular the phrases in Section 544(b)(1) that allow a trustee to "avoid any transfer" that is "voidable under applicable law." He said that Section 544(b)(1) "does not exist in a vacuum; rather, it must be read in concert with other sections of the Bankruptcy Code," such as Section 106(a)(1), which "unambiguously abrogates the federal government's sovereign immunity 'with respect to Section 544.'"

Reading the two sections together, Judge Paez said that the abrogation of sovereign immunity is "absolute" and "thus necessarily includes the derivative state law claim on which a Section 544(b)(1) claim is based."

In terms of logic, Judge Paez said that the government's argument "would essentially nullify Section 106(a)(1)'s effect on Section 544(b)(1), an interpretation we should avoid." He also said, "It would defy logic to waive sovereign immunity as to a claim which could not be brought against the government."

Differing with the Seventh Circuit, Judge Paez appealed to a sense of equity. The Bankruptcy Code, he said, was drafted to put the IRS "on an equal footing with all other creditors." He said "it would be unfair for the governmental unit to participate in the distributions in a bankruptcy case while at the same time shielding itself from liability," quoting the Tenth Circuit from *In re Franklin Savings Corp.*, 385 F.3d 1279, 1290 (10th Cir. 2004).

Saying that the waiver of immunity applies, Judge Paez held that "a trustee need only identify an unsecured creditor, who, but for sovereign immunity, could bring an avoidance action against the IRS."

The Second Issue

The case involved another issue. In a separate, nonprecedential opinion, the Ninth Circuit remanded that facet of the case to the district court.

From the $17 million found to be avoidable, the district court had held that the trustee could not recover $3.6 million that the IRS had refunded to shareholders before bankruptcy as overpayment of taxes.

In the separate *per curiam* opinion, the appeals court said that the trustee's appeal from that feature of the lower court's decision turned on whether the IRS was an initial transferee under Section 550(a)(1). The circuit remanded because the district court had employed the "control test" rather than the Ninth Circuit's "more restrictive dominion test."

The opinions are *Zazzali v. U.S. (In re DBSI Inc.)*, 869 F.3d 1004 (9th Cir. Aug. 31, 2017).

Split decision refuses to invoke 'equity' to override a policy choice made by Congress.

In a Circuit Split, Ninth Circuit Tags Innocent Sellers with Fraudulent Transfer Liability

Should an innocent seller who gave full value be caught in the trap of a fraudulent transfer laid by someone who is defrauding the company he owns?

Siding with the Seventh Circuit and disagreeing with other courts of appeals, a split panel on the Ninth Circuit decided that Congress already made the policy decision and barred a seller from raising the good faith defense available to a subsequent transferee because the fraudster had kept the misappropriated money in a company account.

The owner of a business maintained a secret bank account in the company's name but under his control. Over the years, he diverted $8 million of his company's income into the account, which he used to pay personal and non-company expenses.

After the business went bankrupt, the trustee filed fraudulent transfer suits against 130 people or entities that received money from the secret account. In a test case, the bankruptcy judge dismissed a suit against a couple who sold real property to the owner in return for $220,000 from the secret account. The trustee alleged that the sellers received a constructively fraudulent transfer of $220,000 under Section 548(a)(1)(B) because the company, whose money paid the purchase price, received none of the consideration.

The bankruptcy court believed that the fraudster was the initial recipient of the fraudulent transfer, allowing the sellers to be subsequent transferees entitled to raise the defense of good faith under Section 550(b)(1) because they did not know there was fraud afoot.

The district court reversed in July 2015, ruling that the sellers were the initial transferees, making them ineligible for the good faith defense.

The majority on the court of appeals reached the same conclusion on Aug. 2 in an opinion authored by District Judge Algenon L. Marbley, sitting by designation from the Southern District of Ohio. Circuit Judge Jacqueline H. Nguyen dissented.

The majority opinion allocates the risk of fraud to the seemingly innocent sellers because they, as parties to the transfer, "generally stand in a better position to guard against corporate fraud than do unsuspecting creditors" not in a position to know that the money paying a personal expense came from a corporate account.

Section 550(b) is structured to give the good faith defense to subsequent transferees, but not to the initial transferee. On appeal, the sellers contended that they were subsequent transferees eligible for the defense because the fraudster should be viewed as the initial transferee. The decision in the circuit court therefore turned on the attributes of an initial transferee.

Judge Marbley said that the Ninth Circuit decided in 2006 to follow the Seventh Circuit by adopting the stricter "dominion test," rather than the more lenient "control test" employed, for instance, in the Eleventh Circuit. The question is a matter of federal common law because the Bankruptcy Code does not define "initial transferee" as used in Section 550(a)(1).

According to Judge Marbley, the dominion test focuses on who has legal title. He said that the control test "involves a more gestalt analysis" focusing on "'who truly had control of the money.'"

In the context of an insider, Judge Marbley said that the majority of courts hold that a principal who misappropriates company funds to pay a personal obligation is not an initial transferee. To become the initial transferee, the fraudster must first transfer the money to a personal account, which did not occur in the case at bar because the funds were always held in an account bearing the company's name and tax identification number.

Making the fraudster the initial transferee "both misallocates the monitoring costs that Section 550 sought to impose and deprives the trustee" of potential recoveries, Judge Marbley said. In his view, the minority draw "largely on equitable principles and a concern that seemingly 'innocent' third parties will be held liable for fraudulent transfers."

Judge Marbley declined to make a policy decision based on equitable principles "because Congress already performed that task." He ended by saying that the majority's decision would not let the fraudster off "scot-free" because he remains strictly liable under Section 550(a)(1) as the person "for whose benefit" the initial transfer was made.

Judge Nguyen began her dissent by saying, "There is nothing equitable about today's decision." She called on her circuit to sit *en banc*, repudiate the dominion test, and adopt the "control test used successfully in other circuits."

Even employing the dominion test, Judge Nguyen disagreed. Characterizing the facts, she would have found that "the sham account never belonged" to the company because the fraudster "was acting adversely to [the company] in opening the sham account, [and] he did so in his personal capacity, not as an officer of the company."

Don't be surprised if there is a petition for rehearing *en banc*, and don't be surprised if the petition is granted. But don't hold your breath. It could be two years before there is an opinion *en banc*.

The opinion is *Henry v. Official Committee of Unsecured Creditors (In re Walldesign Inc.)*, 872 F.3d 954 (9th Cir. Oct. 2, 2017).

Venezuela let off the hook for expropriating assets.

Third Circuit Narrowly Interprets Delaware Fraudulent Transfer Law

A transfer by a non-debtor cannot be a fraudulent transfer, according to the majority on a Third Circuit panel interpreting Delaware's version of the Uniform Fraudulent Transfer Act.

The case arose from Venezuela's expropriation of mining assets worth billions. The dissenter said he was "hard-pressed to conceive of a scenario more worthy of a trial court's invocation of equitable powers under the Fraudulent Transfer Act."

The Venezuelan Expropriation

The government of former Venezuelan President Hugo Chavez expropriated a gold mine belonging to the plaintiff, a Canadian gold producer. Venezuelan government-owned Petroleos de Venezuela SA, or PDVSA, became the owner of the gold mine after expropriation. PDVSA later sold a 40% interest in the mine to the Venezuelan central bank for $9.5 billion.

In the World Bank, the plaintiff won a $1.2 billion arbitration award against Venezuela. The Venezuelan government was the only defendant in the arbitration. A federal district court in Washington confirmed the award.

President Chavez vowed publicly that his government would never pay that award nor others resulting from numerous expropriations. To ensure that the arbitration awards could not be enforced, Venezuela took steps to protect its assets in the U.S.

One of the assets was the Citgo oil refining and marketing business in the U.S. PDVSA was Citgo's indirect, ultimate owner. The plaintiff could not sue or collect from PDVSA, a foreign sovereign protected by the Foreign Sovereign Immunities Act.

To frustrate the collection of judgments in the U.S., the Citgo holding company sold $2.8 billion in debt. The holding company then made a $2.8 billion dividend to PDVSA to remove the proceeds from the U.S. and put them beyond the reach of judgment creditors. The transaction allegedly left the Citgo operating company insolvent and with a negative shareholders' equity.

Although unable to sue PDVSA, the plaintiff could sue Citgo's direct parent, a Delaware holding company. Therefore, the plaintiff sued the Citgo holding company in Delaware district court, alleging that the dividend and the subsequent transfers were fraudulent transfers under state law.

The holding company moved to dismiss the Delaware suit, contending there was no fraudulent transfer claim because it was not a debtor liable to the plaintiff on the arbitration award. Although conceding that the Venezuelan government and its alter ego PDVSA were the only debtors, the district court nonetheless denied the motion, believing that a non-debtor could be liable under the Delaware UFTA.

The district court certified the decision for interlocutory appeal to the Third Circuit.

The Majority Opinion

Reversing in an opinion on Jan. 3, Circuit Judge Marjorie O. Rendell wrote for herself and Circuit Judge Thomas I. Vanaskie, saying that her task was to guess how the Delaware Supreme Court would rule.

Judge Rendell said there are three elements to a fraudulent transfer claim: (1) a transfer, (2) by a debtor, (3) with actual intent to hinder, delay or defraud. She said there was no authority from Delaware's highest court saying whether a transfer by a non-debtor could sustain an UFTA claim.

Judge Rendell therefore relied on a Delaware Chancery Court decision for the proposition that "transfers by non-debtors are not fraudulent transfers under" the Delaware UFTA. She placed significance on the plaintiff's failure to allege that the Delaware holding company was liable for the arbitration award. The transfer, she said, was a transfer to a debtor (Venezuela), not a transfer by a debtor.

Making the Delaware company liable, Judge Rendell said, would "undermine a fundamental precept of Delaware corporate law: parent and subsidiary corporations are separate legal entities." She recounted how the plaintiff alleged that PDVSA was Venezuela's alter ego but did not contend that the Delaware holding company was an alter ego or provide "any other basis" to pierce the corporate veil.

Judge Rendell also said that Delaware courts have rejected the idea that there can be liability for aiding and abetting a fraudulent transfer. Similarly, she said, Delaware courts permit suits only against debtors, "thereby shielding advisors from liability."

The Dissent

Circuit Judge Julio M. Fuentes dissented. "[I]t cannot be," he said, that the UFTA, "which is firmly grounded in principles of equity," can leave "the victim of a purposeful and complicated fraud . . . without a remedy" for the holding company's "role in transferring $2.8 billion out of the U.S. to avoid Venezuela's creditors."

Beyond notions of equity, Judge Fuentes said that the transactions were indirect transfers that are voidable under UFTA. He also argued that the Chancery Court decision, relied on by the majority, did not hold that only debtors can be liable. That case, he said, dealt with aiding and abetting claims. "[I]t does not appear that the Delaware courts have ever held that non-debtor transferors are immune from liability under the Act."

Furthermore, Judge Fuentes did not interpret the complaint as alleging aiding and abetting liability. The plaintiff, he said, contended that the Delaware holding company "directly participated in the fraudulent scheme."

Because the majority and the dissent disagree about Delaware law, perhaps the Third Circuit should certify a question to the Delaware Supreme Court if there is a motion for rehearing. Even so, the case is a good example of how hard cases can make bad law.

Rather than attempting to stretch Delaware law, the plaintiff might have crafted a more creative complaint or, as the majority said, try to show that the holding company is Venezuela's alter ego.

The opinion is *Crystallex International Corp. v. Petroleos de Venezuela SA*, 879 F.3d 79 (3d Cir. Jan. 3, 2018).

Delaware district and bankruptcy judges now disagree with the Second Circuit's holding that the federal safe harbor preempts state fraudulent transfer law.

Delaware District Judge Seemingly Splits with Second Circuit on the Safe Harbor

For all practical purposes, District Judge Leonard P. Stark of Delaware has ratified an opinion from June 2016 where Bankruptcy Judge Kevin Gross disagreed with the Second Circuit and held that the safe harbor in Section 546(e) does not bar fraudulent transfer claims brought on behalf of creditors under state law.

In *Note Holders v. Large Private Beneficial Owners (In re Tribune Co.)*, 818 F.3d 98 (2d Cir. 2016), the Second Circuit found no loopholes in Section 546(e) and went so far as to say that the safe harbor bars suits by creditors under state law to recover payments made in securities transactions.

Saying that Second Circuit authority in *Tribune* was not binding on him, Judge Gross adopted the rationale taken by former Bankruptcy Judge Robert E. Gerber of Manhattan in *Lyondell Chemical Co.*, 503 B.R. 348 (S.D.N.Y. 2014), where he held that the safe harbor only bars trustees from suing, not creditors from asserting claims of their own.

Judge Gross's opinion was *PAH Litigation Trust v. Water Street Healthcare Partners LP (In re Physiotherapy Holdings Inc.)*, 2016 WL 3611831, 15-ap-51238 (Bankr. D. Del. June 20, 2016). The defendants filed a motion to allow an interlocutory appeal and for a direct appeal to the Third Circuit, contending that the case raised a dispositive issue of law as to which there is evident disagreement.

In an opinion on Dec. 21, Judge Stark denied both a direct appeal and the motion to allow an interlocutory appeal, saying in the process that Judge Gross had founded his opinion on "well-established Third Circuit and Supreme Court law." While pointing out important factual distinctions between *PAH* and *Tribune*, Judge Stark went almost as far as saying that the Second Circuit was wrong about federal preemption of state fraudulent transfer law, at least in cases involving the leveraged buyout of a nonpublic company.

The PAH Facts

Physiotherapy Holdings Inc. filed under chapter 11 not long after being acquired in a leveraged buyout. After confirmation of a plan, the litigation trust filed suit against the controlling shareholders to recover almost $250 million they received by selling their stock in the LBO.

To form the backbone of the suit, pre-LBO senior noteholders assigned their claims to the litigation trust. Asserting claims under both Section 548 and parallel provisions in Pennsylvania's Fraudulent Transfer Act, the complaint alleged that the LBO was both a constructive fraudulent transfer and a fraudulent transfer with "actual intent."

Significantly, the complaint alleged that the defendants were not innocent selling shareholders. The trust alleged that the controlling shareholders knew the company was issuing false financial statements grossly overstating net income, thus enticing the purchaser to acquire and pay more for the company.

The selling shareholders filed a motion to dismiss. Holding that the Section 546(e) safe harbor was not applicable, Judge Gross denied the motion with respect to the actual fraud claim under Section 548(a)(1)(A) and the senior noteholders' constructive fraud claim under state law. However, he held that the safe harbor was applicable and did dismiss the claims for constructive fraudulent transfers under Section 548(a)(1)(B) and the trustee's claims for actual and constructive fraudulent transfers under state law.

To read ABI's discussion of Judge Gross's decision, explaining why he followed *Lyondell* while rejecting *Tribune*, click here.

Judge Stark Agrees with Judge Gross

Judge Stark laid out the standards for allowing interlocutory and direct appeals to the circuit, under 28 U.S.C. §§ 158(d)(2)(A) and 1292(b). He said that the standards for certifying a direct appeal and granting leave to appeal are "essentially the same." In either instance, there must be "genuine doubt as to the correct legal standard."

Tribune, the authority that Judge Gross rejected, "determined that Section 546(e) preempts state fraudulent transfer law," Judge Stark said.

He said that the defendants' reliance on *Tribune* "ignores the fact that the Bankruptcy Court's [ruling that Section 546(e) did not preempt state law] turned on facts specific to this case," such as the absence of any ripple effect on the markets because the selling shareholders were transferring stock in a non-pubic company. The bankruptcy court also placed reliance on allegations that the selling shareholders "acted in bad faith."

Judge Stark came close to an outright affirmance when he said that Judge Gross's "preemption analysis followed well-established Third Circuit and Supreme Court law."

Summarizing why he was denying an interlocutory and direct appeal and sounding as though he would affirm on the merits, Judge Stark said that the "bankruptcy court's reading of the safe

harbor is supported by the plain language of the statute, and its careful analysis followed controlling Third Circuit and Supreme Court precedent."

In the *PAH* suit, discovery will end and dispositive motions will be due in June 2018. Judge Stark's opinion increases the likelihood that the parties will settle. If that occurs, Judge Stark's opinion may be cited as tantamount to an affirmance.

The opinion is *PAH Litigation Trust v. Water Street Healthcare Partners LP (In re Physiotherapy Holdings Inc.)*, 16-misc-201, 2017 BL 457367 (D. Del. Dec. 21, 2017).

***Delaware's Judge Gross pens another controversial opinion in* PAH Litigation Trust.**

Fraudulent Transfer Claims Aren't Capped by Creditors' Losses

Bankruptcy Judge Kevin Gross of Delaware is back in the news with another important opinion in post-confirmation fraudulent transfer litigation involving Physiotherapy Holdings Inc. His new decision stands for the proposition that creditors who take stock in a reorganized company are entitled to recover more than the principal amount of their claims through successful post-confirmation prosecution of a fraudulent transfer action.

In June 2016, Judge Gross denied the defendants' motion to dismiss and disagreed with *Note Holders v. Large Private Beneficial Owners (In re Tribune Co.*), 818 F.3d 98 (2d Cir. 2016), where the Second Circuit expansively read the safe harbor in Section 546(e) to impliedly preempt state law and bar creditors from pursuing their own fraudulent transfer claims.

In a follow-up decision on Nov. 1 in the same lawsuit, Judge Gross handed the defendants another defeat by holding that recovery on fraudulent transfer claims is not capped by the amount of creditors' claims under a chapter 11 plan.

The Busted LBO

The *Physiotherapy* reorganization involved a typical leveraged buyout gone sour. Barely a year after the LBO closed, the company defaulted on $210 million in senior unsecured notes that had been sold to finance the acquisition. Although the noteholders were owed $237 million with accrued interest at the time of confirmation, the prepackaged plan gave them an allowed unsecured claim of $210 million, for which they received new common stock plus half of recoveries by a litigation trust.

The disclosure statement said that the new stock was worth about $85 million, or 40% of the noteholders' claims.

Somewhat more than two years after confirmation, the noteholders sold their stock in the reorganized company to a third party. In return, they received $282 million. Although more than the principal amount of their claims, the sale proceeds were less than $380 million, what the claims would be worth now, or $470 million, the amount noteholders would have received by maturity.

The Fraudulent Transfer Suit

After confirmation, the trust initiated suit against the sellers in the LBO, seeking to recover about $250 million they received in selling the company and alleging that the transaction was a fraudulent transfer "with actual intent" or was constructively fraudulent. After Judge Gross rejected *Tribune* and denied the defendants' motion to dismiss the complaint last year, the parties entered into mediation.

The mediation came to a roadblock over the question of whether the noteholders' recovery was capped by the amount of their claims. If there were a cap, the noteholders might be entitled to no further recovery, and the sellers could keep what they received in the LBO even though it may have been a fraudulent transfer.

To remove the logjam and foster settlement, Judge Gross agreed at the parties' behest to decide whether the fraudulent transfer claims are capped. Undertaking what might seem like an advisory opinion, Judge Gross assumed without deciding that the LBO did entail a fraudulent transfer.

Judge Gross said that arriving at a decision about a cap "is not as apparent as it may seem." He cited cases from the bankruptcy court in New York and the Ninth Circuit for the proposition that there is no cap. On the other hand, the defendants argued that "fraudulent transfer laws are remedial, not punitive." Furthermore, he said, "Windfalls and punitive damages are not bankruptcy concepts," and creditors "are not entitled to recover more than their unpaid claims."

Arguing for a cap, the defendants contended that a recovery should be awarded only to recover harm to the creditors and that the $250 million sought in the lawsuit exceeded the noteholders' actual losses.

Finding no authority in the Third Circuit, where the Delaware bankruptcy court sits, Judge Gross held that there is no cap. He relied in part on *Moore v. Bay*, 284 U.S. 4 (1931), where Justice Oliver Wendell Holmes, Jr. held that a trustee could avoid an entire fraudulent transfer, not simply the amount to cover claims of creditors in existence at the time of the transfer.

If there were a cap, Judge Gross said, the defendants "would keep most if not all of the transferred money. The Court cannot countenance such an inequitable result if liability exists."

The defendants relied on Section 550, governing the liability of transferees of avoided transfers. They emphasized language in Section 550(a) allowing the trustee to recover "for the benefit of the estate."

Judge Gross said that "'for the benefit of the estate' does not mean for the benefit of creditors," because "estate" means all legal and equitable interests of the debtor.

By accepting stock for their claims, Judge Gross said that the noteholders "took a risk and are entitled to the benefits of their risk-taking." Although they ended up recovering more than the principal amount of their claims, the value of the reorganized company could have declined, and their losses could have increased.

Moreover, Judge Gross pointed out at the end of his opinion that the noteholders sustained a loss despite selling their stock for more than the principal amount of their claims. At present, the noteholders would be owed $380 million and would have taken in $470 million by maturity, in both cases less than they received for their stock in the reorganized company.

To read ABI's discussion of Judge Gross' decision last year, click here. To read about the Second Circuit's *Tribune* opinion, click here.

The opinion is *PAH Litigation Trust v. Water Street Healthcare Partners LP (In re Physiotherapy Holdings Inc.)*, 15-ap-51238 (Bankr. D. Del. Nov. 1, 2017).

Children were the initial transferees of tuition payments, thus giving schools the 'good faith' defense to fraudulent transfers.

Structured Finance Protects Tuition Payments from Fraudulent Transfer Suits

Universities successfully used concepts from structured finance in fending off suits to recover tuition payments as constructively fraudulent transfers.

Bankruptcy trustees around the country have sued colleges and universities to recover fraudulent transfers when parents file bankruptcy and have paid tuition for children over age 18. The March 28 opinion by Chief Bankruptcy Judge Carla E. Craig of Brooklyn, N.Y., collects cases coming out both ways. Some find constructively fraudulent transfers, while others do not.

In the case before Judge Craig, a parent paid tuition for his children both before and after he filed a chapter 11 petition. Following conversion to chapter 7, the trustee sued the universities to recover pre- and post-petition tuition payments. The trustee contended that pre-petition payments were constructively fraudulent transfers under the Bankruptcy Code and state law and that post-petition payments were unauthorized post-petition transfers under Section 549.

Judge Craig granted summary judgment to the universities dismissing the adversary proceedings. She held that the universities were not the initial transferees and were therefore entitled to the good faith defense as subsequent transferees under Section 550(b).

The successful defense hinged on how the universities structured tuition payments.

The universities all created accounts for and in the name of the students. Payments by parents went into the accounts and were applied toward tuition when the students registered for classes. Parents, even though they may have supplied the funds, had no right to access the accounts without the students' permission. If the students were to withdraw, refunds went to the students, and not to parents who may have made the deposits initially.

Judge Craig ruled that the universities were not the initial transferees because undisputed facts showed that the parent did not have dominion or control over the students' accounts when the debtor made transfers into the accounts. After the initial transfers, she said, the debtor could not access the accounts without the students' authorization. Rather, she said, the students had dominion and control over their accounts.

Judge Craig said that the accounts were “akin to bank accounts,” meaning that the universities, in their roles with respect to the accounts, “were mere conduits in the initial transfer from the debtor to his children.” The universities had dominion and control only after the students took actions that resulted in the payment of tuition, but then the schools were subsequent transferees.

Since the universities were subsequent transferees, they were entitled to the good faith defense in Section 550(b). The trustee did not question the universities’ good faith, making them eligible for summary judgment.

Judge Craig’s theory lets the universities off the hook but puts the debtor’s children in the firing line as initial recipients of fraudulent transfers. As initial transferees, the children cannot raise the good faith defense.

Even though the children may have exposure, a trustee might not sue the children because they are likely judgment proof and themselves may be able to discharge liability by filing chapter 7. Or, the children could raise the theories cited by Judge Craig that have been relied upon by courts finding no fraudulent transfer resulting from tuition payments. Given the familial relationship, children likely have a better shot at beating a suit on the merits than would a college or university.

The opinion is *Pergament v. Hofstra Univ. (In re Adamo)*, 16-8122 (Bankr. E.D.N.Y. March 28, 2018).

Preferences & Claims

Eleventh Circuit abandons the notion that new value must remain unpaid to offset a preference.

Circuit Split Narrows on the New Value Defense to a Preference

Narrowing a split among the circuits, the Eleventh Circuit no longer requires that new value remain unpaid on filing to qualify as a defense to a preference.

As it now stands, the Fourth, Fifth, Eighth, Ninth and Eleventh Circuits do not limit the new value defense to subsequent advances of credit that remain unpaid on the filing date. According to the August 14 opinion by Eleventh Circuit Judge Julie E. Carnes, "the Seventh Circuit held, without much discussion, that Section 547(c)(4) does require new value to remain unpaid."

Similarly, she said that the Third Circuit "also stated in a conclusory fashion [in *dicta*] that Section 547(c)(4) requires new value to remain unpaid."

In reality, the Eleventh Circuit was not reversing a prior holding. Judge Julie Carnes, not to be confused with Chief Judge Ed Carnes, said that her court's prior statement in *Charisma Investment Company N.V. v. Airport Systems Inc. (In re Jet Florida System Inc.)*, 841 F.2d 1082 (11th Cir. 1988), was *dicta* and therefore was not binding.

Commenting on Judge Carnes' opinion, Charles Tatelbaum of Miami told ABI, "It's about time."

The Facts in the Eleventh Circuit

The appeal to the Eleventh Circuit involved a typical preference, albeit for big bucks. The supplier to a chain of grocery stores was paid more than $550,000 in the 90-day preference period before bankruptcy. Also during the preference period, the supplier provided new value by delivering goods worth some $435,000.

The supplier conceded that the payments satisfied all of the elements of a preference under Section 547(b).

However, the supplier raised the so-called ordinary course defense under Section 547(c)(2) and the new value defense under Section 547(c)(4). The bankruptcy court rejected the ordinary course defense.

Relying on *Jet Florida*, the bankruptcy court did not allow the supplier to offset new value that the debtor had paid before filing. As a result, the bankruptcy court held the supplier liable for a net of about $440,000 in preferences. Had the defense been allowed, it is possible that the supplier may have had no preference liability at all.

The bankruptcy court certified a direct appeal, which the Eleventh Circuit accepted. The supplier only raised the new value defense on appeal.

Jet Florida's *Dicta*

In *Jet Florida*, the creditor had raised the new value defense under Section 547(c)(4), which allows a creditor to offset "new value" given after a preferential transfer that was "(A) not secured by an otherwise unavoidable security interest; and (B) on account of which new value the debtor did not make an otherwise unavoidable transfer to or for the benefit of such creditor."

The bankruptcy court in *Jet Florida* concluded that the creditor had not given new value as a matter of fact. Agreeing that the creditor had not given new value, the circuit court in *Jet Florida* upheld the finding of a preference.

In the course of the decision, however, the Eleventh Circuit said that the new value defense has "generally been read to require . . . that the new value must remain unpaid." *Id.* at 1083.

Because the statement about remaining unpaid was not necessary to the decision in *Jet Florida*, Judge Carnes said it was *dicta* and was therefore not binding on the court.

Plain Language Saves the Supplier

Analyzing the issue anew, Judge Carnes said that the "plain language" of Section 546(c)(4) "does not require new value to remain unpaid." She also said that "policy considerations strongly disfavor the trustee's position" that new value must remain unpaid to provide an offset to a preference.

Judge Carnes found nothing in the language of Section 546(c)(4) allowing an offset "only for new value that remains unpaid." Instead, she said, the "plain language" in subsections (A) and (B) allow the defense "so long as the transfer that pays for the new value is itself avoidable."

Judge Carnes buttressed her conclusion by analyzing the history of preferences. Under the predecessor to the current preference statute, Section 60c of Bankruptcy Act of 1898 said there was an offset for "such new credit remaining unpaid." The "remaining unpaid" language, she said, was omitted from the Bankruptcy Code, to be replaced by "something substantively different" in the confusing double negatives now found in subsections (A) and (B).

Judge Carnes cited the Commission on the Bankruptcy Laws of the U.S. for recommending before adoption of the Code that the "remaining unpaid" provision be eliminated.

Even if Congress had not intended to make a change from prior law, Judge Carnes said she would reach the same conclusion from "the unambiguous statutory language."

Policy Considerations Point in the Same Direction

Requiring new value to remain unpaid "would hinder the policy objective of encouraging vendors to continue extending credit to financially troubled debtors," Judge Carnes said. Otherwise, a supplier who senses financial trouble would have a "strong disincentive" to continue delivering goods, for fear that preference liability would increase.

Judge Carnes described a hypothetical where a supplier received $5,000 in payments and made $5,000 in advances during the preference period. If "remaining unpaid" were a requirement, the supplier would be liable for the entire $5,000. If it did not matter, the supplier's maximum liability would be $1,000, she said.

Giving suppliers incentives to cut off customers in financial trouble would hasten bankruptcy, while harming both the debtor and other creditors, Judge Carnes said.

The trustee made a virtually unintelligible argument based on the word "otherwise" in subsection (B). Judge Carnes said that no court had accepted the argument and some have rejected it.

Judge Carnes remanded the case to recalculate the amount of the preference, if any, for which the supplier would be liable.

The opinion is *Kaye v. Blue Bell Creameries Inc. (In re BFW Liquidation LLC)*, 17-13588 (11th Cir. Aug. 14, 2018).

Mediation can result in a binding settlement even without a written agreement.

A Casually Written Email by Counsel Can Be an Agreement in the Second Circuit

An exchange of emails with a mediator can constitute a binding settlement, even if the parties never sign a written agreement, the Second Circuit said in a nonprecedential opinion.

The opinion drives home an important practice point: A casually written email can be a binding contract. Unless you intend for an email to be binding, always say that agreement depends on negotiating and signing a definitive settlement agreement.

As plan administrator, Lehman Brothers Holdings Inc. was in mediation with one of some 250 defendants in a so-called clawback suit where Lehman was attempting to recover payments made after bankruptcy. The amount of the payment the defendant would make was the only issue in mediation. The mediation took place while the defendants' motion was *sub judice* seeking dismissal of the adversary proceeding.

The mediator sent Lehman and the defendant an email confirming that they had accepted his proposal and agreed on the amount of a payment in settlement of Lehman's claim against that defendant. Lehman then sent the defendant the draft of a written settlement agreement. According to the defendant, the agreement contained additional terms that had never been discussed, much less agreed upon in mediation, such as the timing and manner of payment, the identity of the parties to the settlement, the scope of releases, and other terms.

Subsequently, the defendant requested changes in the agreement to which Lehman agreed. According to the bench opinion by Bankruptcy Judge Shelley C. Chapman in March 2017, the defendant's counsel sent Lehman an email saying its client would sign the written agreement as revised.

According to Judge Chapman, she issued her opinion granting the motion to dismiss the adversary proceeding against the defendant and others hours after the defendant's counsel said the client would sign the agreement. A few days later, the defendant said it would not sign the settlement agreement.

Lehman filed a motion to enforce the settlement agreement, which Judge Chapman granted.

In her bench opinion, Judge Chapman said the refusal to sign the settlement was a "change of heart" because she had granted the motion to dismiss, not for lack of intent not to be bound absent a signed, written agreement. Applying the factors required by *Winston v. Mediafare Entertainment Corp.*, 777 F.2d 78 (2d Cir. 1985), Judge Chapman ruled that the settlement agreement was enforceable, although unsigned.

District Judge Denise Cote upheld Judge Chapman, and so did the Second Circuit in a *per curiam* opinion on July 18.

The circuit court analyzed the four *Winston* factors one by one. Two were in favor of finding a settlement, and two were not. The appeals court said it was a "close case."

On telling the mediator there was agreement on the settlement amount, the appeals court said the defendant "did not expressly reserve the right not to be bound in the absence of a writing." The first *Winston* factor therefore weighed in favor of finding an intent to be bound, the circuit said.

There was no partial performance, so the second *Winston* factor weighed against finding an agreement.

The third factor weighed in favor of an agreement, the circuit said, because the defendant's failure to identify disagreement on any material issues was "strong evidence" of agreement. The appeals court "comfortably" concluded that signing the agreement was the only remaining step, because the defendant "reneged" on the agreement only after the bankruptcy judge ruled that she would dismiss the adversary proceeding.

The fourth factor concerns the regularity with which writings are required. That factor was in favor of the defendant because Lehman conceded that no settlements had been in effect during the entire Lehman bankruptcy without a written agreement.

The circuit court said that the "balance tips in favor of finding an intention to be bound," given the absence of an express reservation of rights and the lack of material terms remaining to be negotiated.

It is unclear whether the appeals court would have found a binding agreement had the defendant not later said it would sign the settlement. However, the appeals court focused on the original email exchange when the mediator notified the parties that they had agreed on the settlement amount. The opinion therefore might be understood to stand for the proposition that there was a binding agreement at the earlier point in time, because the amount was the only issue in mediation.

Nonetheless, the opinion is nonprecedential, so its precedential value is limited.

The opinion is *Shinhan Bank v. Lehman Brothers Holdings Inc. (In re Lehman Brothers Holdings Inc.)*, 17-2700 (2d Cir. July 17, 2018).

Eighth Circuit sides with the Third: 'Reasonably ascertainable,' not 'reasonably foreseeable,' determines which creditors are entitled to actual notice.

Eighth Circuit Broadly Draws the Line to Identify 'Unknown' Claims that Are Discharged

Taking sides with the Third Circuit, the Eighth Circuit established a "reasonably ascertainable" test for deciding whether a creditor received constitutionally adequate notice by publication of a potential toxic tort claim.

Even though the debtor had been sued numerous times by similar creditors and the debtor's property was a Superfund site, the appeals court concluded that the debtor had no obligation to give mailed (or actual) notice to all former workers at the plant.

Employed by a trucking company, a driver transported a chemical between 1990 and 1995 to a plant operated by predecessor corporations of the debtor. After several changes of name and ownership, the company confirmed a plan and received a chapter 11 discharge in 2010.

In 2012, the driver was diagnosed with a form of leukemia. After his death, his wife sued the reorganized debtor. The district court denied a motion for summary judgment by the debtor, who contended that the claim was barred by the discharge. After trial, a jury awarded $1.7 million to the driver's widow.

The company appealed. In an opinion on January 26, the Eighth Circuit set aside the judgment, ruling that the wife's claim was discharged because there was constitutionally adequate notice of the debtor's bankruptcy and the bar date.

The wife and her deceased husband were not listed as creditors and did not receive actual notice by mail. The debtor, however, published notice several times in two national newspapers and in a local newspaper where the plant was located.

The district court ruled that the driver's claim had arisen before bankruptcy, meaning that the claim ordinarily would have been discharged because the driver did not file a claim. The district court concluded that the claim was not discharged because the driver should have been given actual notice.

Writing for the Court of Appeals, Circuit Judge Duane Benton concluded that the district court had employed the incorrect standard for deciding the form of notice to which the creditor was entitled.

Judge Benton recited the general rule that a known creditor is entitled to actual notice by mail. For unknown creditors, notice by publication is constitutionally sufficient.

The district court believed that notice by publication was inadequate and that the claim was not discharged because the claim was "reasonably foreseeable." The district court based its conclusion on several factors: (1) The debtor had been fined $2.5 million by the EPA for discharges of the chemical that caused the driver's leukemia; (2) similar claims were 10% of the debtor's yearly toxic tort litigation, and (3) the plant had been declared a Superfund site requiring remediation.

Following the Third Circuit's decision in *Chemetron Corp. v. Jones*, 72 F.3d 341 (3d Cir. 1995), Judge Benton ruled that "reasonably ascertainable" was the standard, not "reasonably foreseeable."

Judge Benton identified several factors calling for reversal of the judgment. First, the Bankruptcy Rules only require giving notice of the names used by the debtor within eight years of bankruptcy. The years 1990-95 were well beyond the eight-year window, and none of the names under which the company operated at that time were among the 90 companies listed on the notices. However, Judge Benton conceded that following the Bankruptcy Rules may not always result in constitutionally adequate notice.

Of more significance, the debtor employed an experienced bankruptcy consultant to identify potential creditors. The consultant identified one million potential creditors to receive actual notice. The driver was not among them, thus labeling him an unknown creditor.

Citing *Tulsa Professional Collection Services Inc. v. Pope*, 485 U.S. 478, 490 (1988), Judge Benton said that publication notice to unknown creditors "generally suffices" after a "reasonably diligent search."

Next, Judge Benton concurred with the Third Circuit's *Chemetron* decision holding that debtors "cannot be required to provide actual notice to anyone who potentially could have been affected by their actions; such a requirement would completely vitiate the important goal of prompt and effectual administration of debtors' estates."

Like the Third Circuit, Judge Benton therefore held that the line to cordon off unknown creditors depends on whether the claim is "reasonably ascertainable," not "reasonably foreseeable." Because the claim was not "reasonably ascertainable" given the extensive search undertaken by the debtor's consultant, notice by publication was constitutionally adequate, and the claim was therefore discharged.

The opinion is *Dahlin v. Lyondell Chemical Co.*, 16-3419, 2018 BL 26501 (8th Cir. Jan. 26, 2018).

Perishable Commodities Act

Ninth Circuit reverses its own precedent and eliminates a circuit split by favoring farmers.

En Banc, **Ninth Circuit Holds: Only 'True Sales' of** Receivables Comply with PACA

The Ninth Circuit sat *en banc*, reversed the three-judge panel by a vote of 8/3, overruled its own precedent, eliminated a split of circuits and closed a gaping loophole that the San Francisco-based appeals court had previously created in the federal Perishable Agricultural Commodities Act, or PACA (7 U.S.C. § 499a *et seq*.).

In *Boulder Fruit Express & Heger Organic Farm Sales v. Transportation Factoring, Inc.*, 251 F.3d 1268 (9th Cir. 2001), the Ninth Circuit had held that a lender to a fresh produce wholesaler can circumvent the strictures of PACA by denominating a secured loan as a sale of accounts receivable.

By virtue of its *en banc* opinion on Feb. 22, the Ninth Circuit has now aligned itself with the Second, Fourth and Fifth Circuits by holding that a transaction must be a "true sale" before a purchaser of accounts receivable can acquire an interest in a wholesaler's accounts ahead of the interests of produce suppliers who are beneficiaries of a PACA trust.

The PACA Loophole and the Split

Congress adopted PACA to protect farmers who were usually unpaid when a fresh produce wholesaler declared bankruptcy. The statute creates a statutory trust protecting growers by putting them ahead of accounts receivable *lenders*. Farmers, however, do not have recourse under PACA against *purchasers* of receivables. In deciding whether a financial institution is immune from PACA, the Second, Fourth and Fifth Circuits have first required the court to decide whether a true sale actually occurred and, second, to examine whether the sale was commercially reasonable.

In *Boulder Fruit* in 2001, the Ninth Circuit made a loophole in PACA by holding that the court need only decide whether a transaction was commercially reasonable before cutting off PACA protection. There was no threshold test in the Ninth Circuit to determine whether the transaction was a true sale so long as the transaction denominated itself as a sale of receivables.

Finding itself bound by *Boulder*, a three-judge panel of the Ninth Circuit ruled against farmers in a *per curiam* decision, *S&H Packing & Sales Co. v. Tanimura Distributing Inc.*, 850 F.3d 446 (9th Cir. Feb. 27, 2017). In a concurring opinion, two judges on the panel argued that *Boulder Fruit* was "wrongly decided" and urged the circuit to sit *en banc* to bring "the Ninth Circuit into line with the other circuits that have considered the issue."

The Ninth Circuit granted rehearing *en banc* in June, heard oral argument in September and overruled *Boulder Fruit* in an opinion for the majority written by Circuit Judge Ronald M. Gould.

The Majority's Opinion

Judge Gould held that the court must first "conduct a threshold true sale inquiry" before deciding whether a hypothecation of accounts receivable was "commercially reasonable." He based his decision on "the logical outcome of reading PACA, PACA's legislative history, and consideration of PACA's purpose."

In particular, legislative history told Judge Gould that "our focus should be on the true nature of the transactions at issue." The court, he said, "must focus on the true substance of PACA-related transactions and not on artificial indicators or labels." Later, he added, "labels . . . should be of little or no significance."

The lender argued that the result would be absurd if it had paid full value for receivables and was later required by PACA to pay farmers a second time for the same receivables.

Judge Gould said the lender was "wrong to describe the scenario as absurd. It is instead the result of a Congressional choice."

Judge Gould analogized PACA to state laws pertaining to general contractors, subcontractors and owners of real estate, because state law can force an owner to pay twice, just like a PACA lender. If an owner has not obtained releases of liens by subcontractors, the owner must pay the subcontractors a second time even if the owner has paid the general contractor. The PACA lender can pay twice if it has not policed the borrower to ensure that suppliers have been paid with the proceeds of its loans.

On remand, Judge Gould instructed the court to "use all the tools at its disposal . . . to determine whether the agreement was in substance a true sale or in substance a lending agreement."

The facts of the case suggest that the transaction was a secured loan rather than a true sale of accounts receivable, because the lender could force the wholesaler to buy back receivables proven uncollectable.

Judge Gould lauded the concurring opinion in the panel decision. He said, "This opinion is in substantial agreement with arguments made in [Circuit] Judge [Michael J.] Melloy's concurrence and draws heavily therefrom." Judge Melloy, from the Eighth Circuit, was sitting by designation on the three-judge panel.

The Dissent

In an opinion written by Circuit Judge Sandra S. Ikuta, the dissenters contended as a matter of policy that the majority's rule "allows the trust to accept the benefit of a loan agreement but disregard the obligation to repay it."

With regard to the law, Judge Ikuta relied on "basic trust principles" for the proposition that a trustee does not violate his/her fiduciary duty to trust beneficiaries by obtaining a secured loan.

Judge Gould answered the argument by saying that PACA imposes duties beyond those in trust law. He said that the dissenters gave "too little weight to the protective purposes of PACA" and disregarded "the purpose of PACA to protect agricultural growers."

Judge Gould clerked on the Sixth Circuit and the Supreme Court before being appointed to the Ninth Circuit in 1999. Judge Ikuta clerked for the Ninth Circuit and Supreme Court before her appointment to the circuit bench in 2006.

To read ABI's report on the decision by the three-judge panel and the concurrence, click here.

The opinion is *S&H Packing & Sales Co. v. Tanimura Distributing Inc.*, 14-56059 (9th Cir. Feb. 22, 2018).

Consumer Bankruptcy

Fair Debt Collection Practices Act

Thomas Ambro on the Third Circuit answers a question the Supreme Court left open in Henson v. Santander.

FDCPA Applies to Debt Collectors Even if They Own the Debt

The Third Circuit jumped through a loophole the Supreme Court left open intentionally in *Henson v. Santander Consumer USA Inc.*, 137 S. Ct. 1718 (2017), by holding a debt purchaser is subject to the federal Fair Debt Collection Practices Act, or FDCPA, if its principal business is the collection of debts.

In *Henson*, the maiden opinion by newly-appointed Justice Neil M. Gorsuch, the headline holding was: Someone who purchases a defaulted debt is not a "debt collector" and is therefore not subject to the FDCPA, 15 U.S.C. § 1692, *et seq*.

A bank in *Henson* had purchased a debt already in default that had been originated by another lender. The opinion was often (but incorrectly) interpreted to mean that the FDCPA can never apply to a debt collector who has purchased a defaulted debt for its own account. However, Justice Gorsuch was careful to highlight two questions the Court did not decide:

(1) The debtor argued that the bank came within the FDCPA because it regularly collected debts for another. Justice Gorsuch said that question was not raised in the petition for *certiorari*, and the Court did not agree to review it; and
(2) Justice Gorsuch said the Supreme Court had not agreed to address another aspect of the definition of a debt collector in Section 1692a(6), which includes someone "in any business the principal purpose of which is the collection of any debts."

In his August 7 opinion for the Third Circuit based on the "plain text" of the statute, Circuit Judge Thomas L. Ambro latched onto the second unresolved question by holding that the FDCPA applies to "an entity whose principal purpose of business is the collection of any debts . . . regardless of whether the entity owns the debts it collects."

The Facts in the Third Circuit

The facts on the appeal before Judge Ambro were similar to those in *Henson*, except that the plaintiff in *Henson* had not argued below that the bank's principal business was debt collection.

In the Third Circuit, the plaintiffs owned a home subject to a mortgage owing to a bank taken over by the Federal Deposit Insurance Corp. Initially, they continued making monthly payments

after the takeover, but the FDIC neither cashed nor returned the checks. Eventually, the plaintiffs stopped sending monthly checks.

The FDIC declared the loan in default and sold it to a purchaser who demanded payment in full in an amount more than the plaintiffs owed. Having made several communications that might violate the FDCPA, the purchaser initiated foreclosure proceedings.

The homeowners filed suit in district court, alleging violations of the FDCPA. In several pleadings, the defendant-purchaser admitted that its sole business was acquiring and collecting debts.

Following a bench trial but before the district court rendered its decision, the Supreme Court handed down *Henson*. After additional briefing, the district court ruled that the purchaser was a debt collector and was liable for having violated the FDCPA.

The purchaser appealed, contending in the Third Circuit that it was not a debt collector subject to the FDCPA because it owned the debt.

Judge Ambro's Analysis

The FDCPA applies to a "debt collector" but not to a "creditor." A "debt collector" is defined as someone who uses the mails or interstate commerce "in any business the principal purpose of which is the collection of any debts" or someone "who regularly collects" debts owed to "another." 15 U.S.C. § 1692a(6).

A "creditor" under the FDCPA is someone who extends credit or is someone "to whom a debt is owed." The term "creditor" excludes "any person to the extent that he receives an assignment or transfer of a debt in default solely for the purpose of facilitating collection of such debt for another." 15 U.S.C. § 1692a(4) and (6).

Before *Henson*, the law in the Third Circuit followed the so-called default test in *Pollice v. National Tax Funding L.P.*, 225 F.3d 379, 403 (3d Cir. 2000), where the purchaser of a debt is a debt collector subject to the FDCPA if the debt was purchased after default.

Under *Pollice*, the purchaser in Third Circuit appeal would have been a "debt collector," but Judge Ambro said that *Henson* "recently repealed the 'default' test we followed."

Judge Ambro said that only one circuit court since *Henson* has ruled on the FDCPA in a precedential opinion. In that case, the District of Columbia Circuit held that the defendant was not a debt collector because there was no evidence that the bank's principal business was the collection of debt or that it was collecting the debt for someone else.

Addressing "the task before us today," Judge Ambro said that no circuit has issued a precedential opinion "on *Henson*'s applicability to the 'principal purpose' definition of 'debt collector.'" Picking what *Henson* held and what it did not hold, he said that *Henson* "affects" but "did not decide" who "fits the 'principal purpose' definition of 'debt collector.'"

Judge Ambro said that the phrase "any debt" as used in the statute does "not distinguish to whom the debt is owed." In contrast, he said, "debts owed or due . . . another" only applies to the "regularly collects" definition.

Contending that it could not be a debt collector because it also met the definition of creditor, the purchaser in substance argued that the definitions are mutually exclusive. Judge Ambro rejected the argument because, "following *Henson*, an entity that satisfies both is within the [FDCPA's] reach."

Whether the defendant owns the debt, Judge Ambro said, "does not resolve whether that entity is a debt collector." Because the purchaser conceded that its principal business was collecting debts, Judge Ambro held that the debt buyer was subject to the penalties in the FDCPA because it was a "debt collector under the 'principal purpose' definition."

To read ABI's discussion of Henson, click here.

The opinion is *Tepper v. Amos Financial LLC*, 17-2851 (3d Cir. Aug. 7, 2018).

The Eighth Circuit bars clever litigation tactics designed to evade the FDCPA on suits to collect time-barred claims.

Eighth Circuit Broadly Interprets the FDCPA to Protect Consumers

The Eighth Circuit set up a test case where the Supreme Court could decide, in the wake of *Spokeo Inc. v. Robins*, 136 S. Ct. 1540, 194 L. Ed. 2d 635, 84 U.S.L.W. 4263 (Sup. Ct. 2016), whether damages under the federal Fair Debt Collection Practices Act, or FDCPA, are sufficiently "concrete" to pass constitutional muster.

The Eighth Circuit's opinion also pushes back against the tendency of some courts to read the FDCPA so narrowly that it fails its mission as a consumer protection statute.

The case centered around the practice of suing on debts where collection is barred by the statute of limitations. Intending to avoid liability under state laws or the FDCPA, the creditor will dismiss suits when consumers appear for trial. Otherwise, the creditor would obtain judgments against those not appearing or defending.

In the case that went to the Eighth Circuit, the debtor appeared, ready to try the case, but the creditor dismissed the suit. A month later, the creditor sued, alleging violations of the FDCPA. The district judge dismissed the suit, saying, among other things, that the creditor had only engaged in "permissible litigation tactics and not actionable false assertions."

In an opinion on Aug. 29, Circuit Judge Duane Benton reinstated the suit, reversing all the grounds for dismissal.

Relying on *Spokeo*, the creditor contended in the Eighth Circuit that the consumer-plaintiffs lacked constitutional standing because they were only alleging *de facto* damages created by statute, not the required "concrete" injury.

Broadly holding that violations of the FDCPA meet constitutional requirements when stale debts are involved, Judge Benton said that "Congress created a statutory right to be free from attempts to collect debts not owed, helping to guard against identified harms," such as the "risk of mental distress" and marital discord that can accompany the "harm of being subjected to baseless legal claims."

The creditor contended that serving discovery requests on the consumers' attorney was not an FDCPA violation because it was not served on the consumers themselves. Since papers served on

an attorney "routinely" come to clients' attention, Judge Benton held that the service of discovery requests caused "concrete injury in fact."

For those engaged in practice under the FDCPA, we recommend reading the opinion in full, because Judge Benton handed down many holdings regarding consumers' rights.

For instance, the district court dismissed claims because the suit was not commenced within the one-year statute of limitations under the FDCPA. More particularly, the district judge said that the communications relied on in the complaint all related back to the filing of the creditor's original complaint, which was beyond the FDCPA's one-year window.

Judge Benton rejected the relation-back theory, holding that the limitations clock begins ticking with each alleged violation of the FDCPA.

Characterizing the creditor's pleadings and other actions as "permissible litigation tactics," the district court dismissed under 28 U.S.C. § 1692(e), which prohibits "any false, deceptive, or misleading representation or means in connection with the collection of any debt."

Judge Benton said that "the fact that it used an ordinarily 'permissible litigation tactic' does not insulate it from FDCPA liability" when the consumer plausibly alleges that the creditor threatened to go to trial.

Without mentioning all of Judge Benton's holdings, his analysis of Section 1692(f) is also significant. The creditor contended that the discovery requests did not violate that section, which prohibits debt collectors from using "unfair or unconscionable means to collect or attempt to collect any debt."

The district court dismissed, saying that the consumers were unlikely to be deceived by court papers served on the consumers' attorney.

Judge Benton countered by saying that Section 1692(f) contains no "misled, deceived, or duped" requirement. That section only proscribes "unfair or unconscionable" means to collect debts. He said that cases interpreting that section "do not impose a 'misled, deceived, or duped' requirement."

The FDCPA, the judge said, does not merely prohibit activities "that mislead consumers into paying debts not owed." The statute, "by its terms, guards against many other harms — the mental distress that can cause 'marital instability' and 'the loss of jobs,' as well as 'invasions of individual privacy.'"

Reversing the district court for having dismissed the consumer's suit, Judge Benton said, "The attempted collection of debts not owed harms consumers not just by inducing the payment of false

claims. It also forces consumers to spend time and money addressing the false claims — even if they know they do not actually owe the claimed debt."

Judge Benton was appointed to the circuit bench in 2004 by President George W. Bush.

If the debt-collection bar is looking for a case worthy of the Supreme Court, the original *Spokeo* suit may be first in line. After remand from the Supreme Court, the Ninth Circuit ruled on Aug. 15 that the plaintiff had alleged constitutionally necessary "concrete" damages. To read ABI's discussion of *Spokeo* after remand, click here. For ABI's report on the Supreme Court's *Spokeo* decision, click here.

Whether the high court grants *certiorari* is uncertain because there still does not seem to be a circuit split. Nonetheless, the justices originally granted *certiorari* in *Spokeo* although there was no split at the time.

The opinion is *Demarais v. Gurstel Chargo PA*, 869 F.3d 685 (8th Cir. Aug. 29, 2017).

The Code or rules must change to bar debt collectors from filing stale claims, Judge Dow says.

Courts Can't Sanction Debt Collectors for Filing Stale Claims after *Midland Funding*

Now that the Supreme Court has allowed debt collectors to file stale claims, the statute or the Bankruptcy Rules must be amended before courts can halt the practice, according to Bankruptcy Judge Dennis R. Dow of Kansas City, Mo.

In *Midland Funding LLC v. Johnson*, 137 S. Ct. 1407, 197 L. Ed. 2d 790, 85 U.S.L.W. 4239 (Sup. Ct. May 15, 2017), the Supreme Court held that a debt collector who files a claim that is "obviously" barred by the statute of limitations has not engaged in false, deceptive, misleading, unconscionable, or unfair conduct and thus does not violate the federal Fair Debt Collection Practices Act.

The U.S. Trustee mounted a frontal attack on a debt collector engaged in the business of filing proofs of claim where collection would be barred by the statute of limitations. In an adversary proceeding begun eight months before the high court decided *Midland Funding*, the U.S. Trustee alleged that regularly filing claims based on stale debts was a "systemic abuse of the bankruptcy process."

The U.S. Trustee sought a nationwide injunction, a monitor, unspecified monetary damages, and sanctions for routinely filing stale claims. Despite finding the creditor's "behavior disturbing," Judge Dow dismissed the complaint while allowing the U.S. Trustee to proceed with objections to two stale claims.

Although critical of the creditor's practices and procedures, the bulk of Judge Dow's Sept. 1 opinion leads to the conclusion that the current state of the law and rules cannot be employed to outlaw so-called robo-signing or the filing of stale claims.

For example, Judge Dow found that the creditor's "alleged process for preparing and reviewing claims fell short of the requirement of Official Form 10 and Bankruptcy Rule 9011." Despite the fact that the creditor used "questionable practices," the judge concluded that the facts did not lend to the imposition of sanctions, in part because the form was not amended until 2016 "to require that the individual signing the proof of claim personally review it."

Judge Dow faulted the creditor's elaborate robo-signing procedures because there was "no indication" that the person who signed the claims "knew if, or to what extent, that process was followed." He also said it was "inconceivable that an individual could comply with the instructions

for Official Form 10 without ever examining the claim." Evidently, the same person's signature appeared on about 54,000 claims.

Ultimately, the complaint failed to state a claim for sanctions, Judge Dow said, because the U.S. Trustee did not allege "bad faith in connection with its 'robo signing' practice," because the propriety of the practice was at least debatable.

The U.S. Trustee was barred from seeking sanctions under Bankruptcy Rule 9011 for filing stale claims because he had "failed to abide by the safe harbor provisions of that rule." Sanctions were similarly unavailable under Section 105 because the statutes of limitations in most states do not extinguish these types of claims. Also on the question of whether the filing of stale claims violates the Bankruptcy Code, Judge Dow said that the definition of "claim" is "extremely broad."

Therefore, "considering applicable state law and the provisions of the Code," Judge Dow decided that "creditors have the right to file such claims and that doing so is not sanctionable." There is no violation of Rule 9011, he said, unless the creditor continues asserting the claim "after the statute of limitations has been raised."

Locking the door after slamming it shut, Judge Dow said the U.S. Trustee would not be entitled to sanctions even if the creditor had been filing claims that did not comply with Rule 3001(c). The remedy for failure to file a claim in proper form, he said, is to strip the claim of its *prima facie* validity, "besides those enumerated in Rule 3001(c)."

The "other appropriate relief" allowed under the rule "does not include the disallowance of a claim." Likewise, there is no independent cause of action for a violation of Rule 3001.

Putting his finger on the nub of the issue, Judge Dow held that the creditor's behavior was "not sanctionable and may not be treated as such until changes are made either by Congress or the Rules Committee," even though the creditor's "conduct is unsettling and perhaps even distasteful or unseemly in some respects." In addition, Judge Dow said he had "no power to grant relief which would purport to be binding as to claims filed and conduct occurring in cases other than ones before this Court." Even if there were nationwide power, Judge Dow said he "would decline to exercise it."

The opinion is *Casamatta v. Resurgent Capital Services LP (In re Freeman-Clay)*, 578 B.R. 423 (Bankr. W.D. Mo. Sept. 1, 2017).

Discharge/Dischargeability

Seven weeks apart, two circuits reach diametrically different conclusions about good faith as a defense to an intentional act that violates the discharge injunction.

First Circuit Splits with the Ninth over Good Faith Defense to Discharge Violation

Over a comprehensive dissent, the First Circuit ruled that the Internal Revenue Service intentionally violates the discharge injunction when an IRS employee knows there was a discharge but nonetheless "takes an intentional action" later found to violate the discharge, even if the IRS had a good faith belief that its action did not violate the discharge.

The First Circuit's June 7 opinion represents a stark split with a decision handed down by the Ninth Circuit less than seven weeks ago: *Lorenzen v. Taggart (In re Taggart)*, 888 F.3d 438 (9th Cir. April 23, 2018), petition for panel rehearing and rehearing *en banc* filed June 6, 2018. Although the First Circuit dissent cited *Taggart*, the majority did not.

The First Circuit's dissent underscores an arguably longstanding circuit split on the question of whether good faith is a defense to an alleged violation of the discharge injunction.

The majority opinion for the First Circuit, holding that good faith is not a defense to contempt, was written by Circuit Judge Norman H. Stahl. Joining the majority opinion was retired Supreme Court Associate Justice David H. Souter, sitting by designation. The dissent was by Circuit Judge Sandra L. Lynch.

The Facts in the First Circuit

The debtor filed a chapter 7 petition and received a discharge. The IRS was aware of the discharge.

Among his $600,000 in total debt, the debtor owed the IRS about $550,000 in taxes. The IRS had a good faith basis for believing that the taxes were not dischargeable under Section 523(a)(1)(C) because the debtor, allegedly, had willfully attempted to evade payment of the taxes. The IRS therefore took the position that the tax debt was not automatically discharged under Section 523(c)(1). Thus, the IRS did not object to the dischargeability of the debt before the debtor received his general discharge.

After entry of the general discharge, the IRS repeatedly notified the debtor of its belief that the taxes were not automatically discharged. After the IRS eventually levied against an account

receivable owing to the debtor, he filed an adversary proceeding in bankruptcy court seeking a declaration that the debt indeed had been discharged. Allegedly because of mental infirmities afflicting the assistant U.S. Attorney (AUSA) who represented the IRS, the government presented insufficient evidence, leading the bankruptcy judge to grant summary judgment declaring that the taxes were discharged. The IRS did not appeal the ruling that the debt was discharged.

The debtor later filed a complaint against the IRS under 26 U.S.C. § 7433(e), seeking sanctions for willful violation of the discharge injunction by issuing levies against his assets. In defense, the IRS argued there was no willful violation because the government reasonably believed that the debt was not discharged.

The bankruptcy judge found a willful violation and ruled in favor of the debtor. On appeal, the district court remanded for the bankruptcy court to consider the AUSA's mental impairment.

On remand, the IRS and the debtor reached a partial settlement narrowing the issues. To avoid extensive litigation over the AUSA's mental impairment and whether his impairment would give the government a defense, the IRS agreed that the debtor could have $175,000 in damages if an appellate court ultimately were to rule that a reasonable belief that the debt was excepted from discharge was not a defense to contempt.

The bankruptcy court decided that good faith was not a defense and ruled against the IRS. The district court affirmed, and the IRS appealed.

The Majority Opinion

Given the stipulation limiting the issue on appeal, Judge Stahl said the appeals court would decide whether the IRS's good faith belief meant there was no willful violation of the discharge injunction under Section 7433(e).

Adopted in 1998, Section 7433(e) allows a taxpayer to recover damages from the U.S. if the IRS, in connection with the collection of taxes, "willfully violates any provision of" the automatic stay under Section 362 of the Bankruptcy Code or Section 524 and its injunction barring the collection of discharged debt.

Judge Stahl said that the statute defines neither "willfully" nor the phrase "willfully violates." To find a meaning for the terms, he surveyed the definition given those words by the circuit courts when the statute was adopted in 1998.

Although the dissenter disagreed about unanimity among the courts of appeals, Judge Stahl said that the circuit courts agreed that the "phrase 'willful violation' had an established meaning in the context of violations of the automatic stays [*sic*] as of 1998: a creditor willfully violated the automatic stay if it knew of the automatic stay and took an intentional action that violated the

automatic stay. A good faith belief in a right to the property was not relevant to determining whether the creditor's violation was willful."

Judge Stahl next concluded that Congress intended to give the same meaning to violations of the discharge injunction, in part because "the plain language of Section 7433(e) does not distinguish between" violations of the automatic stay and discharge.

Although Judge Stahl said he was relying "primarily" on what Congress understood "willful violation" to mean in 1998 on adopting Section 7433(e), he said that later First Circuit decisions hewed to the same definition for violations of both the automatic stay and the discharge injunction.

Although the dissenter disagreed, Judge Stahl said that his definition of "willful violation" did not entail an overbroad interpretation of the wavier of sovereign immunity in Section 7433(e).

The IRS contended that Judge Stahl's interpretation would force the government to seek a declaration about the dischargeability of debts for tax fraud, even though Section 523(a)(1)(C) excepts them from discharge automatically.

Judge Stahl rejected the argument, finding "policy considerations" against "allowing the IRS to attempt to collect purportedly discharged debts without facing potential consequences." He said the IRS had several alternatives.

First, the IRS could have filed an objection to the dischargeability of the debt, although it was not required to do so before the entry of the general discharge. Second, the IRS could have filed an adversary proceeding and sought a declaration about dischargeability before beginning collection activity.

Third, the IRS could have attempted to collect the debt, as it had done in the case at bar, and gamble that the bankruptcy court would find for the government and rule that the taxes were not discharged.

The Dissent

In dissent, Judge Lynch said that her panel was handing down the first circuit court opinion construing "willfully violates" in Section 7433(e). The majority, she said, "gets this one wrong."

Judge Lynch said her circuit was the first to deprive the government of sovereign immunity when acting "on a reasonable and good faith belief." In Section 7433(e), she found no indication of a waiver of immunity "where the IRS acts reasonably and in good faith," even if the belief turns out to be erroneous.

Rather than following circuit law, Judge Lynch would have adopted the approach of the Supreme Court where she said the justices held in the context of Section 523 that a willful injury includes only acts that "were specifically intended to cause injury, not all intentional acts that resulted in injury."

Of special significance, Judge Lynch disagreed with the majority's statement that the circuits were in agreement before 1998. Although the majority opinion reflected the holding of seven circuits, she said that the First, Fifth and Sixth Circuits would allow a good faith defense to an alleged willful stay violation. Where she said the "majority attempts to deny the existence of this circuit split," Judge Lynch said that those three circuits "had held that the mere knowledge of a stay was insufficient to show a 'willful violation.'"

In addition to older authority from those three circuits, she cited *Taggart*, decided by the Ninth Circuit on April 23. She read the Ninth Circuit as allowing a good faith defense. "Indeed," she said, "the Ninth Circuit does not even impose a reasonableness requirement." For ABI's discussion of *Taggart*, click here.

Judge Lynch placed significant reliance on Section 523(a)(1)(C), which does not "require the IRS to first obtain a judicial determination that an exception to discharge applies." The subsection, she said, "means that Congress chose <u>not</u> to require that the IRS seek a pre-collection determination from the bankruptcy court." [Emphasis in original.]

"Given that Congress created this exception to discharge and did not require the IRS to seek a pre-collection determination that the tax debts are not dischargeable, there is no reason to say that the IRS should incur the risk of having damages found against it even if it acted on a reasonable and good faith belief," Judge Lynch said.

Are There Grounds for *Certiorari*?

The First Circuit's decision and *Taggart* are very much at odds. The Ninth Circuit permits a good faith defense to a discharge violation, while the First Circuit does not.

Should the losing parties in either circuit petition for *certiorari*, they surely will claim there is a circuit split. However, the majority on the First Circuit found no circuit split, although the dissenter did.

By ruling on Section 7433(e), the First Circuit was not construing the same statute as the Ninth. If a *certiorari* petition is based on divergent opinions by the two circuits just seven weeks apart, the justices might shy away from granting the petition because the underlying statutes are not the same.

However, there surely is a lack of clarity about the availability of a good faith defense when a panel of the First Circuit cannot agree on whether there is a circuit split. The Supreme Court might decline to grant *certiorari* until there is a decision more starkly raising a circuit split. *Taggart* might become a better vehicle for *certiorari* after the Ninth Circuit disposes of the pending petition for rehearing and rehearing *en banc*.

Although the dissent in the First Circuit says there is a circuit split about the good faith defense generally, the dissenter also said her panel was the first appeals court to rule on Section 7433(e). Even though the underlying issue is applicable to Sections 362 and 524 of the Bankruptcy Code, the Supreme Court might not be inclined to grant *certiorari* to the First Circuit and review the first decision on Section 7433(e).

All things considered, *Taggart* therefore might be the better vehicle for *certiorari*. The debtor in *Taggart* contends that the Ninth Circuit's opinion represents a split with the Fourth and Eleventh Circuits on the availability of a good faith defense.

If there is a petition for *certiorari* in *Taggart*, the Supreme Court may request the opinion of the U.S. Solicitor General on whether to grant or deny the petition, known as a CVSG for "consider the views of the Solicitor General." A CVSG would allow the government to weigh in on the existence of a split (or not) and presumably urge the justices to review the case.

Given the outcome in the First Circuit, the government well may urge a grant of *certiorari* in *Taggart*, especially if *certiorari* to the First Circuit is less likely.

Either case would enable the Supreme Court to rule on a fundamental, recurring issue in bankruptcy law: Does good faith allow a creditor to escape the consequences of an intentional violation of the principal relief a debtor obtains through bankruptcy?

The opinion is *IRS v. Murphy*, 17-1601 (1st Cir. June 7, 2018).

An unreasonable but good faith, subjective belief that there is no injunction bars a finding of contempt in the Ninth Circuit.

Violation of Discharge Is Now Difficult to Prove in the Ninth Circuit

A creditor's subjective, good faith belief that its action does not violate the discharge injunction precludes finding the creditor in contempt, even if the discharge injunction did apply and the creditor's belief was "unreasonable," the Ninth Circuit ruled in an April 23 opinion.

The opinion appears to mean that a creditor can act in good faith even if the creditor's belief is unreasonable. In other words, litigation in the Ninth Circuit over contempt of the discharge injunction will focus on the creditor's subjective good faith, without regard to whether the creditor's belief was right or wrong, reasonable or unreasonable.

The facts were horribly complex. With apologies for oversimplification, we summarize the facts as follows:

Before bankruptcy, the debtor transferred his interest in a closely held corporation. After the debtor received his chapter 7 discharge, two other shareholders sued the debtor in state court for transferring his interest without honoring their contractual right of first refusal. They also sued the transferee of the stock.

After the debtor raised his discharge as a defense in state court, the parties agreed he would not be liable for a monetary judgment. The state court eventually ruled in favor of the creditors and unwound the transfer.

The creditors then sought attorneys' fees as the prevailing parties, invoking a fee-shifting provision in the shareholders' agreement. The state court ruled that the debtor "returned to the fray" and thereby made himself liable for post-discharge attorneys' fees.

Meanwhile, the debtor reopened his bankruptcy case, seeking to hold the creditors in contempt for violating the discharge injunction. The bankruptcy judge sided with the debtor and imposed sanctions. The Bankruptcy Appellate Panel reversed the finding of contempt, ruling that the creditors' good faith belief that their actions did not violate the injunction absolved them of contempt.

Meanwhile, the state appellate court and a federal district court in related litigation both ruled that the debtor's participation in the litigation did not constitute returning to the fray, thus taking

away the grounds for imposing attorneys' fees and lending credence to the notion that the creditors did technically violate the injunction.

In sum, judges disagreed over whether the discharge injunction applied to the litigation to recover attorneys' fees.

The debtor appealed the BAP's opinion to the Ninth Circuit, where Circuit Judge Carlos T. Bea upheld the BAP and found no contempt. In the process, he expanded the defenses available to someone charged with contempt of a discharge injunction.

To impose sanctions, existing Ninth Circuit precedent requires the debtor to show that the creditor knew the discharge injunction was applicable and prove that the creditor intended the actions that violated the injunction. In the case at hand, knowledge of the applicability of the injunction was the only issue.

Based on *In re Zilog Inc.*, 450 F.3d 996 (9th Cir. 2006), Judge Bea said that knowledge of the injunction cannot be proven by merely showing that the creditor was aware of the bankruptcy. Citing a footnote in *Zilog*, he went on to hold that "the creditor's good faith belief that the discharge injunction does not apply to the creditor's claim precludes a finding of contempt, even if the creditor's belief is unreasonable."

Judge Bea acknowledged that his interpretation of *Zilog* is "somewhat at tension" with two other Ninth Circuit precedents. Although Judge Bea said that *Zilog* was binding, it is arguable that the footnote in *Zilog* was *dicta* and therefore was not binding. Regardless of whether *Zilog* was binding or not, Judge Bea's opinion is now law in the Ninth Circuit, although it is unclear whether it was necessary for him to rule that an unreasonable belief is not actionable.

Based on his reading of *Zilog*, Judge Bea concluded, like the BAP, that the creditor had a good faith belief that the discharge injunction was inapplicable on the theory that the debtor had "returned to the fray." The creditor's belief in that regard was strengthened because the state trial court agreed.

Recall, however, that the state appellate court and the district court took the opposite view by concluding that the debtor had not "returned to the fray" but had been compelled to litigate. In other words, judges disagreed about the applicability of the injunction.

Although the creditors' belief in the inapplicability of the injunction ultimately was proven wrong, Judge Bea said that "their good faith belief, even if unreasonable, insulated them from a finding of contempt."

Judge Bea's opinion applies a subjective test with respect to belief in the inapplicability of the injunction. Moreover, there is no contempt even if the creditor's subjective belief is unreasonable.

Consequently, it seems that reliance on counsel's advice would always absolve a client from contempt liability in the Ninth Circuit.

Judge Bea's opinion also seems to stand for the proposition that there is no contempt if reasonable minds could differ on the applicability of the injunction. Since it's often debatable whether the discharge injunction applies, contempt henceforth may be difficult to prove in the Ninth Circuit.

Because an unreasonable belief is not grounds for a finding of contempt, an argument evidently must be at least frivolous before there is contempt.

We submit that the appeals court could have reached the same result on more narrow grounds by finding good faith since the trial judge in state court supported the creditors' belief by ruling that the injunction did not apply. By ruling more narrowly, the appeals court could have avoided pronouncing a rule that gives creditors license to disregard discharge injunctions by making pretextual arguments.

It is not clear from the opinion whether the same contempt standard applies to violation of the automatic stay. If it does, the automatic stay will have lost its teeth in the Ninth Circuit.

The opinion is *Lorenzen v. Taggart (In re Taggart)*, 888 F.3d 438 (9th Cir. April 23, 2018); petition pending for rehearing and rehearing *en banc*.

Eighth Circuit says orders reducing nondischargeable claims may not be binding on the creditor.

No Contempt on Discharge Violation of Nondischargeable Debt, Circuit Says

The Eighth Circuit arguably narrowed a June 2016 opinion from its Bankruptcy Appellate Panel that could have been interpreted to mean that a decision in bankruptcy court reducing the amount of a nondischargeable debt is not enforceable outside of bankruptcy, the rules of *res judicata* or collateral estoppel to the contrary notwithstanding.

In chapter 13, a man listed his former wife as the holder of a priority unsecured domestic support obligation. The Missouri Division of Child Support Enforcement initially filed an unsecured priority claim for about $36,000. Believing it had incorrectly calculated the claim, the Division later filed an amended claim for over $88,000.

The debtor objected to the amended claim. The bankruptcy court disallowed the $88,000 claim and allowed the $36,000 claim, having concluded that the Department waived the excess under Missouri law by acquiescing to lower payments after the children were emancipated.

The debtor completed his five-year plan and got a discharge. The Department never appealed the disallowance order or the plan confirmation order.

After discharge, the Department began garnishing the debtor's salary to collect the disallowed $52,000. The bankruptcy court held the Department in contempt of the discharge injunction.

The BAP reversed, holding that the "discharge injunction does not apply to a nondischargeable domestic support obligation, even the disallowed portion." The debtor appealed and lost once more in an Aug. 22 opinion for the Eighth Circuit authored by Circuit Judge James B. Loken.

Judge Loken ducked the more significant issue regarding the preclusive effect of the bankruptcy court's ruling that the Department had waived the $52,000 claim under state law, because, he said, it was an appeal only from the contempt order, not the disallowance order.

With regard to contempt, Judge Loken said that the bankruptcy court could not use Section 105(a) to impose sanctions in contravention of specific statutory provisions, citing *Law v. Siegel*, 134 S. Ct. 188 (2014). He referred to Sections 523(a)(5) and 1328(c)(2) for the proposition that domestic support obligations "are not dischargeable under any circumstances," citing *United Student Aid Funds Inc. v. Espinosa*, 559 U.S. 260 (2010).

Together, those principles "eliminated the basis for the bankruptcy court's sanctions order," Judge Loken said.

In simple terms, the Eighth Circuit seems to say there is no contempt power available to enforce a bankruptcy court order reducing a nondischargeable claim.

Judge Lokens sidestepped the larger issue by refusing to "render an advisory opinion" on the preclusive effect of the bankruptcy court's order disallowing the additional claim for $52,000. Consequently, the circuit court expressed "no view on the merits of whether [the debtor] remains personally liable for the disallowed portion of [the Department's] bankruptcy claim." "These are not easy issues," he added.

With regard to whether the bankruptcy court even had jurisdiction to enforce its prior claim disallowance order, Judge Lokens said that *Local Loan v. Hunt*, 292 U.S. 234 (1934), "might give the bankruptcy court ancillary jurisdiction to enforce" that order. On the other hand, he said, the fact that domestic support claims are not dischargeable under any circumstances "puts a very different gloss on the issue," citing *Siegel*.

In substance, Judge Lokens might be saying that provisions of the Bankruptcy Code making some types of debt automatically nondischargeable may somehow divest the bankruptcy court of jurisdiction. Or, perhaps, the power of the bankruptcy court regarding nondischargeable claims does not extend beyond the bankruptcy case itself.

Although it is cold comfort for the debtor, Judge Lokens said that the state court was "fully competent" to rule on the preclusive effect of the bankruptcy court's disallowance order.

The opinion lends itself to a petition for rehearing *en banc*.

To read ABI's discussion of the BAP opinion and the dissent, click here.

The opinion is *Spencer v. State of Missouri Department of Social Services*, 868 F.3d 748 (8th Cir. Aug. 22, 2017).

A nondischargeability judgment under Section 523 doesn't require prejudgment interest at the lower federal rate.

Prejudgment Interest at the Higher State Rate Can Be Ok on Nondischargeability

If a creditor obtains a judgment after trial in bankruptcy court finding a debt nondischargeable for fraud, shouldn't the court award prejudgment interest at the federal rate because the award was made under federal law, Section 523(a)(2)(A)?

Answer: Not necessarily. The Ninth Circuit held that the bankruptcy court properly exercised discretion in awarding prejudgment interest at the higher state rate.

After litigating for two years in state court, the debtor filed bankruptcy on the eve of trial. The creditors sued in bankruptcy court, where they ultimately prevailed on their nondischargeability complaint when the bankruptcy judge awarded them damages plus prejudgment interest at the California rate of 7% rather than the 0.4% federal rate.

The Ninth Circuit Bankruptcy Appellate Panel upheld the larger interest award, and the debtor appealed again.

To no avail, the debtor contended that the bankruptcy court was obliged to award prejudgment interest, if any, at the lower federal rate because the claim was based on federal law, namely Section 523(a)(2)(A). The Ninth Circuit disagreed in a non-precedential, *per curiam* opinion on June 18, upholding the bankruptcy court's exercise of discretion.

The circuit court recited the general proposition that prejudgment interest is left to the sound discretion of the trial court, informed by "substantial evidence" regarding "considerations of fairness," with the goal of making "the wronged party whole."

The appeals court said the record "well supports" the bankruptcy court's exercise of discretion.

Relevant factors included the filing of bankruptcy on the eve of a trial that would have been held in state court, where the judge would have imposed prejudgment interest at the state rate. Moreover, the elements of fraud under California law "are much like the elements that must be shown in a nondischargeability proceeding," the circuit court said.

Were the case in federal court under diversity jurisdiction, the circuit court noted that "the California rate would have applied."

In April, we reported *Hamilton v. Elite of Los Angeles Inc. (In re Hamilton)*, 584 B.R. 310 (B.A.P. 9th Cir. April 17, 2018), where the Ninth Circuit BAP held that a creditor who obtains a pre-petition judgment on a debt that is later declared nondischargeable is entitled to post-judgment interest at the state rate throughout. To read ABI's discussion of *Hamilton*, click here.

The opinion is *Zenovic v. Crump (In re Zenovic)*, 17-60017 (9th Cir. June 18, 2018).

Fraudsters get no sympathy from the Sixth Circuit on dischargeability.

Penalties for Fraud Are Nondischargeable Despite **Chapter 13's 'Superdischarge'**

Penalties for fraudulently obtaining government benefits are nondischargeable despite the so-called superdischarge in chapter 13, according a May 29 opinion from the Sixth Circuit.

The circuit court was reviewing two cases with nearly identical facts. In both cases, an individual fraudulently obtained unemployment benefits by failing to disclose employment income. After discovering fraud, the state imposed orders of restitution and penalties for fraudulently obtaining unemployment benefits.

The restitution and penalties for one debtor were approximately $6,900 and $27,000, respectively, and $4,300 and $16,700 for the other. In other words, the penalties were about four times larger than the benefits that were fraudulently obtained.

In the debtors' chapter 13 cases, the state objected to the dischargeability of both the restitution awards and the penalties. The debtors conceded that the restitution awards were nondischargeable under Section 523(a)(2)(A) as money obtained by "false pretenses, a false representation, or actual fraud."

However, the debtors argued that the penalties were dischargeable in chapter 13 because they fell under Section 523(a)(7) as a "fine, penalty, or forfeiture payable" to a governmental unit that "is not compensation for actual pecuniary loss."

Although debts covered by Section 523(a)(7) are ordinarily nondischargeable, the superdischarge in Section 1328(a)(2) makes (a)(7) penalties dischargeable once chapter 13 debtors complete their plan payments. (Section 523(a)(2) debts are not covered by the superdischarge in Section 1328(a)(2) and remain nondischargeable in chapter 13.)

One bankruptcy judge ruled that the penalties were dischargeable, and the other held that they were not. On appeal in district court, the penalties were held nondischargeable.

Circuit Judge Eugene E. Siler, Jr. concluded that the penalties were nondischargeable.

Judge Siler was most persuaded by *Cohen v. de la Cruz*, 523 U.S. 213 (1998), where the Supreme Court held that treble damages for fraud are nondischargeable under Section 523(a)(2).

He described *Cohen* as holding that "penalties associated with fraud should be regarded as essentially the same as the fraud itself."

Judge Siler rejected several arguments offered by the debtors. To the contention that exceptions to discharge are construed strictly against the creditor, he said that bankruptcy benefits the "honest but unfortunate" debtor.

The debtors relied on the rule of construction that a more specific statute, like Section 523(a)(7), should control over the more general provision in Section 523(a)(2). However, Judge Siler found no authority for the proposition that a debt may not be covered by two subsections in Section 523(a). Indeed, he said the subsections are not mutually exclusive.

Significantly, Judge Siler read the Supreme Court's recent decision in *Husky International Electronics Inc. v. Ritz*, 136 S. Ct. 1581 (2016), to mean that a debt can be nondischargeable under both subsections (a)(2) and (a)(7).

Judge Siler held that the penalties arose "from fraud perpetrated against the Agency," thus making the penalties nondischargeable under subsection (a)(2).

In *Husky*, the Supreme Court held that a debt can be nondischargeable for "actual fraud" under Section 523(a)(2)(A) even if the debtor made no misrepresentation to the creditor. To read ABI's discussion of *Husky*, click here.

The opinion is *Andrews v. Michigan Unemployment Insurance Agency*, 16-2383 (6th Cir. May 29, 2018).

Bankruptcy court may overrule a state court that rules incorrectly on the discharge of a debt.

Sixth Circuit Expounds on a Loophole in the *Rooker-Feldman* Doctrine

The Sixth Circuit expounded on a loophole in the *Rooker-Feldman* doctrine that will sometimes allow a bankruptcy court to disregard a state court judgment upholding the validity and enforceability of a mortgage.

Named for two Supreme Court decisions, *Rooker-Feldman* means that federal courts lack subject matter jurisdiction to review judgments by state courts. In other words, someone cannot mount a lawsuit in federal court amounting to an appeal from a state court judgment.

In *Hamilton v. Herr* (*In re Hamilton*), 540 F.3d 367 (6th Cir. 2008), the Sixth Circuit laid down a rule dealing with situations where *Rooker-Feldman* collides with discharge under Section 524(a).

Hamilton involved a situation where a state court had ruled that a debt was not discharged. Could the debtor then ask the bankruptcy court, in effect, to overrule the state court and hold that the debt was discharged? Would the debtor's resorting to bankruptcy court violate *Rooker-Feldman*?

As Sixth Circuit Judge John M. Rogers said in his July 18 opinion, *Hamilton* means that "state courts may interpret discharge orders, but only if they do so correctly. Otherwise, they violate Section 524(a) by modifying the discharge order . . . . When a state court interprets the discharge order incorrectly, its judgment is void *ab initio* and therefore poses no *Rooker-Feldman* bar to subsequent review in the lower federal courts."

The applicability of *Hamilton* was the centerpiece of the appeal before the Sixth Circuit.

The Unrecorded Mortgage

In her chapter 7 petition in 2004, the debtor scheduled a second mortgage on her home as a secured claim. The debtor received her discharge, not knowing that the lender failed to record the mortgage until three months after bankruptcy. Recordation occurred about a month before discharge, thus apparently in violation of the automatic stay.

The debtor stopped paying the mortgage about two years after bankruptcy. More than 10 years after bankruptcy, the lender began foreclosure in state court. The state court ruled that the second

mortgage was valid and enforceable. Just before the foreclosure sale, the debtor filed a chapter 13 petition and initiated an adversary proceeding to avoid the lien under the Section 544(a) strong-arm powers.

The debtor proffered two theories. The bankruptcy court did not rule on the first, where she sought to avoid the mortgage under the strong-arm powers, contending that it was never properly perfected.

Instead, the bankruptcy court ruled in her favor on a second theory: that the mortgage had never attached because a nonstandard provision in the mortgage required recordation as a condition to attachment.

The Bankruptcy Appellate Panel reversed, based on *Rooker-Feldman*. Although the first theory was raised in the BAP, the panel did not rule on the issue, thus preserving the question for Sixth Circuit review. To read ABI's discussion of the BAP opinion, click here.

The Circuit's Opinion

To rule on the applicability of *Rooker-Feldman*, Judge Rogers analyzed both of the debtor's theories. He concluded that the doctrine precluded granting relief under the second theory but not the first.

The second claim – that the mortgage was unenforceable because the lien never attached – was barred by *Rooker-Feldman* because it amounted to an appeal from the state court's judgment that the mortgage was valid and enforceable. To rule in the debtor's favor, Judge Rogers said, "the bankruptcy court would need to reach a conclusion precisely opposite from the state court on the issue of whether the lien attached."

Consequently, *Hamilton* did not apply to that theory, because Section 524(a) "only protects debtors from being held *personally liable* for discharged debts," Judge Rogers said. [Emphasis in original.] The discharge injunction, he said, does not prohibit a creditor from foreclosing on a valid lien that existed before bankruptcy.

By upholding the validity of the lien, the state court in no manner affected the debtor's personal liability. Thus, the bankruptcy court improperly ruled in favor of the debtor.

On the other hand, Judge Rogers ruled that *Rooker-Feldman* did not prelude the bankruptcy court from granting relief under the strong-arm power. Recall that neither the bankruptcy court nor the BAP had ruled on that theory.

The strong-arm theory rested on the notion that the mortgage was never validly perfected because it was recorded in violation of the automatic stay. *Rooker-Feldman* therefore did not

apply, Judge Rogers said, because "it does not invite the bankruptcy court to review the state court's handiwork."

Judge Rogers went on to say that the "bankruptcy court could accept the state court's judgment as completely correct when entered, yet still rule for [the debtor] on the ground that the lien was never perfected."

Because the strong-arm theory had not been litigated, the circuit court reversed and remanded for the claim to "be decided in the first instance in the court or courts below." The appeals court expressed no view on the validity of the strong-arm theory.

The Chapter 13 Debtor's Standing

The lender argued on appeal that the chapter 13 debtor had no standing, contending that the strong-arm claim was property in the earlier chapter 7 case and was not part of the later chapter 13 estate.

The question of whether only the chapter 13 trustee could prosecute the strong-arm claim was not an issue because the trustee consented to the debtor's motion for derivative standing.

Judge Rogers said that the lender offered "no suggestion why [the strong-arm] claims would not have been included in" the chapter 13 estate. He said that the lender's argument was "inconsistent with the text of Section 544(a)[, which] indicates that Section 544(a) rights are granted anew each time the debtor files for bankruptcy."

The opinion is *Isaacs v. DBI-ASG Coinvestor Fund III LLC (In re Isaacs)*, 17-5815 (6th Cir. July 18, 2018).

Circuit court bases its decision on the omission of Section 523(a)(16) from Section 1328(a).

Chapter 13 Discharges Post-Filing Condo Assessments in the Ninth Circuit

Resolving a split among the lower courts in its jurisdiction, the Ninth Circuit ruled that condominium assessments coming due after a chapter 13 filing will be discharged when the debtor completes plan payments.

The debtor moved out of her condominium unit before filing a chapter 13 petition. Her plan called for surrendering the unit, which sat unoccupied for more than four years during the chapter 13 case. The lender eventually foreclosed about six months before the debtor completed her plan payments.

Before the debtor received her discharge, the condominium association brought suit to determine the dischargeability of the post-filing assessments that arose between the filing date and foreclosure. Affirmed in district court, the bankruptcy court ruled that the post-filing assessments arose post-petition and were not discharged.

The Ninth Circuit reversed in a July 10 opinion by District Judge Eduardo C. Robreno of Philadelphia, sitting by designation. An amendment to the statute by the Bankruptcy Reform Act in 1994 played a key role in the decision.

In the early 1990s, the Seventh and Fourth Circuits reached different results about post-filing assessments in chapter 7 cases. The Chicago-based court held that post-filing condominium assessments were dischargeable, theorizing that the obligations arose when the debtor purchased the unit before bankruptcy, even though the liability was unmatured and contingent on filing.

The Fourth Circuit split with the Seventh by holding that post-filing assessments were not dischargeable because they ran with the land and arose each month.

Congress intervened in 1994 on the side of the Fourth Circuit with Section 523(a)(16), which provides that condominium or cooperative assessments due and payable after filing are not dischargeable. By virtue of Section 523(a), that subsection is applicable to discharges in chapters 7, 11 and 12, but only to chapter 13 hardship discharges under Section 1328(b).

Significantly, the Section 523(a) exception from discharge is not applicable to the so-called superdischarge that the debtor received under Section 1328(a) upon completing her plan payments.

In deciding how to rule, Judge Robreno mentioned that a chapter 13 discharge is broader than the discharge in any other chapter. In addition, he said that bankruptcy is designed to provide a fresh start and that provisions in the Bankruptcy Code are to be construed liberally in favor of debtors.

Also in terms of policy, Judge Robreno said that the "definition of claim is very broad." Based on several factors, he concluded that post-petition assessments are prepetition claims even though they are unmatured and contingent on filing.

Judge Robreno said that the debtor's personal liability for post-filing assessments met the Ninth Circuit's "fair contemplation" test for categorizing claims as prepetition. He also noted that unmatured and contingent debts are discharged under Section 1328(a).

The liability for post-filing assessments, according to Judge Robreno, was created when the debtor purchased the unit, not as a "result of a separate, post-petition transaction."

In chapter 13, Judge Robreno said, the only exceptions to discharge are in Section 1328(a)(1)-(4). "Notably absent," he said, is a reference to Section 523(a)(16). He concluded that the omission of Section 523(a)(16) from Section 1328(a) "was purposeful."

Judge Robreno bolstered his conclusion that the assessments were dischargeable by reference to the legislative history accompanying Section 523(a)(16), where the House Report said that post-filing assessments are dischargeable "[e]xcept to the extent that the debt is nondischargeable under" Section 523.

Near the end of his opinion, Judge Robreno said there was "no legal basis for distinguishing between whether [the debtor] retained possession of her condominium unit post-petition and, thus, continued to enjoy the benefit of occupancy at no cost, or, instead, surrendered it at some point."

Read literally, the quotation might mean that a debtor could remain in possession of a condominium unit during chapter 13 and escape liability for assessments if the condominium association slept on its rights and did not take action to recover payments due after filing. However, the statement may only relate to Judge Robreno's rejection of the association's argument for liability based on notions of equity.

The opinion is *Goudelock v. Sixty-01 Association of Apartment Owners*, 16-35384 (9th Cir. July 10, 2018).

Courts are split on whether personal liability to produce suppliers results in a nondischargeable debt under Section 523(a)(4).

Personal Liability for a PACA Trust Is Dischargeable, Judge Mark Says

On an issue where the lower courts are split, a bankruptcy judge in Miami decided that officers of a produce wholesaler are not saddled with nondischargeable debts if suppliers of perishable agricultural commodities are unpaid.

Deciding a question he called "a close one," Bankruptcy Judge Robert A. Mark concluded that a trust created under the Perishable Agricultural Commodities Act (7 U.S.C. § 499a, *et seq*.), or PACA, does not give rise to a "technical trust" and therefore does not result in a nondischargeable debt under Section 523(a)(4) for committing fraud "while acting in a fiduciary capacity." Although the Eleventh Circuit has not ruled on the precise issue, Judge Mark interpreted authority from the Atlanta-based appeals court as mandating the outcome.

PACA and the Case at Hand

To protect farmers and suppliers who were usually unpaid when a fresh produce wholesaler declared bankruptcy, Congress originally adopted PACA in 1930 by imposing a floating trust on a purchaser's inventory and proceeds. Among other things, PACA creates a statutory trust protecting growers and suppliers by putting them ahead of accounts receivable lenders.

The chapter 7 debtors owned and operated a fresh produce wholesaler that was subject to PACA. Before bankruptcy, the officers had been sued under PACA by produce suppliers. The suit ended in a stipulation of settlement where the company and the officers took on joint and several liability for almost $300,000. When the officers later filed bankruptcy, little had been paid.

The produce suppliers sued in bankruptcy court to declare that the debt was nondischargeable under Section 523(a)(4). They contended that their produce, once sold, became the corpus of a PACA trust and that the debtors had fiduciary duties to ensure that enough proceeds remained to pay their invoices in full.

The debtors filed a motion to dismiss, which Judge Mark granted in his August 6 opinion.

Judge Mark's *Ratio Decidendi*

Judge Mark said the Bankruptcy Code does not define "fiduciary capacity." The "only clear consensus," he said, is that "acting in a fiduciary capacity means something more than simply having fiduciary duties." Citing *Quaif v. Johnson*, 4 F.3d 950, 953 (11th Cir. 1993), only a technical trust falls under Section 523(a)(4). Although courts agree there must be a technical trust, Judge Mark said there is no "consensus" about "what constitutes a 'technical trust.'"

In the Eleventh Circuit, Judge Mark said, a technical trust is not created involuntarily, like a resulting or constructive trust. Rather, a technical trust arises voluntarily, like an express trust.

Because Section 523(a)(4) pertains only to debts incurred "while acting" in a fiduciary capacity, Judge Mark said that a technical trust must exist before the alleged defalcation.

There is no technical trust under PACA, Judge Mark said, "until a court imposes additional duties . . . after a prior showing of malfeasance."

Critically, the Eleventh Circuit has held that PACA does not require segregation, allows comingling, and permits the use of trust assets for other purposes "prior to a showing of dissipation," Judge Mark said. The ability of a PACA dealer "to comingle trust assets with other assets precludes a finding that a PACA trust is a technical trust," the judge ruled. As additional support, he cited the Fifth Circuit for holding that the ability to use trust assets for another purpose "is fatal to finding that a technical trust exists."

Demonstrating the division of authority, Judge Mark cited the Sixth Circuit and the Ninth Circuit Bankruptcy Appellate Panel, which held in non-PACA cases that segregation is not required. He also conceded that "a majority of [lower] courts" have held that PACA trusts are technical trusts. He took issue with those decisions because, in his view, "an identified trust *res* without a segregation requirement is not enough."

As further support for his conclusion, Judge Mark cited the Fifth and Seventh Circuits, which both held that failure to pay proceeds of lottery ticket sales did not involve a technical trust.

Judge Mark ended his opinion by saying he would certify the question for direct appeal to the Eleventh Circuit.

The opinion is *Coosemans Miami Inc. v. Arthur (In re Arthur)*, 17-1378 (Bankr. S.D. Fla. Aug. 6, 2018).

Arbitration

New case seems inconsistent with Second Circuit's prior opinion compelling arbitration over an automatic stay violation.

Second Circuit Bars Arbitration in a Class Action for Violating the Discharge Injunction

Often solicitous of financial institutions caught up in bankruptcy litigation, the Second Circuit nonetheless held that the bankruptcy court properly exercised its discretion by refusing to allow arbitration in a class action alleging a violation of the Section 524 discharge injunction.

The unanimous opinion on March 7, written by Circuit Judge Rosemary S. Pooler, casts doubt on the continuing influence of *MBNA America Bank v. Hill*, 436 F.3d 104 (2d Cir. 2006). *Hill* stood for the proposition that a court in the Second Circuit must order arbitration in a class action alleging a willful violation of the Section 362 automatic stay.

The new decision from the Second Circuit came down two days after the Supreme Court issued its opinion in *U.S. Bank NA v. The Village at Lakeridge LLC,* 15-1509 (Sup. Ct. March 5, 2018), prescribing the standard of appellate review for mixed questions of law and fact. The Second Circuit did not cite *Lakeridge* and might have stated the standard of review differently had it analyzed the high court's new authority regarding bankruptcy appeals.

Judge Pooler's decision picked the winner between two district judges in New York who had reached diametrically opposite results on the same facts. Another winner is Bankruptcy Judge Robert D. Drain of White Plains, N.Y., who made the decision that was upheld by the Second Circuit on March 7.

The Class Action

An individual got a chapter 7 discharge covering credit card debt. Despite the discharge, the credit card lender continued reporting the debt as charged off rather than discharged in bankruptcy. After having received a discharge, the debtor reopened the chapter 7 case and filed a class action in bankruptcy court alleging that the failure to report the debt as discharged was an attempt at bringing pressure to repay the debt and thus violated the discharge injunction under Section 524 of the Bankruptcy Code.

The lender filed a motion to compel arbitration, relying on a provision in the credit card agreement calling for arbitration of "any controversy." Bankruptcy Judge Drain denied the motion to compel arbitration in May 2015, and the lender took an immediate appeal, permitted by the Federal Arbitration Act.

District Judge Nelson S. Román of White Plains upheld denial of the motion to compel arbitration. Interpreting *Hill*, he said that a bankruptcy judge has discretion to "override an arbitration agreement" if the lawsuit is a core proceeding based on provisions of the Bankruptcy Code that "inherently conflict" with the Federal Arbitration Act.

Judge Román found the lawsuit to be core, even though it was a class action, because "discharge is clearly a right created by federal bankruptcy law" and all class members were bankrupts. He next held that arbitrating claims under Section 524 "would necessarily jeopardize the objectives of the Bankruptcy Code."

In *Hill*, the Second Circuit had compelled arbitration in a class suit alleging a violation of the automatic stay when the debtor had received a discharge, the case had been closed, and the automatic stay was no longer in effect. Judge Román distinguished *Hill* because the case before him involved the discharge injunction, which is the "central purpose" of bankruptcy and remains in effect "even after the conclusion of the bankruptcy proceedings."

"[A]rbitration of a discharge violation would jeopardize this central objective," Judge Román said. To the *Hill* analysis, Judge Román added a fourth consideration: uniformity. He said that the need for uniformity was "compelling" because there could be "wildly inconsistent" results in arbitration.

In a case decided in October 2015 called *Belton v. GE Capital Consumer Lending Inc. (In re Belton)*, Vincent L. Briccetti reached the opposite result, also interpreting *Hill*. To read ABI's discussion of *Belton*, click here. Judge Briccetti and the Second Circuit both denied motions in *Belton* for leave to appeal.

As it turns out, the Second Circuit largely adopted Judge Román's logic, aided by an *amicus* brief submitted by Professors Ralph Brubaker, Robert M. Lawless and Bruce A. Markell and Tara Twomey of the National Consumer Bankruptcy Rights Center.

Mootness

The Second Circuit considered whether the appeal was moot because the lender was willing to update the credit reports for everyone in the class.

Judge Pooler ruled that the appeal was not moot because "the question presented and the relief sought both remain unsettled."

The ruling on mootness is significant because the result in *Hill* turned in part on the creditor's repayment of debt allegedly collected in violation of the automatic stay. Therefore, a defendant's ploy like the one in *Hill* may no longer suffice to kill off an appeal in the Second Circuit.

The Standard of Appellate Review

Next, Judge Pooler dealt with the standard of review, which she said "has been inconsistently or improperly applied by this Court."

Without citing *Lakeridge*, which had been decided two days earlier in the Supreme Court, and without analyzing whether the case presented mixed questions of law and fact, Judge Pooler said that the court would conduct *de novo* review of the core status of the suit. Similarly, she said, the review is *de novo* regarding the bankruptcy court's conclusion that arbitration would cause a "severe conflict" with the Bankruptcy Code.

After *Lakeridge*, appellate courts must decide that review is primarily legal in nature, rather than factual, before concluding that review is *de novo*. Judge Pooler did not undertake that analysis.

In deciding whether review is *de novo* or for clear error, *Lakeridge* tells appellate courts to examine whether review primarily entails a legal or factual analysis. Finding a "severe conflict" between arbitration and the Bankruptcy Code might entail either a legal or factual analysis.

Depending on the particular facts giving rise to the alleged violation of the discharge injunction, appellate review might invoke the plain error rule if the appellate court's task focuses more on the facts underlying the conclusion of "severe conflict."

The Merits

Hill taught that the court has discretion to disregard an arbitration agreement if the proceeding is core and presents a "severe conflict" with the Bankruptcy Code. In deciding whether the class plaintiff-debtor in the new cases should have been obliged to arbitrate, *Hill* therefore provided the legal precedent, but the facts in that case were "easily distinguished," Judge Pooler said.

Because the creditor conceded that the issue was core, Judge Pooler was only required to analyze whether Congress intended for the statutory right to a discharge to be non-arbitrable, thus giving the bankruptcy court discretion to refuse to compel arbitration.

Judge Pooler said that discharge is the "foundation" and the "central purpose" of bankruptcy. Therefore, arbitrating a claimed violation of the discharge injunction would "seriously jeopardize" the proceeding because (1) the discharge injunction is integral to providing a fresh start, (2) the claim was made in "an ongoing bankruptcy matter," and (3) the bankruptcy court's equitable power to enforce its own injunctions is "central to the structure of the Code."

Perhaps undercutting *Hill*, Judge Pooler said that the "putative class action does not undermine this conclusion" because the automatic stay in *Hill* had become moot by closing the debtor's bankruptcy case.

Attempting to distinguish *Hill*, Judge Pooler said that violation of the discharge injunction, as opposed to an automatic stay violation, offends "the central goal of bankruptcy," contrasted with a violation of the automatic stay, which is no longer in effect in a closed case.

Further, Judge Pooler said the discharge injunction was "still eligible for active enforcement," compared with the automatic stay, which had lapsed. Judge Pooler did not consider that damages could be sought for a violation of the automatic stay by reopening a closed bankruptcy case.

Without citation of authority, Judge Pooler said that the discharge injunction is "enforceable only by the bankruptcy court and only by a contempt citation." Arbitration therefore presented "an inherent conflict with the Bankruptcy Code," Judge Pooler said, because "the bankruptcy court alone has the power to enforce the discharge injunction."

Having found an "inherent conflict," Judge Pooler quickly concluded that the bankruptcy judge did not abuse his discretion in ruling out arbitration.

What Remains of *Hill*?

It is at least arguable that *Hill* should have required Judge Pooler to impose arbitration. Since the Second Circuit was not sitting *en banc*, her three-judge panel could not overrule *Hill*.

In *Hill*, the issue was also core, but the appeals court required arbitration, overruling the two lower courts.

The *Hill* court concluded that arbitration would not "seriously jeopardize the objectives of the Bankruptcy Code," in part because the automatic stay "is not so closely related to an injunction that the bankruptcy court is uniquely able to interpret and enforce." In the March 7 opinion, Judge Pooler neglected to note that the discharge injunction can be raised as an affirmative defense in any court.

Hill also found significance in the fact that the plaintiff's bankruptcy case had been closed. However, the debtor's case also had been closed in the appeal before Judge Pooler, but the bankruptcy judge had reopened the case to permit the filing of the class action.

Hill, therefore, may be limited in the future to class actions in district court seeking redress for violations of the automatic stay. *Hill* might not require arbitration if the debtor alone seeks damages for an automatic stay violation under Section 362(k), and *Hill* might not apply to a class action in bankruptcy court seeking redress for an ongoing violation of the automatic stay.

The March 7 decision presents an opportunity for the Second Circuit to sit *en banc*, either to set aside Judge Pooler's opinion or overrule *Hill* outright. However, *en banc* rehearing is exceedingly rare in the Second Circuit. Stay tuned nonetheless.

The opinion is *Credit One Bank NA v. Anderson (In re Anderson)*, 16-2496 (2d Cir. March 7, 2018); petition for *certiorari* filed June 5, 2018.

Wages & Dismissal

Dissenter contends that the majority misread the circuit's own precedent.

Ninth Circuit Creates Split on Appellate Standard for **'Consumer Debt' Determination**

Either creating a circuit split or accentuating an existing split, a divided panel of the Ninth Circuit disagreed on the standard of appellate review on appeal from an order from the bankruptcy court deciding whether an obligation is a consumer or business debt under Section 707(b)(1).

The issue is akin to the question in *U.S. Bank NA v. The Village at Lakeridge LLC,* 15-1509 (Sup. Ct.), where the Supreme Court will decide this term whether the standard of appellate review for non-statutory insider status is *de novo* or clearly erroneous, or a combination of both.

The appeal in the Ninth Circuit turned in large part on that court's own precedent in *Zolg v.Kelly (In re Kelly)*, 841 F.2d 908, 911 (9th Cir. 1988). The majority and the dissent couldn't even agree on what *Kelly* meant.

The majority read *Kelly* to mean that a home mortgage can be either a consumer or business debt, depending on the "primary purpose" of the loan. The dissent understands *Kelly* to mean that a home mortgage, as a matter of law, is always a consumer debt. The majority and dissent also disagree about the appellate standard prescribed by *Kelly*.

The Facts

A man who lived in Jackson, Wyo., had worked 25 years for a luxury hotel chain, earning $225,000 a year. Hoping for advancement to a more senior executive position, he applied for a job at a luxury resort in Aspen, Colo. Although offered a job in Aspen for $300,000, he could not afford either to rent or buy a home in Aspen, where home prices are higher than in Jackson.

The new employer sweetened the offer by granting him a $500,000 mortgage toward the purchase of a home in Aspen. The new employer also gave him a guaranteed annual bonus to cover the below-market interest on the loan.

He took the job, but his wife and children remained in Wyoming. The home he purchased in Aspen was too small for his entire family. He continued using banks in Wyoming and did not move the registration of his car to Colorado.

The man considered the house in Aspen to be a "placeholder" because his new employer was planning to develop a new resort in Jackson, allowing him to move back to Wyoming and join his family.

After the economy crashed in 2008, the new employer terminated plans for the new resort in Wyoming. Abandoning hope of returning to Wyoming, he sold his home in Jackson, and his family joined him in Aspen.

Four years after taking the job in Aspen, the man resigned and later filed a chapter 7 petition, owing $550,000 on the loan from his employer.

The employer moved to dismiss the chapter 7 petition for abuse under Section 707(b)(1), contending his debts were primarily consumer, thus making him ineligible and requiring him to convert the case to either chapter 13 or chapter 11 if he wanted a discharge eventually.

The bankruptcy judge held a trial and denied the motion to dismiss, concluding that the Colorado mortgage was a business debt, making him eligible for chapter 7 because his debts overall were "primarily" business debts. On appeal, the Ninth Circuit Bankruptcy Appellate Panel upheld the bankruptcy court.

The Majority Opinion

Writing for herself and Circuit Judge Marsha S. Berzon, Circuit Judge Morgan Christen upheld the BAP in an opinion on Oct. 16 that appears to mean that characterization of a debt as consumer or business is a fact to be found by the trial court and reviewed for clear error, not a legal conclusion that an appellate court can review *de novo* based on undisputed facts.

The employer contended that appellate review should be *de novo* because the underlying facts were undisputed. The employer also argued that a home mortgage is always a consumer debt. Judge Christen disagreed on both counts.

Judge Christen interpreted *Kelly* to mean that a court must divine the "primary purpose" of a debt in deciding whether the obligation is consumer or business. *Kelly* held, in her view, that home mortgages are usually but not always consumer debts. She disputed the dissenter's understanding of *Kelly* to mean that home mortgages are always consumer debts.

The debtor's "multiple motives" for taking the mortgage required the bankruptcy court to engage "primarily" in a "factual, rather than legal, inquiry." Since the decision in the bankruptcy court was essentially a factual inquiry, the appellate standard is clear error, Judge Christen said.

Judge Christen admitted that the courts are split on the standard of review, with the Eighth Circuit BAP also holding "that the purpose of a debt is a factual finding reviewed for clear error." The Fifth and Tenth Circuits, she said, hold to the contrary.

Judge Christen cited a number of undisputed facts to buttress the bankruptcy court's conclusion that the mortgage primarily had a business purpose. She therefore concluded that the bankruptcy

court did not clearly err in finding that the mortgage was "undertaken for a business purpose connected with furthering his career, rather than a personal, family or household expense."

The Dissent

Circuit Judge Jacqueline H. Nguyen dissented, saying that the majority applied "the wrong standard of review, creating a circuit split in the process."

Judge Nguyen interpreted *Kelly* as meaning, "in no uncertain terms," that the trial court makes a predominantly legal determination subject to *de novo* review when the facts are not in dispute. She counted the Fourth, Fifth, Sixth and Tenth Circuits as also holding that the characterization of consumer debt is subject to *de novo* review.

Beyond the appellate standard, Judge Nguyen said that the majority were wrong on the merits, because she understood *Kelly* to mean that "all loans to purchase a home are consumer debt."

Finality

Like the BAP, the appeals court addressed the question of whether denial of a motion to dismiss under Section 707(b) is a final order eligible for appeal to the circuit.

Without dissent from Judge Nguyen, Judge Christen followed the "majority of circuits" by holding that denial of a motion to dismiss under Section 707(b) is a final order because it conclusively determines a discrete issue resolving the debtor's eligibility for a discharge in chapter 7.

Judges Christen and Nguyen were both appointed by President Barack Obama.

In a similar case, *Bushkin v. Singer (In re Bushkin)*, 15-1285, 2016 BL 236937 (B.A.P. 9th Cir. July 22, 2016), the Ninth Circuit BAP classified living expenses as business debts if they were intertwined with a profit motive. The appeal to the circuit in *Bushkin* was being held in abeyance pending the decision in this case. To read ABI's discussion of *Bushkin*, click here.

The opinion is *Aspen Skiing Co. v. Cherrett (In re Cherrett)*, 873 F.3d 1060 (9th Cir. Oct. 16, 2017).

Although there may be standing to appeal, failure to object can bar an appeal under doctrines of waiver or forfeiture.

Ninth Circuit Widens Split on Failure to Object and Standing to Appeal

The Ninth Circuit explained when the failure to appear or object results in the loss of the right to appeal an order entered in bankruptcy court.

Basically, the failure to object or appear does not result in a loss of standing to appeal. Assuming there is a pecuniary interest at stake, standing on the sidelines instead can result in waiver or forfeiture, as District Judge Matthew F. Kennelly of Chicago explained in his May 29 opinion for the Ninth Circuit. Judge Kennelly was sitting by designation.

Although failure to appear or oppose may or may not result in loss of appellate standing depending on the circuit where the issue arises, the outcome often may end up being the same by invocation of the doctrines of waiver and forfeiture.

The Ninth Circuit Case

A chapter 7 trustee filed a motion to assume an executory contract. Individuals who had a pecuniary interest in the contract were given notice, but they did not file an objection, nor did they appear in court in opposition. At the hearing, the bankruptcy judge announced he would grant the motion as being unopposed.

Before the bankruptcy judge signed an assumption order, the individuals filed a motion for reconsideration, stating reasons for denying the assumption motion. Rather than treat the failure to oppose as a default, the bankruptcy judge denied the reconsideration motion on the merits.

After entry of the assumption order, the individuals appealed. The district judge dismissed the appeal for lack of standing, ruling that the appellants were not aggrieved parties because they had not opposed or appeared in opposition to the assumption motion.

Judge Kennelly reversed and remanded.

The Circuit Split on Standing

The district court relied on *dicta* from a 1985 Ninth Circuit opinion saying that objecting or appearing in bankruptcy court is "usually" a prerequisite to being an "aggrieved person" with standing to appeal. That case, however, was decided on other grounds.

Judge Kennelly said that the circuits are split on whether attendance or objection are prerequisites to being an aggrieved person with standing to appeal. The Seventh Circuit requires objection to confer appellate standing, while the Fourth Circuit does not, he said.

Siding with the Fourth Circuit, Judge Kennelly said, "We do not automatically toss a litigant out of court for noncompliance with a trial court rule without allowing the litigant to explain why the noncompliance should be excused."

Bankruptcy standing, according to Judge Kennelly, concerns whether someone is "'aggrieved,' not whether one makes that known to the bankruptcy court." He therefore held that "an appellant's failure to attend and object at a bankruptcy court hearing has no bearing on the question of whether that appellant has standing to appeal."

Although failure to attend and object may result in waiver or forfeiture, "it does not present a jurisdictional standing issue," Judge Kennelly said.

Although they are often used interchangeably, Judge Kennelly said that waiver and forfeiture are different concepts. Forfeiture is the failure to assert a right in a timely fashion, while waiver is the intentional relinquishment or abandonment of a right.

Because the appellants had objected in their motion for rehearing, Judge Kennelly said they had not waived their arguments against assumption. On the other hand, he said, "the question of forfeiture is open for determination on remand."

Since the appellants clearly had a pecuniary interest, they had standing to appeal. On remand, Judge Kennelly instructed the district court to decide whether the appellants forfeited their opposition to the assumption motion and whether the bankruptcy court's order should be reversed for plain error.

The opinion is *Harkey v. Grobstein (In re Point Center Financial Inc.)*, 16-56321 (9th Cir. May 29, 2018); rehearing and rehearing *en banc* denied July 12, 2018.

New York judge rules that the **IRS Handbook** *is not controlling on auto expenses for the means test.*

On the Means Test, a Single Debtor Can Take Deductions for Two Cars

On an issue dividing the lower courts, Bankruptcy Judge Alan S. Trust of Central Islip, N.Y., ruled that a single individual can claim a deduction for two automobiles in calculating the means test to determine whether the debtor's case represents "presumptive abuse."

The U.S. Trustee filed a motion to dismiss, contending that the debtor could take a deduction for only one automobile. If one of the deductions were eliminated, the debtor would have failed the means test, and his case would have been dismissed for presumptive abuse under Section 707(b)(2) unless he were to convert to chapter 13.

In his Jan. 11 opinion, Judge Trust analyzed the case as a question of statutory construction.

On line 11 of Form 122A-2, the debtor claimed ownership of two cars. On line 12, he listed auto expenses of $616, the exact amount shown on the IRS Local Standards for the New York metropolitan area for someone who owns two cars.

The trustee argued that the court instead should follow the *IRS Handbook*, which allows a single person a deduction for only one car.

Judge Trust said that Section 707(b)(2)(A)(ii)(1) does not tell the court to refer to the *IRS Handbook*. Rather, he said, the subsection says the deduction "shall be" determined by the National and Local Standards. The Local Standards applicable to autos allow a deduction for one or two autos "and [do] not expressly limit a single-person household debtor's operation costs to one vehicle," the judge said.

The "fact that the *IRS Handbook* could be read to conflict with the statute and official form is irrelevant for a presumed abuse case, because Congress did not expressly build the *IRS Handbook* into the statute nor did the Judicial Conference of the U.S. build the *IRS Handbook* into the official form," Judge Trust said.

Consequently, Judge Trust found no presumed abuse because he allowed the single debtor with no dependents to take deductions for the two autos he owned. He held that "the *IRS Handbook* is not controlling and in fact would be at odds with the Means Test as defined, none of which limit a single-person-household debtor to one vehicle expense where the debtor actually owns or leases two or more vehicles."

The opinion is *In re Addison*, 16-74856, 2018 BL 10506 (Bankr. E.D.N.Y. Jan. 11, 2018).

On dismissal before chapter 13 confirmation, the debtor gets undistributed funds, not a creditor with a valid state court levy.

Section 1326(a)(2) Overrides a Levy Under State Law

On an issue where the courts are split, a district judge in Virginia upheld the bankruptcy court's ruling that a chapter 13 trustee must return undistributed funds to the debtor, rather than honor a garnishment under state law, if the case was dismissed before a plan was confirmed.

Owing a state agency more than $74,000 for child support arrears, a man filed a chapter 13 petition. After filing, he sent about $3,000 to the trustee. With the debtor unable to craft a confirmable plan, the bankruptcy court dismissed the case.

After dismissal and while the trustee was still holding the $3,000, the state agency served a garnishment order on the trustee. The debtor objected, contending he was entitled to a return of the funds under Section 1326(a)(2).

When the trustee sought instructions, the bankruptcy court decided that the money should go to the debtor. The state agency appealed and obtained a stay pending appeal.

In an opinion on Oct. 19, District Judge Norman K. Moon of Lynchburg, Va., agreed with the bankruptcy judge.

Judge Moon framed the question as being whether the court should follow Section 1326(a)(2) or honor an otherwise valid levy under state law.

Eliminating exceptions that do not apply when a chapter 13 case is dismissed before confirmation, Judge Moon quoted Section 1326(a)(2) to say that the trustee must "return any such payments . . . to the debtor . . . ." That language, he said, "is determinative."

To the state agency's argument that the termination of the automatic stay on dismissal allows a levy on the debtor's property, Judge Moon said that Section 362 "does not contradict or muddle Section 1326(a)(2)'s statement about who gets the funds."

Next, the state argued that the trustee was obliged to comply with state law under 28 U.S.C. § 959(b). The state's argument failed under the Constitution's Supremacy Clause, Judge Moon said, because state law contradicts the mandate of Section 1326(a)(2).

Finally, Judge Moon justified his conclusion by referring to policy as reflected in *Harris v. Viegelahn*, 135 S. Ct. 1829, 1835 (2015), where the Supreme Court said that a debtor should not be penalized for pursuing chapter 13 voluntarily.

The opinion is *Commonwealth of Virginia v. Beskin*, 17-028 (D. Va. Oct. 19, 2017).

Large student loans do not justify dismissal of a chapter 13 case when chapter 11 is the only alternative, Bankruptcy Judge Janet S. Baer says.

Chicago Judge Erases Chapter 13 Debt Limits on Student Loans

If an individual's debts are principally student loans, there should be no debt limit in chapter 13, according to Bankruptcy Judge Janet S. Baer of Chicago.

In her Dec. 27 opinion, Judge Baer created a bankruptcy remedy where none otherwise would exist for an individual who is swamped by student loans but would be ineligible for chapter 7.

The chapter 13 debtor owed about $570,000 on student loans and another $22,500 on credit cards. He was living paycheck to paycheck, Judge Baer said. His monthly take-home pay of some $2,700 left him with about $475 in disposable income.

Under an income-based repayment plan, the debtor had been repaying his student loans at the rate of $268 a month. If he continued the payments for 25 years, any unpaid balance would be forgiven. The amount of his monthly payment would increase or decrease depending on a rise or fall in his income.

The trustee moved to dismiss, because the debtor's unsecured liabilities exceeded the maximum of $394,725 in "noncontingent, liquidated, unsecured" debt permitted in chapter 13 by Section 109(e).

Claiming that the student loans were contingent, the debtor argued that he was within the chapter 13 debt limit. He contended that the student loans were contingent because a portion could be forgiven in the future.

Judge Baer didn't buy the contingent argument. In the Seventh Circuit, a debt is noncontingent "if the event giving rise to liability has already occurred." The debt, she said, came into existence when the debtor signed the loan agreement. "It is the possibility of forgiveness that is contingent," the judge said, "not the debt itself."

Nonetheless, Judge Baer said, Section 109(e) by itself does not require dismissal. That section only contains chapter 13 eligibility standards.

Dismissal is governed by Section 1307(c), which says that the court "may" convert to chapter 7 or dismiss for "cause." It then lists 11 nonexclusive grounds representing dismissal for cause. Failure to meet the debt limit in Section 109(e) is not one of the listed factors.

Analyzing whether there was cause to dismiss, Judge Baer surveyed the evolution of chapter 13. Citing legislative history, she said that the debt limits were added "to keep debtors with large businesses from filing chapter 13 cases." The debt limits shunt owners of large businesses into chapter 11, where there are more creditor protections.

Concern for creditor protection does not exist when an individual debtor has large educational debt, Judge Baer said. Indeed, unsecured creditors of student loan debtors would prefer chapter 13 because they might realize some recovery compared to chapter 7. Student loan lenders would not be harmed because student loans ordinarily are not discharged in chapter 13. In addition, caselaw allows a debtor to put student loans in a separate class with potentially higher payments than those to unsecured creditors.

Judge Baer noted how the unsecured debt limit in chapter 13 has risen only 7.6% a year since 1978, while the cost of post-secondary education has risen 20.7% annually. The result has been an explosion in student loan debt, a fact that did not exist in 1978 with adoption of the Bankruptcy Code.

Judge Baer found no "cause" for dismissal, in part because the "express language of Section 1307(c) does not require the court to dismiss." Furthermore, not dismissing would be in the best interest of creditors, the estate and the debtor.

The debtor, she said, can remain current on his student loans in chapter 13 while he pays some of his future earnings to general unsecured creditors.

If the debtor were ineligible for chapter 7, the debtor would have no viable bankruptcy alternative absent chapter 13, since conversion to chapter 11 would impose "substantial fees" on the debtor. In addition, Judge Baer said, chapter 11 entails "'too cumbersome a procedure' that is simply not suited for a reality such as his."

The opinion is *In re Pratola*, 578 B.R. 414 (Bankr. N.D. Ill. Dec. 27, 2017).

With no circuit authority, lower courts are split on the fate of standing trustees' fees when a chapter 13 case is dismissed before confirmation.

No Statutory Fees for Standing Chapter 13 Trustees if Dismissal Precedes Confirmation

With no authority as yet from the courts of appeals, the lower courts are divided on the right of a standing trustee to retain his or her statutory fees if a chapter 13 case is dismissed before confirmation.

Bankruptcy Judge Mary Ann Whipple of Toledo, Ohio, decided that the "plain language" of Section 1326(a)(2) takes precedence over 28 U.S.C. § 586(e), which "lacks such clarity," she said.

The case involved joint chapter 13 debtors who paid about a $10,500 to the standing chapter 13 trustee. The plan was never confirmed, and the case was dismissed. The bankruptcy court approved the trustee's final report and dismissed the case, calling for the trustee to retain about $900 in statutory fees and return the remainder to the debtors.

One of the debtors sought reconsideration, disallowance of the trustee's statutory fees, and disgorgement of the fee that the trustee had retained.

In her Sept. 29 opinion, Judge Whipple said that the *Handbook for Chapter 3 Standing Trustees*, published by the Executive Office of the U.S. Trustees, provides no guidance. If a chapter 13 case is dismissed before confirmation, the *Handbook* says that the standing trustee must reverse the payment of the percentage fee "if there is controlling law in the district requiring such reversal."

The *Handbook* is equivocal because, as Judge Whipple said, the two controlling statutes point in different directions.

Section 1326(a)(2) says that if a plan is not confirmed, "the trustee shall return any [payments made by the debtor] not previously paid out and not yet due and owing to creditors . . . to the debtor, after deducting any unpaid claim allowed under Section 503(b)."

Seemingly to the contrary, Section 586(e) provides that the standing trustee "shall collect such percentage fee from all payments received by [the standing trustee] under plans in the cases under" chapters 12 and 13.

Judge Whipple said that none of the courts of appeals had resolved the conflict in the two sections, and the lower courts are in disagreement. She said there is no controlling law in her district.

In deciphering which statute to follow, Judge Whipple said that the "plain language of Section 1326 is clear." When a chapter 13 case is dismissed before confirmation, she said that use of the word "shall" requires the standing trustee "to return all such payments, including the statutory percentage fee being held by the trustee, after deducting any allowed administrative expense claims."

By comparison, Judge Whipple said that Section 586(e)(2) "lacks such clarity," in part because it deals with collection but not ultimate disposition.

Consequently, Judge Whipple granted the motion for reconsideration, modified the dismissal order, and required the trustee to pay the statutory fee to the debtor.

The opinion is *In re Lundy*, 15-32271, 2017 BL 347466 (Bankr. N.D. Ohio Sept. 29, 2017).

Plans & Confirmation

Split decision allows a lender to take property out of an estate automatically.

Eleventh Circuit Requires No Objection to Overturn a Final Confirmation Order

In the words of the dissenter, the Eleventh Circuit penned an opinion on Dec. 11 “that will impede the effectiveness of our bankruptcy system and will undermine its purpose.”

The majority held that property covered by Georgia’s pawn statute, although remaining in the debtor’s possession, automatically drops out of the estate once the redemption period elapses. Even a chapter 13 plan is incapable of paying the lender’s claim in full and allowing the debtor to retain his car.

More surprisingly, the majority held that the title lender was not required to file an objection to confirmation of the plan. Although the lender also did not appeal confirmation of the plan, the majority nonetheless held that the confirmed plan did not bind the creditor because the lender had previously filed a motion to declare that the car was no longer estate property.

The decision has a number of shortcomings, among them the majority’s lack of discussion of Section 541(b)(8), which gives only limited protections to pawn brokers and title lenders. The opinion does not explain why a confirmed plan is not binding and thereby insinuates that a creditor need not oppose confirmation if a related issue is in litigation.

The majority opinion, written by a circuit judge appointed by President Donald Trump, means that states can pass laws eviscerating debtors’ rights under the Bankruptcy Code by taking property automatically out of the estate. The opinion also says that state laws prevail unless Congress has shown an intent for the Bankruptcy Code to be paramount.

The Typical Title Loan

The debtor obtained a loan before bankruptcy, secured by the title to his car, but he retained possession of the car. Before the redemption period elapsed under state law, the debtor filed a chapter 13 petition. The debtor did not pay off the title loan within the additional 60 days provided by Section 108(b).

Georgia’s automobile pawn statute gives the borrower a 30-day grace period after maturity to redeem the car. If not redeemed, title automatically passes to the lender.

After the additional 60 days had run, the lender filed a motion to declare that the car was no longer property of the estate and to modify the automatic stay permitting repossession of the car.

The debtor opposed the motion, which was not decided before the bankruptcy court confirmed the chapter 13 plan.

The lender had filed a secured claim. Approved by a confirmation order that the lender did not appeal, the plan provided for paying the claim in full with interest at 5%.

At the hearing on the stay relief motion after confirmation, the lender conceded that it had not objected to confirmation. The bankruptcy judge denied the stay relief motion, holding that the car remained property of the estate even after expiration of the extended redemption period. The bankruptcy court also held that the lender was bound by the confirmed plan.

The district court affirmed, holding that the chapter 13 plan could modify the lender's rights. To read ABI's discussion of the district court opinion, click here.

The Eleventh Circuit reversed in a Dec. 11 opinion by Circuit Judge Kevin Newsom. Judge Newsom was Articles Editor for the *Harvard Law Review*. After clerking on the Ninth Circuit, he clerked on the Supreme Court for Justice David H. Souter.

The Plan Was Not Binding

Judge Newsom first ruled that the plan was not binding because the title lender had not "slept on its rights" by failing to object to confirmation of the plan.

"[O]n the unique facts of this case," Judge Newsom said, the lender's motion to modify the stay "adequately preserved its position." He said there was "no substantive difference between the styled-as-such [objection to confirmation] that the dissent would seemingly require and the motion for relief [from the stay that the title lender] actually filed."

The lender "put the *substance* of its position . . . squarely before the bankruptcy court," Judge Newsom said. [Emphasis in original.] He went on to say that the lender was not required to file a confirmation objection to preserve the contention that the car was no longer estate property, because that issue "was adequately teed up" in the stay relief motion.

Although Judge Newsom said the facts of the case were "unique," his opinion could be interpreted to mean that previously filed pleadings in chapter 11 or 13 cases will suffice as confirmation objections, although not denominated as such. Evidently, the bankruptcy judge must scour the docket for pleadings raising issues that might also pertain to confirmation.

Even if the lender had preserved the issue, Judge Newsom's opinion does not explain why the appeal was not moot as a consequence of the confirmation order that the lender did not appeal.

The Car 'Dropped Out' of the Estate

Next, Judge Newsom held that the car "dropped out" of the estate by "the 'automatic' operation of Georgia's pawn statute." He said that a "clear majority" of lower courts have held that property subject to a pawn statute can cease automatically to be estate property.

Judge Newsom cited *Butner v. U.S.*, 440 U.S. 48, 55 (1979), and *Barnhill v. Johnson*, 503 U.S. 393, 398 (1992), for the proposition that property interests are created and defined by state law. However, he did not mention *Barnhill's* more important holding that federal law nonetheless determines the time of a transfer, an issue not discussed but pertinent to the case at hand.

Since state law automatically divests an owner of title, Judge Newsom said that the Bankruptcy Code could alter the outcome "only if we find some clear textual indication that Congress intended that result."

The "likeliest candidate," Judge Newsom said, was the automatic stay. Section 362(a), though, "has no application to the particular circumstances of this case," he said.

Although conceding that "some courts" have held that the automatic stay tolls an unexpired redemption period, Judge Newsom cited Section 108(b) as making the automatic stay inapplicable. Were it otherwise, he said, the general would control the specific, and Section 108(b) would be superfluous.

Although the automatic stay prevents creditors from prying assets out of the estate, Judge Newsom said "it does not separately prevent those assets from evaporating on their own — as here, 'automatically' — pursuant to the ordinary operation of state law."

Next, Judge Newsom said that Section 541 does not freeze estate property as of the filing date. The statute, he said, "neither clearly says nor unambiguously implies . . . that a bankruptcy estate, once created, necessarily remains static."

Finally, Judge Newsom held that Section 1322(b)(2) "has no field of application in this case." Although that section allows a chapter 13 plan to modify the claims of secured creditors, it did not apply because the car was no longer estate property by the time of confirmation.

Joining Judge Newsom's opinion was District Judge Federico A. Moreno from the Southern District of Florida, sitting by designation.

The Dissent

Circuit Judge Charles R. Wilson, appointed by President Bill Clinton, dissented, saying this "should be an easy case," because "a confirmed chapter 13 bankruptcy plan enjoys a preclusive, binding effect."

The law, he said, "required an objection before plan confirmation, not a retroactive recasting of motions as objections."

Judge Wilson pointed to the lender's concession in bankruptcy court and the bankruptcy judge's consequently finding that the lender had not filed an objection to confirmation. Reviewed for clear error, that finding, he said, "is insurmountable." He also said there was "ample evidence to support the fact that [the lender] *affirmatively declined* to object." [Emphasis in original.]

Therefore, Judge Wilson said he would have ruled that the lender was "bound by the confirmed plan."

Taking the stay relief motion as a confirmation objection, Judge Wilson said, means that "judges will need to scour the docket prior to each confirmation hearing."

Next, Judge Wilson cited *United Student Aid Funds Inc. v. Espinosa*, 559 U.S. 260 (2010), for the idea that even an "illegal" plan provision binds a creditor.

With regard to the question of estate property, Judge Wilson said that "state law cannot operate to alter the bankruptcy estate after its creation — and it certainly cannot serve to dispossess the bankruptcy estate of property."

On the filing of the chapter 13 petition, the lender had a secured claim that the debtor could modify under Section 1322(b)(2). Congress, Judge Wilson said, "provided no mechanism for property of the estate to evaporate."

Judge Wilson pointed to Section 541(b)(8) as authority for the idea that the car remained estate property. That section was added along with the BAPCPA amendments in 2005 to give additional protections to pawn brokers and title lenders.

Section 541(b)(8) says that estate property does not include tangible property, other than written evidences of title, if the property is collateral for a loan, the property is in the possession of the lender, the debtor has no obligation to repay the loan, and the debtor has not redeemed the property within the time provided by state law.

Judge Wilson said that the section would have applied if the lender were in possession of the car, but that was not the case.

The majority cited Section 541(b)(8), but as evidence of a situation where property can drop out of the estate automatically. Arguably, Congress intended for Section 541(b)(8) to be the only circumstance when a title lender or pawn broker can automatically obtain title to property after bankruptcy, and that section by its terms was inapplicable to the case at hand.

Overview

The majority opinion gives states the ability to write laws automatically taking property out of a bankruptcy estate. Theoretically, states could make reorganization impossible in chapter 13 or chapter 11 by transferring all manner of property automatically to lenders or other creditors.

By requiring specific evidence that Congress intended for the Bankruptcy Code to override state law, the majority would make bankruptcy law less uniform and more a reflection of the idiosyncrasies of state law. Judge Newsom seemed to import rules regarding implied repeal of federal statutes to cases involving federal preemption of state law.

The majority opinion in some ways resembles *WD Equipment v. Cowen (In re Cowen)*, 849 F.3d 943 (10th Cir. Feb. 27, 2017), where the Tenth Circuit held that passively holding an asset of the estate, in the face of a demand for turnover, does not violate the automatic stay in Section 362(a)(3) as an act to "exercise control over property of the estate." The majority opinion and *Cowen* both chip away at the primacy of the Bankruptcy Code and diminish debtors' rights and remedies.

The issue decided in *Cowen* is on direct appeal to the Tenth Circuit in *Davis v. Tyson Prepared Foods Inc. (In re Garcia)*, 17-3247 (10th Cir.), where the debtor will presumably ask for *en banc* argument or rehearing. For ABI's discussion, click here.

A debtor who does not redeem a car is not without relief. Presumably, the loan typically would be far smaller than the value of the car, thus allowing the debtor to mount a constructive fraudulent transfer suit against the lender. Nonetheless, the cost of an avoidance suit will be greater than and in addition to the cost of confirming a plan. Notably, a pawn broker or title lender entitled to retain property is still subject to an avoidance action under Section 541(b)(8).

The opinion is *Title Max v. Wilber (In re Wilber)*, 876 F.3d 1302 (11th Cir. Dec. 11, 2017), petition for rehearing *en banc* denied Feb. 14, 2018.

On direct appeal, Seventh Circuit upholds Bankruptcy Judge Thorne by allowing chapter 13 debtors to retain anticipated refunds from earned income tax credits.

Seventh Circuit Allows Anticipated Tax Refunds to Be Offset by Expenses in Chapter 13

Affirming Bankruptcy Judge Deborah L. Thorne on direct appeal, the Seventh Circuit held that a chapter 13 debtor can prorate an earned income tax credit in calculating disposable income and may offset the tax refund income with "reasonably necessary expenses to be incurred throughout the year."

The appeals court rejected the chapter 13 trustee's argument that the tax credit should be turned over in full to allow an extra payment to creditors, without deduction for any expenses.

The Poverty Level Debtor's $4,000 Tax Credit

A single mother of three children, the below-median income debtor had an annual income of about $30,000, well below the median income threshold of $87,000 in Chicago. Calculating projected monthly income, the debtor included a proration for her anticipated earned income tax credit of about $4,000 a year.

After several amendments to her schedules, the debtor proposed a 48-month plan paying her creditors $74 a month, an amount equal to her calculation of monthly disposable income. Creditors would receive a total of about $6,000. In other words, the plan would have paid creditors three or four times more were the tax refunds earmarked in full for creditors, without deduction.

In calculating disposable income, the debtor in substance included several one-time expenses that she could not incur or pay without using the earned income tax credit, such as buying beds for her sons, who were sleeping on air mattresses. The appeals court said that the additional expenses allowed the debtor to "retain some, or even all, of her tax credits."

Even with the extra income from the tax refund and the additional expenses, Judge Thorne found that the debtor had "a pretty skinny budget overall."

The chapter 13 trustee objected to confirmation, arguing that the debtor should turn over the entire amount of the earned income tax refund when received to fund additional payments to creditors.

Consolidating three chapter 13 cases raising identical issues, Judge Thorne overruled the objections and confirmed the debtors' plans in March 2017. Judge Thorne later certified an issue for direct appeal. The Seventh Circuit agreed to hear the direct appeal, saying there was no authority from the Supreme Court or the Seventh Circuit saying whether tax credits are disposable income.

Interestingly, the trustee and the debtor agreed that tax credits are disposable income. Prompting a dissent from one judge on the panel, the appeals court nonetheless went on to decide the next question: Can a debtor prorate tax credits to be offset by anticipated expenses?

The Seventh Circuit Opinion

In his March 22 opinion, Circuit Judge Joel M. Flaum agreed with the parties and held that tax credits are included in "currently monthly income," as defined in Section 101(10A)(A) and referred to in Section 1325(b)(1).

Nonetheless, Judge Flaum said that including tax credits within currently monthly income "does not mean that the debtor must pay the entire tax credit to the trustee as disposable income."

To retain some or all of the tax refunds, the trustee argued that the debtor must file a motion to amend the plan every time a refund comes in. Judge Flaum said that Judge Thorne rejected that idea "to alleviate the burdens that the motion-to-modify process imposes on trustees, debtors, and the court."

Judge Flaum likewise rejected the argument, relying on *Hamilton v. Lanning*, 560 U.S. 505 (2010), where the Supreme Court adopted a "forward-looking approach" and said that "the court may account for changes in the debtor's income or expenses that are known or virtually certain at the time of confirmation."

Judge Flaum said that Judge Thorne "properly allowed *Lanning* to calculate [the debtor's] projected disposable income," because her receipt of the tax credit refund was "virtually certain."

On the other hand, Judge Flaum said, the trustee's argument "is just another version of the rigid mechanical approach the Supreme Court rejected in *Lanning*." In contrast, Judge Thorne's approach of offsetting expenses against anticipated tax refunds "is exactly the kind of forward-looking approach that the Supreme Court endorsed in *Lanning*."

In a two-page opinion, Circuit Judge Daniel A. Manion concurred in part and concurred in the judgment, but not in a fashion undercutting the holding regarding the treatment of expenses to offset tax refunds.

Judge Manion said the circuit should not have accepted the case because the trustee and the debtor agreed on the issue that Judge Thorne certified for direct appeal. However, he concurred with the remainder of the opinion, holding "that the bankruptcy court did not abuse its discretion in overruling the trustee's objections to the debtor's chapter 13 plan." He would have expressed no opinion "on whether the earned income tax credit qualifies as income under the Bankruptcy Code" because there was "no adverse briefing on the issue and the resolution would not affect the outcome."

The opinion is *Marshall v. Blake*, 17-2809 (7th Cir. March 22, 2018).

Courts are also split on whether a five-year plan begins on confirmation or on the first chapter 13 plan payment.

Colorado Judge Differs with Two Circuits on Chapter 13 Payments Beyond Five Years

Disagreeing with the Third and Seventh Circuits, Bankruptcy Judge Elizabeth E. Brown of Denver held that the bankruptcy court lacks discretion to allow a final payment on a chapter 13 plan more than five years after the first plan payment.

A couple confirmed a chapter 13 plan obligating them to pay about $900 a month for five years. Less than a year after confirmation, the husband lost his job. The court approved a modified plan lowering the monthly payment to $10, with a proviso that the couple file amended schedules and an amended plan within 30 days after the husband got a new job.

When the husband was employed again, they informed their bankruptcy lawyer, but he had forgotten about the proviso.

After the couple completed their plan payments, the chapter 13 trustee remembered the proviso, analyzed their tax returns, and calculated a $17,000 shortfall had the couple amended the plan on time.

The debtors and the trustee agreed to a stipulation allowing the couple to pay off the $17,000 over several months after the final plan payment. Without advance approval from the court, the couple went ahead and paid the additional $17,000 so they could obtain a chapter 13 discharge.

In her Jan. 23 opinion, Judge Brown declined to approve the stipulation but converted the case to chapter 7, where the couple nonetheless may obtain a discharge.

Judge Brown tackled two major questions on which the courts are split. First, she was tasked with deciding when the clock on the five years begins to run. If the period begins with the first payment after confirmation, the $17,000 payment would have fallen within the five-year window and she would have approved the stipulation, giving them a chapter 13 discharge.

Unfortunately for the debtors, Judge Brown sided with those courts that start the clock running with the first payment after filing, thus causing the $17,000 payment to occur beyond five years.

If the five years begins running on the first payment after confirmation, debtors would be saddled with "additional burdens," Judge Brown said, because they would be making monthly payments for more than five years, since confirmation usually does not occur at the first

confirmation hearing. We recommend reading Judge Brown's opinion in full text to appreciate her reasoning for deciding that the clock begins running on the first plan payment after filing.

Judge Brown was therefore required to address the second question: Does the court have discretion to allow a final payment beyond five years?

The Third and Seventh Circuits have found discretion to allow a final payment after five years. *See In re Klaas*, 858 F.3d 820 (3d Cir. 2017); and *Germeraad v. Powers*, 826 F.3d 962 (7th Cir. 2016). For ABI's discussion of those cases, click here and here.

Judge Brown instead adopted the conclusions of the Tenth Circuit Bankruptcy Appellate Panel and several bankruptcy courts that do not permit payments outside of five years. Although Judge Brown was technically not bound by the Tenth Circuit BAP, ruling otherwise would have assured a reversal were she appealed.

Again, we recommend reading the opinion in full on the issue of discretion to make a late payment.

Even if she had sided with the circuit courts, Judge Brown said she would not have changed her ruling.

The debtors were not blameless, she said, because they made lower payments for three years after the plan should have been modified to increase the monthly payments. The debtors, she said, were "not directly culpable for this failure because they timely informed their attorney."

Nevertheless, she said, the clients "must be held accountable for the acts and omissions of their attorney."

Judge Brown also said she did not want to "send a message to other debtors that they are free to ignore plan requirements when it suits them and then cure the default . . . if discovered by the trustee or some other party."

The opinion is *In re Humes*, 11-39684, 2018 BL 35274 (Bankr. D. Colo. Jan. 23, 2018).

Eleventh Circuit inveighs against harming innocent creditors by invoking judicial estoppel.

En Banc, Eleventh Circuit Narrows Applicability of Judicial Estoppel in Bankruptcy

At the urging of one of the judges on the original panel, the Eleventh Circuit sat *en banc* and reversed two of its prior decisions by holding that a court must consider all the facts and circumstances before invoking the doctrine of judicial estoppel. To prevent a defendant from reaping an "unjustified windfall," the intentional failure to list a claim belonging to a bankrupt no longer results in the automatic application of judicial estoppel.

Even after the Sept. 18 opinion by Circuit Judge Jill Pryor, the Eleventh Circuit still has not gone as far as the Fifth Circuit when the New Orleans-based court sat *en banc* and functionally held in *Reed v. City of Arlington*, 650 F.3d 571 (5th Cir. 2011), that a defendant in a lawsuit cannot assert judicial estoppel to inflict harm on a bankruptcy trustee and innocent creditors based on a debtor's shortcomings.

The Facts

A woman initiated an employment discrimination suit two years before filing a chapter 7 petition. The employer learned about the bankruptcy and filed a motion to dismiss based on judicial estoppel, because the debtor had not scheduled the lawsuit among her assets. The debtor modified her schedules to list the claim, and the chapter 7 trustee retained the debtor's litigation counsel as special counsel to pursue the suit on behalf of the estate.

The debtor then converted her case to chapter 13 and confirmed a plan, but the chapter 13 case was dismissed when the debtor failed to make plan payments.

Invoking judicial estoppel, the district court dismissed the discrimination suit. Recognizing that it was bound by Eleventh Circuit precedent, the appeals court's three-judge panel upheld dismissal in February 2016 in an unsigned, 32-page *per curiam* opinion.

One of the three judges on the panel, Circuit Judge Gerald B. Tjoflat, wrote a special concurrence that reads like a dissent. He urged the appeals court to rehear the case *en banc* and overrule two Eleventh Circuit precedents that he believed were "wrongly decided." Anyone confronted with an issue involving judicial estoppel should study Judge Tjoflat's 78-page concurrence from last year, because it reads like a treatise discussing everything there is to know on the subject.

The appeals court granted rehearing *en banc*, heard argument in February and reversed its own precedents in Judge Pryor's 33-page opinion.

'Mockery' No Longer Automatic

Judge Pryor began by reaffirming the circuit's general rule that judicial estoppel applies when a litigant takes inconsistent positions and intends "to make a mockery of the judicial system." Her opinion focused on the mockery element because the debtor unquestionably took inconsistent positions by originally omitting the suit from her schedules.

Under the circuit's *Barger* and *Burnes* decisions from 2003 and 2002, respectively, Judge Pryor said that the mockery element was conclusively established by a debtor's nondisclosure, "even if the plaintiff corrected his bankruptcy disclosures after the omission was called to his attention and the bankruptcy court allowed the correction without penalty."

Judge Pryor devoted her opinion to explaining why the court was reversing *Barger* and *Burnes* and holding that the court instead "should consider all the facts and circumstances," including the "plaintiff's level of sophistication, his explanation for the omission, whether he subsequently corrected the disclosure, and any action taken by the bankruptcy court concerning the nondisclosure." She said that "voluntariness alone does not necessarily establish a calculated attempt to undermine the judicial process."

In refusing to impose judicial estoppel reflexively, Judge Pryor seemed largely motivated to avoid giving "an unjustified windfall" to "an otherwise liable civil defendant," in the process harming "innocent creditors." She recognized that *pro se* debtors may not understand how the requirement for disclosing contingent and unliquidated claims also means claims that the debtor holds, not just claims against the debtor.

Judge Pryor explained why courts should not automatically apply judicial estoppel even in chapter 13 cases. Because the debtor must satisfy the best interests test to confirm a plan, creditors in chapter 13 would be harmed just like in chapter 7 if a claim by the debtor is treated as worthless.

Is a *Cert* Petition Next?

Judge Pryor said there is a split of circuits even after abandoning *Burnes* and *Barger*. Like her court now holds, the Sixth, Seventh and Ninth Circuits previously ruled that the "mockery" element requires showing more than an intention not to disclose.

The Fifth and Tenth Circuits, she said, take the opposite view by endorsing "the inference that a plaintiff who omitted a claim necessarily intended to manipulate the judicial system."

Judge Pryor may have overstated the circuit split.

The *en banc* opinion in *Reed*, written for the Fifth Circuit by Circuit Judge Carolyn King, laid down a "general rule that, absent unusual circumstances, an innocent trustee can pursue for the benefit of creditors a judgment or cause of action that the debtor fails to disclose." She also said that judicial estoppel must be applied "flexibly" to achieve "substantial justice," a principle that Judge Tjoflat advocated in his concurrence in the Eleventh Circuit's original decision last year.

In substance, the applicability of judicial estoppel is now virtually irrelevant in the Fifth Circuit when a trustee is prosecuting a previously undisclosed claim for the benefit of creditors. The Fifth Circuit also endorsed the idea of precluding a culpable debtor from benefitting from successful prosecution by directing any recovery exclusively toward creditors.

Therefore, the Fifth Circuit's pre-*Reed* automatic invocation of judicial estoppel may no longer be good law in that circuit. Even if it is, the principle has little relevance after *Reed*, which permits recoveries on undisclosed claims to benefit innocent creditors.

Consequently, the Tenth Circuit may be the only circuit functionally at odds with four other circuits. As such, there may not be a fully developed, entrenched split warranting a grant of *certiorari*. For lack of a final order, a *certiorari* petition also would be premature at this juncture because the circuit remanded for more than ministerial duties.

The *Amicus* in the Eleventh

Supporting the debtor, J. Erik Heath of San Francisco submitted an *amicus* brief in the Eleventh Circuit on behalf of the National Association of Consumer Bankruptcy Attorneys. In addition to explaining how Eleventh Circuit precedent had gone beyond the purpose of judicial estoppel, he recommended adopting the approach in *Reed* by granting a trustee standing to pursue a claim not available to a debtor in view of judicial estoppel.

Unfortunately, Judge Pryor did not cite *Reed* or consider how that case might inform the relief available on remand. Although the Eleventh Circuit "may not have explicitly gone the route of *Reed*," Heath told ABI in an email that he believes it's "part of the result." He also praised the appeals court for overruling *Barger* and thereby allowing "trustees to escape judicial estoppel."

Remand to the Panel

When a circuit court reverses, it ordinarily remands to the trial court. But not here.

Judge Pryor remanded the case to the original three-judge panel "to consider whether the district court abused its discretion in applying judicial estoppel *and to resolve any other remaining issues*." [Emphasis added.]

The mandate to consider other issues should allow the three judges to opine on a result like *Reed*, where creditors can benefit but the debtor cannot.

To read ABI's discussion of the panel decision from February 2016, click here.

The opinion is *Slater v. U.S. Steel Corp.*, 12-15548, 2017 BL 327629, 130 FEP Cases 727 (11th Cir. Sept. 18, 2017).

Lower courts split three ways on 401(k) contributions and the calculation of disposable income in chapter 13.

District Court Allows 401(k) Contributions in Chapter 13 Up to the IRS Limits

On an issue where there is a dearth of appellate authority, District Judge Elizabeth Erny Foote of Shreveport, La., sided with the majority of bankruptcy courts by holding that voluntary post-filing contributions to a 401(k) plan are not included in a chapter 13 debtor's calculation of disposable income so long as the contributions do not exceed the amounts allowed by the Internal Revenue Service.

The appeal demonstrates the obstacles that the Supreme Court erected in *Bullard v. Blue Hills Bank*, 135 S. Ct. 1686 (S. Ct. 2015), to appeals from orders denying confirmation of chapter 13 plans.

The husband and wife debtors filed a chapter 13 plan where the husband would make voluntary 401(k) contributions throughout the life of their five-year plan, deducting the payments from the calculation of disposable income in determining the amount to be paid to creditors. The bankruptcy judge denied confirmation, because the contributions represented 12% of the husband's gross income. However, the bankruptcy judge said he would confirm a plan with a 3% contribution.

The bankruptcy judge confirmed the plan after the debtors amended their plan by reducing the 401(k) contribution to 3%. The debtors then appealed confirmation of their own plan. The debtors could not appeal from denial of their first plan because *Bullard* holds that denial of confirmation is not a final order.

Reversing the bankruptcy court's limitation on retirement plan contributions in her May 23 opinion, Judge Foote meticulously laid out the legislative quagmire on the question of whether 401(k) payments can be deducted from the calculation of disposable income in Section 1325(b)(2)(A). Statutory interpretation is further complicated by the hanging paragraphs added to Section 541(b)(7) by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

Courts have three answers to this question. Judge Foote said that a majority allow debtors to shelter contributions not exceeding the limits allowed by the IRS. A second group of courts do not allow deductions for retirement plans, and the third permits contributions not larger than the debtor was making before filing.

Judge Foote followed the majority approach, because she read the plain meaning of the statute as demonstrating "that Congress intended to exclude retirement contributions from available disposable income as defined by the code in Section 1325(b)."

Judge Foote had another holding of significance for debtors, stemming from the bankruptcy judge's finding that the plan was not filed in good faith given the size of the retirement plan contributions.

Judge Foote held that "the amount contributed by a debtor within the legal limits established by the Internal Revenue Service cannot be the sole basis for determining that a plan has been filed in bad faith." She remanded the case for the bankruptcy judge to make a redetermination of good faith based on the appropriate Fifth Circuit standard.

We recommend reading the opinion in full text for Judge Foote's thoughtful analysis of the statute and case law on all sides of the issue. The opinion is available at 2018 U.S. Lexis 86761 or 2018 BL 183240.

Editorial comment: Now that traditional employer-sponsored pensions are rapidly disappearing and being replaced by 401(k)s, courts that effectively prohibit or limit voluntary pension contributions are sentencing debtors to poverty in their retirements. This writer doubts that Congress intended for the effects of chapter 13 to persist so long after the completion of plan payments. (The foregoing commentary reflects the opinion of the writer, not ABI.)

The opinion is *Miner v. Johns*, 17-879 (W.D. La. May 23, 2018).

Compensation

In the Fifth Circuit, chapter 7 trustees lock in higher compensation.

Fifth Circuit Holds that Chapter 7 Trustees Presumptively Get Statutory Commissions

The Fifth Circuit sided with the Seventh by holding that the statutory commission for a chapter 7 trustee in Section 326(a) is presumptively reasonable and must be allowed by the bankruptcy court except in exceptional circumstances that "should be a rare event."

Since the 2005 BAPCPA amendments to Section 330, Circuit Judge Leslie H. Southwick said in his Jan. 26 opinion that two approaches have developed regarding the allowance of commissions for a chapter 7 trustee. Led by the Seventh Circuit, some courts, he said, hold that the sliding-scale commissions in Section 326(a) are "not simply a maximum but also a presumptively reasonable fixed commission." Some of those courts nonetheless say that the commission can be adjusted in "extraordinary circumstances."

Other courts do not view the commission rate as presumptively reasonable but allow compensation, functionally speaking, after applying the "reasonableness" standards in Section 330(a)(3).

Judge Southwick explained that the 2005 amendments removed a chapter 7 trustee from the professionals explicitly subject to the Section 330(a)(3) factors. Those standards still apply to chapter 11 trustees and other professionals.

Although Section 330(a)(1)(A) still says that a trustee must be allowed "reasonable compensation" for "actual, necessary" services, the BAPCPA amendments also added Section 330(a)(7), which provides that in "determining the amount of reasonable compensation to be awarded to a trustee, the court shall treat such compensation as a commission, based on Section 326."

While Judge Southwick did not say so, the amendments generally were viewed as ensuring that a trustee in a lucrative case would receive the maximum commission to make up for "no asset" cases entailing nothing more than the $60 flat fee under Section 330(b).

Judge Southwick decided to follow the Seventh Circuit, believing that the amendments established a "commission-based award" as opposed to the "compensation-based awards" granted pre-BAPCPA. To continue fixing "reasonable" compensation after BAPCPA, he said, would give "little practical effect to the amended language."

Judge Southwick held, “Section 330(a)(7) therefore treats the commission as a fixed percentage, using Section 326 not only as a maximum but as a baseline presumption for reasonableness in each case.”

He recognized that “Section 330 still allows a reduction or denial of compensation,” but only in a “rare event” where “‘exceptional’ is the key.”

The opinion is *LeJeune v. JFK Capital Holdings LLC (In re JFK Capital Holdings LLC)*, 16-31151, 2018 BL 27630 (5th Cir. Jan. 26, 2018).

Ethical issues abound when a committee counsel's own financial interest conflicts with its client's interests.

Ninth Circuit Requires Explicit Objection to Avoid Forfeiting an Appeal

Ostensibly to avoid a conflict with its own client, the attorneys for a creditors' committee forfeited the right to appeal because the firm did not explicitly lodge an objection on its own behalf to a structured dismissal that left the estate with nothing to pay fees.

In an opinion on July 25, the Ninth Circuit expounded on a circuit split the appeals court had widened on May 29 in deciding *Harkey v. Grobstein (In re Point Center Financial Inc.)*, 890 F.3d 1188 (9th Cir. May 29, 2018); rehearing and rehearing *en banc* denied July 12, 2018. To read ABI's discussion of *Point Center*, click here.

The proposed settlement before the Ninth Circuit in the new appeal may have been defective under *Czyzewski v. Jevic Holding Corp*., 137 S. Ct. 973 (2017). To lodge and preserve a *Jevic* objection, counsel for the committee might have been required first to withdraw as attorneys for the creditors, then oppose a transaction that was beneficial to its former clients. Laudably more loyal to unsecured creditors than to its own financial interest, the committee's counsel did not withdraw and did not object on their own behalf, thus losing the ability to appeal, according to the Ninth Circuit.

The New Ninth Circuit Case

A chapter 11 trustee had been appointed for a corporate debtor that owned valuable real estate. The trustee negotiated a so-called structured dismissal where the lender would take title to the property in exchange for secured debt. The lender agreed to carve out $150,000 for distribution to unsecured creditors and another $350,000 to pay the trustee and his professionals.

With dismissal the eventual result, the estate would have nothing to pay other chapter 11 administrative expenses, such as fees earned by counsel for the debtor and the committee. The $350,000 was couched as a surcharge against the lender's collateral under Section 506(c). By skipping over administrative claimants, the $150,000 payment to unsecured creditors had no similar statutory justification.

The bankruptcy court approved the sale before the Supreme Court handed down *Jevic*.

At the hearing to approve the sale, counsel for the debtor and committee filed objections for their clients. However, the firms did not file written objections on their own behalf. At the hearing, both firms stated that they were representing their clients and never said they objected to the sale in their own right as administrative creditors.

After the bankruptcy court approved the sale, the two firms filed notices of appeal on their own. No appeal was filed on behalf of the debtor or the committee. There being no stay pending appeal, the sale closed.

On a first appeal, the district court dismissed the appeal, finding that the two firms did not have standing because they had not appeared and objected on their own in bankruptcy court.

Point Center

While the appeal was pending from the district court's dismissal, the Ninth Circuit decided *Point Center*. On a circuit split, the Ninth Circuit took the side holding that attendance or objection are not prerequisites to being an aggrieved person with standing to appeal. Although the appellant had standing, the Ninth Circuit held in *Point Center* that the appellant's failure to object in bankruptcy court nevertheless could result in waiver or forfeiture. The circuit court remanded the case for the lower courts to determine whether the appellant had forfeited the right to appeal.

Forfeiture Found in the New Case

On the question of whether the firms had forfeited their right to appeal, the opinion for the Ninth Circuit by Sixth Circuit Judge John M. Rogers, sitting by designation, said that neither firm had "explicitly objected" to the sale in bankruptcy court. Ordinarily, he said, the circuit would remand for the lower court to determine whether there was forfeiture.

According to Judge Rogers, the case at hand was "unusual" because the elements of forfeiture had been thoroughly briefed and argued, albeit in the context of "attendance and objection" in bankruptcy court. The record, he said, was therefore "sufficient" for deciding whether there had been forfeiture.

Although the bankruptcy court on its own was concerned with how other administrative claims would be paid, Judge Rogers said there was no "clear indication" at the approval hearing that the two firms were appearing or objecting on their own behalf. He said there was a "total failure to inform the bankruptcy court that they intended to pursue their own interests."

Despite the bankruptcy judge's concern that committee counsel would not be paid, Judge Rogers said that the "contextual evidence . . . is simply not enough to undo what the record makes clear: the law firms were at the hearing and objecting on behalf of their clients."

Avoiding a conflict was also used against the committee's counsel. Like the district court, Judge Rogers doubted that the committee's counsel would have created a conflict with its own client by raising an objection that the money earmarked for unsecured creditors instead should be applied to chapter 11 administrative expenses. The "logical conclusion," Judge Rogers said, was that the firm was appearing and objecting only on behalf of the committee, which believed that the sale price was too low.

For Judge Rogers, the dispositive fact was the lack of "any evidence" that someone appeared or objected in bankruptcy court on behalf of the firms or "otherwise informed the bankruptcy court" that someone was representing the two firms.

Having decided that the firms forfeited their objection, Judge Rogers added belt and suspenders by reaching the merits and finding no clear error by the bankruptcy court in ruling that the trustee and his professionals were entitled to payment under Section 506(c), which allows a surcharge against a lender's collateral. He also ruled that the settlement was in the best interests of unsecured creditors because the trustee had been unsuccessful in selling the property to anyone aside from the secured lender.

The Unresolved *Jevic* Question

Were the committee's counsel oblivious to a conflict with its own clients, the firm could have argued that earmarking for unsecured creditors violated the principle that *Jevic* later ratified.

Here are ethics questions that are left unresolved: (1) During negotiations on the sale, how could the committee's counsel have avoided an ethical problem by negotiating on the firm's own behalf and seeking to redirect some or all of the $150,000 to the payment of administrative expenses?; (2) Since the committee was objecting to the sale price as inadequate, could the firm have objected on *Jevic* grounds without violating an ethical obligation?; (3) After the deal was struck, could the firm have withdrawn as counsel for the creditors' committee before the approval hearing and opposed a settlement that was beneficial to its own former client? (N.B.: The bankruptcy judge, according to Judge Rogers, refused to allow committee counsel to withdraw alongside filing an appeal.); and (4) Did appealing violate an ethical obligation to the committee?

The opinion is *Reed & Hellyer APC v. Laski (In re Wrightwood Guest Ranch LLC)*, 16-56856 (9th Cir. July 25, 2018).

Section 502(b)(4) shields debtors from overreaching lawyers in a new context.

Bankruptcy Judge Regulates the Unregulated Debt-Reduction Service Industry

A bankruptcy judge on Long Island, N.Y., interpreted Section 502(b)(4) to mean that a debt-reduction service provider ordinarily will not have an allowable claim based on the client's outstanding debt when the client files bankruptcy.

Bankruptcy Judge Robert E. Grossman of Central Islip, N.Y., described the debt-reduction service business as a "rapidly growing" industry "with little to no regulation" that serves clients who are "often unsophisticated, have limited means, and are facing severe financial hardship."

The service provider filing a claim in the case before him was a licensed attorney who, according to Judge Grossman, was "operating in a professional manner."

The husband and wife clients, who later filed a chapter 13 petition, came to the service provider with about $125,000 in unsecured debt. Among other things, the written agreement called for the clients to pay 39% of any negotiated debt reductions and a 20% flat fee based on total outstanding debt if the agreement were terminated.

Over 13 months before bankruptcy, the service provider took $1,450 a month from the debtors' bank account. The payments, totaling $18,850, covered the $2,900 flat fee for setting up the account plus a 39% contingency fee of $5,339 for debt reductions that were negotiated before bankruptcy. The service provider had applied the remainder toward the payment of claims that were settled.

The clients filed bankruptcy a month after terminating the agreement. The service provider filed a claim for about $17,250, representing the 20% contingency fee that was due on termination based on outstanding debt. The service provider conceded that he had been paid in full for the negotiated debt reductions.

The debtors objected to the claim because they were proposing a 100% plan. Judge Grossman sustained the objection in his May 18 opinion and expunged the claim in its entirety, nonetheless recognizing that the court must be "sensitive to the rights attorneys have to enter into a written agreement."

Judge Grossman did not reach the issue of whether the fee arrangement was enforceable under state law or whether it was an unenforceable penalty.

Instead, he said the controversy was governed by Section 502(b)(4), which disallows a claim "for services of an . . . attorney of the debtor, [if] such claim exceeds the reasonable value of such services."

Judge Grossman reasoned that the "reasonable value" of service in Section 502(b)(4) should be measured "under both a federal standard and under state rules of professional conduct." Because the debtors had filed a legally sufficient claim objection, he said the burden shifted to the creditor to prove that the amount of the claim was reasonable.

Since the creditor had been fully compensated for services provided to the debtors before filing, Judge Grossman said he could "think of no scenario where a $17,248.03 flat fee for termination, in addition to the guaranteed minimum fee already paid, would constitute reasonable value for debt reduction services for unsettled debts."

Judge Grossman said his conclusion "furthers the stated purpose" of Section 502(b)(4) "to prevent overreaching by attorneys to the detriment of unsecured creditors in bankruptcy." The result, he said, "also protects the unsophisticated debtor facing severe financial hardship."

The opinion is *In re Regino*, 16-74352 (Bankr. E.D.N.Y. May 18, 2018).

Split grows on whether 'substantial contribution' claims are limited to chapters 9 and 11.

"Substantial Contribution" Claim Allowed in Chapter 13

Swimming against the tide and deepening a split of authority, courts in Michigan granted an administrative claim to a creditor for making a "substantial contribution" in a chapter 13 case, when Section 503(b)(3)(D) only explicitly authorizes claims of that type in chapters 9 and 11.

As retained counsel for a chapter 7 trustee, a law firm objected to an exemption claimed by husband and wife debtors in annuities worth about $100,000. Before the objection was adjudicated, the debtors converted the case to chapter 13. The firm was not retained in the chapter 13 case.

When the chapter 13 trustee didn't pursue the objection, the law firm did. Ultimately, the bankruptcy court disallowed the exemption. As a result, the debtors were forced to amend their plan and provide for 100% payment to unsecured creditors.

The law firm then sought allowance of an administrative claim for having made a substantial contribution to the chapter 13 case.

The bankruptcy court in Michigan allowed the "substantial contribution" claim in the amount of about $23,000 for the lawyers' work during the chapter 13 case, relying on *Mediofactoring v. McDermott* (*In re Connolly North America LLC*), 802 F.3d 810 (6th Cir. Sept. 21, 2015), where the Sixth Circuit held that bankruptcy courts have discretion to allow an administrative claim to a creditor in chapter 7 who made a substantial contribution.

On appeal, the debtors argued it was error to allow a "substantial contribution" claim in chapter 13, because Section 503(b)(3)(D) only explicitly authorized allowance of an administrative claim for making a "substantial contribution in a case under chapter 9 or 11 of this title." The debtors also contended that *Mediofactoring* was not controlling because that case involved chapter 7, and they were in chapter 13.

Relying on *Mediofactoring*, District Judge Paul D. Borman of Detroit rejected the debtors' arguments in an opinion on Nov. 15 and upheld the bankruptcy court's allowance of a "substantial contribution" claim.

Mediofactoring, according to Judge Borman, stands for the proposition that use of the word "including" in Section 503(b) "confers discretion on a bankruptcy court to award administrative expenses on a case-by-case basis, and that the express mention of Chapter 9 and Chapter 11 in

Section 503(b)(3)(D) does not negate that fact." He also said, "Nothing about the statutory interpretation in [*Mediofactoring*] is unique to the Chapter 7 context."

Judge Borman said that a "substantial contribution" claim is allowable outside of chapters 9 and 11 depending upon "the totality of the pertinent facts, and the relevant equitable considerations."

There was "no question," Judge Borman said, that the law firm conferred a substantial benefit because creditors stand to recover 100% as a result of disallowance of the exemption claim. Because the chapter 13 trustee did not object to the exemption, the lawyers benefitted the estate when no one else was willing to do so.

Judge Borman also rejected the argument that *Lamie v. U.S. Trustee*, 540 U.S. 526, 124 S. Ct. 1023, 157 L. Ed. 2d 1024 (2004), bars allowance of the administrative claim. There, the Supreme Court held that Section 330(a)(1) precludes allowance of compensation to a debtor's counsel from estate funds if the attorneys were not retained under Section 327.

Lamie, Judge Borman said, dealt with payment of compensation under Section 330(a)(1), while the case before him was based on Section 503(b), "a different statutory provision entirely." He said there was no authority for the notion that *Lamie* "has anything to do with Section 503(b)(3)(D)."

Recently, a bankruptcy court in California followed *Mediofactoring*, joined the minority, disagreed with the Third Circuit, declined to follow its own Bankruptcy Appellate Panel, and found discretion to allow a "substantial contribution" claim in chapter 7. *In re Maqsoudi*, 566 B.R. 40 (Bankr. C.D. Cal. April 3, 2017). For ABI's discussion of *Maqsoudi*, click here. To read about *Mediofactoring*, click here.

The opinion is *Sharkey v. Stevenson & Bullock PLC (In re Sharkey)*, 17-11237, 2017 BL 409909 (E.D. Mich. Nov. 15, 2017).

Exemptions

Fourth Circuit avoids a result that would have left some debtors ineligible for any exemptions.

Three Circuits Approve Extraterritorial Application of **a State's Exemptions**

Joining the Eighth and Ninth Circuits and handing down another debtor-friendly opinion, the Fourth Circuit cleaned up some of the mess that Congress made in Section 522(b)(3)(A) regarding exemptions claimed by individuals who change their domicile before filing bankruptcy.

The May 4 opinion by Circuit Judge Robert B. King rejected plausible interpretations of the statute that could leave some debtors ineligible for any exemptions, state or federal.

The debtor moved to West Virginia from Louisiana four months before filing bankruptcy. Utilizing Louisiana's exemption statute, he claimed exemptions for about $3,500 of personal property located in West Virginia.

The trustee objected to the exemptions, contending that Louisiana exemptions could not be applied extraterritorially in view of the Supreme Court's presumption against extraterritoriality. The bankruptcy court allowed the exemptions and was upheld on appeal by District Judge Irene M. Keeley of Clarksburg, W.Va.

Again upholding the exemptions in the circuit court, Judge King characterized Judge Keeley's opinion as "well reasoned" and "comprehensive." To read ABI's discussion of Judge Keeley's opinion, click here.

The Statutory Mess

Attempting to prevent abuse, Congress made a hash out of Section 522(b)(3)(A) and compounded the problem by adding the so-called hanging paragraph, which, Judge King said, "has been the subject of some dispute in the bankruptcy courts."

Generally, a debtor is eligible for exemptions in the state where the debtor had been domiciled for 730 days before bankruptcy. To deter exemption shopping by people who would move within two years before bankruptcy to take advantage of another state's more generous exemptions, Section 522(b)(3)(A) provides that the debtor must take exemptions from the state where he or she resided for the largest part of the 180-day period before the 730-day period.

The statute had a problem, however, because Section 522(b)(3)(A) would leave some debtors eligible for no exemptions. To fill the gap, Congress added the hanging paragraph, which allows

the debtor to claim federal exemptions specified in Section 522(d) if (b)(3)(A) makes a debtor ineligible for any state's exemptions.

The Case at Hand

The trustee conceded that the debtor could invoke Louisiana exemptions under Section 522(b)(3)(A) for property located in Louisiana. However, the trustee disputed the claim for exemptions covering the debtor's property in West Virginia, even though Louisiana does not limit the application of its exemptions to Louisiana residents or to property in Louisiana.

The trustee argued for the presumption against extraterritoriality, also known as the anti-extraterritoriality approach, under which a bankruptcy court may not give extraterritorial effect to any state's exemption laws. His theory would have precluded the debtor from using Louisiana law to exempt property in West Virginia.

The Fourth Circuit's Analysis

Judge King said that "almost all courts" have rejected the trustee's theory because it "would lead to nonsensical results." An example: Debtors who move would be ineligible for exemptions because they likely would have no property in their former domicile, the only state in which they could have exemptions under the anti-extraterritoriality approach. Judge King said that the only bankruptcy court to adopt this theory was "promptly overturned on appeal."

The second minority view, called the preemption approach, would permit a debtor to apply a state's exemption laws to nonresidents and out-of-state property, even if state law does not allow extraterritorial effect. Like Judge Keeley, Judge King rejected the idea. If "Congress had intended to override state laws limiting the use of exemption schemes to in-state residents or in-state property, it would not have placed the hanging paragraph in Section 522(b)(3)," he said.

The preemption approach, he said, would make the hanging paragraph applicable only to debtors who had resided in foreign countries.

Judge King adopted the so-called state-specific approach, which is followed by the Eighth and Ninth Circuits and a majority of courts. He said it best embodies congressional intent and the bedrock principle that "exemptions are entitled to the most liberal construction in favor of the debtor."

Judge King said there were no principles of Louisiana law that would bar out-of-state debtors from utilizing Louisiana's exemption statute. He also rejected the trustee's reliance on the Supreme Court's presumption against extraterritoriality.

Citing Fourth Circuit precedent, Judge King said that the presumption does not apply to conduct that occurs largely within the U.S. Therefore, he allowed the debtor to rely on Louisiana law and exempt property in West Virginia.

A Proposal to 'Fix' Section 522

In the circuit court, *pro bono* co-counsel for the debtor was Eugene Wedoff, the immediate past president of American Bankruptcy Institute and a former bankruptcy judge in Chicago.

In a message to ABI, Judge Wedoff said that "Section 522 is very much in need of a Congressional 'fix.'"

Judge Wedoff believes that Congress should "make the debtor immediately subject to the exemption law of the state to which a debtor has moved, but cap the homestead exemption and perhaps other very large exemptions for two years after the move at the level set by the debtor's former state of domicile."

Judge Wedoff said that his proposal would "eliminate the 'millionaire's loophole' that Congress was concerned about in BAPCPA without creating the confusion caused by applying a state's exemptions to debtors who are no longer domiciled in that state."

The "simplest fix," Judge Wedoff said, would be "a set of uniform federal exemptions, but that is very unlikely to be politically possible."

The opinion is *Sheehan v. Ash*, 17-1867 (4th Cir. May 4, 2018).

After rehearing, the Fifth Circuit rediscovers the snapshot rule by giving finality to exemptions in chapter 7.

Reversing Itself, Fifth Circuit Panel Reinstates Finality to Exemptions in Chapter 7

In a remarkably short time, a panel of the Fifth Circuit saw the error in its ways, vacated an opinion handed down on July 19, 2017, and held that exempt property on the filing date does not lose its exempt status even if it is converted to nonexempt property after the filing of a chapter 7 petition.

The *per curiam* opinion on Sept. 5 removes a cloud of perpetual uncertainty that had been hanging over chapter 7 debtors in the Fifth Circuit. For seven weeks, when the July opinion was good law, a chapter 7 debtor who liquidated exempt property was in peril even if the case had been closed and the time for objecting to exemptions had long since passed.

The new opinion establishes two principles in the Fifth Circuit. As we will discuss later, the holding in *In re Frost*, 744 F.3d 384 (5th Cir. 2014), is now limited to chapter 13 cases, and *In re Zibman*, 268 F.3d 298 (5th Cir. 2001), does not apply to cases where the time for objecting to exemptions has elapsed.

The Facts

The case involved a couple who filed a chapter 7 petition with about $130,000 in an individual retirement account, or IRA. They scheduled the IRA as exempt under Texas law. There were no objections to the claimed exemption, and the trustee eventually issued a no-asset report.

Starting a few days before filing and continuing for seven months, the couple withdrew all the money from the IRA, spent most of it on living expenses, and did not reinvest any proceeds in another IRA.

Learning that the IRA had been liquidated and not reinvested, the trustee demanded that the couple turn over the IRA proceeds, because Texas law provides that withdrawals from an IRA must be reinvested in another IRA within 60 days to retain their exempt character. When the trustee made her demand, the debtors still held about $30,000 in proceeds from the IRA.

The bankruptcy judge ruled in favor of the trustee and required the couple to turn over the $130,000. The district court affirmed.

The Original Panel Opinion

The original panel opinion from July was based largely on *Frost*, where a couple owned a home when they filed a chapter 13 petition. Later, they sold the home but did not reinvest the proceeds in another exempt homestead. Without saying in the opinion whether the case was in chapter 7 or 13, the Fifth Circuit held in *Frost* that the proceeds lost their exempt status, relying in part on *Zibman*, discussed below.

Lower courts were divided on whether *Frost* also applied to chapter 7 cases. Some courts believed that *Frost* should apply only in chapter 13 cases because Section 1306(a)(1) brings after-acquired property into the estate. Since there is no counterpart in chapter 7, those courts would not invoke *Frost* in chapter 7 cases.

The original panel opinion in July, written by Circuit Judge Edward C. Prado, resolved the issue by holding that *Frost* applied equally in chapter 7. The appeals courts developed the notion of conditionally and unconditionally exempt property.

Unconditionally exempt property, like an IRA or a homestead, could become conditionally exempt on being sold or liquidated. If proceeds were not reinvested in exempt property within the time permitted by state law, the conditionally exempt money would lose its exempt character.

Arguably splitting with every other circuit and seemingly abandoning the snapshot rule, the original panel opinion in effect held that exemptions never become final even if the time for objection has run out.

The original opinion was important because it meant that debtors in Texas and perhaps elsewhere could not take money from an IRA until after the chapter 7 case was closed. It also meant that a chapter 7 debtor in Texas could not sell an exempt homestead after filing because it would lose the exemption if the proceeds were not reinvested in a new homestead within six months.

Even after the chapter 7 case had been closed, a trustee could reopen the case and demand turnover. Following the July decision, it was unclear how long debtors were required to hold exempt property even after a chapter 7 case was closed.

The Motion for Rehearing

On August 2, the husband moved for panel rehearing and rehearing *en banc*, supported by an *amicus* brief filed by Prof. Christopher G. Bradley of the Univ. of Kentucky College of Law, retired Bankruptcy Judge Leif M. Clark, and attorneys Stephen W. Sather and Michael Baumer, both of Austin.

The last brief on the rehearing petitions was filed on Aug. 21. Without holding oral argument, the panel issued its 14-page *per curiam* opinion on Sept. 5, withdrawing the prior opinion, reversing the bankruptcy court, remanding the case, and denying the petition for rehearing *en banc*. In effect, the panel reversed its prior opinion and allowed the debtors to retain all proceeds from the liquidated IRA.

The Rationale after Rehearing

Originally mandated by the Supreme Court in *White v. Stump*, 266 U.S. 310 (1924), and largely ignored in the prior opinion, the new opinion reaffirmed the snapshot rule, which in substance provides that exemptions are fixed on the filing date. The appeals court then examined *Frost* and *Zibman*, ultimately limiting the holdings of both.

Zibman, which predated *Frost*, concerned debtors who sold their exempt homestead two months before filing a chapter 7 petition but did not reinvest the proceeds in another home. The appeals court held that the proceeds lost their exempt status because the Texas statute protects only a homestead, not proceeds of a homestead.

The new opinion then did what *Frost* did not do: It limited the holding to chapter 13 because after-acquired property is not brought into a chapter 7 estate. The new opinion characterized the IRA proceeds as a newly acquired property interest.

Since the time for objecting to exemptions had expired, the new opinion said "there was no means by which the [debtors'] newly acquired property interest [in the IRA proceeds] could become part of the chapter 7 estate."

The new opinion emphasized how *Zibman* dealt with debtors who had sold their home before filing, giving them only a conditional exemption on the filing date. The new opinion thus limits *Zibman* to situations where an exempt asset is sold before bankruptcy but not reinvested in another exempt asset within the time allowed by state law.

Finality of Exemptions Emphasized

The new opinion helps debtors generally because the appeals court emphasized the finality resulting from the lack of objections to exemptions.

The debtors had liquidated some of the IRA before filing, thus giving the trustee an opening to demand turnover of those moneys, based on *Zibman*. Nonetheless, the new opinion allowed the debtors to retain even those proceeds. Because the trustee "did not timely object to the claimed exemption," she "could not contest the exemption's validity after the time for objection passed," the opinion says.

Consequently, the new opinion also limits *Zibman* to cases where the time for objection to exemptions has not elapsed.

The new opinion emphasizes the differences between chapters 7 and 13. The *per curiam* opinion says the two chapters "are not meant to always yield the same results."

With regard to after-acquired property, the opinion holds that "a new property interest the debtor acquires after filing for bankruptcy becomes part of the estate in a chapter 13 case but does not become part of the estate in a chapter 7 case, even if the debtor acquires the new property by transforming a previously exempted asset into a nonexempt one."

The debtor was represented by William P. Haddock from Pendergraft & Simon LLP in Houston.

To read ABI's coverage of the July opinion and the motion for rehearing, click here and here.

The opinion is *Hawk v. Engelhart (In re Hawk)*, 871 F.3d 287 (5th Cir. Sept. 5, 2017).

Selling a home after filing chapter 7 does not destroy the homestead exemption.

Fifth Circuit Expands *Hawk* to Permit Sale of a Home After a Chapter 7 Filing

In *Hawk v. Engelhart (In re Hawk)*, 871 F.3d 287 (5th Cir. Sept. 5, 2017), the Fifth Circuit held that property in an exempt individual retirement account on the filing date does not lose its exempt status if it is converted to nonexempt property after the filing of a chapter 7 petition. In other words, the snapshot rule is a shield for the debtor, not a sword in the hands of a trustee.

In a March 7 opinion, the Fifth Circuit expanded *Hawk* to cover homesteads, thus allowing a chapter 7 debtor to sell a home after filing but not lose the exemption even if the proceeds were not reinvested in another house.

The debtor, who waived his discharge, owned a home in Texas on the filing date. There were no objections to the claimed homestead exemption. With the bankruptcy court's approval seven months after filing, the debtor sold his home for $364,000, but he did not reinvest the proceeds in another home within the six-month window in Texas for maintaining an exemption in the proceeds. Instead, the debtor used the proceeds to pay some of his debts.

The chapter 7 trustee mounted an adversary proceeding against the debtor and the recipients of the proceeds, contending that the proceeds belonged to the estate because they lost their exempt status six months after the sale.

The bankruptcy judge ruled that the proceeds were exempt because the home was exempt on the filing date. The district court reversed before the Fifth Circuit decided *Hawk*, and the debtor appealed.

In the Fifth Circuit, the trustee argued that *Hawk* was inapplicable because that case involved a retirement account, not a homestead.

In a *per curiam* opinion on March 7, the Fifth Circuit reversed the district court and reinstated the judgment of the bankruptcy court dismissing the trustee's lawsuit. The Fifth Circuit saw "no reason why *Hawk*'s analysis should not also apply to Texas's homestead exemption." The court said that the "proceeds" rule under the Texas exemption statute "expands rather than limits the scope of the exemption."

In terms of policy, the circuit court said that fixing the exemption once and for all on the filing date avoids "the uncertainty that the trustee's position would inject into the large number of chapter 7 cases that bankruptcy courts confront."

In *Hawk*, the three-judge panel on the Fifth Circuit granted rehearing and set aside the opinion it had filed only seven weeks earlier. To read ABI's discussion, click here.

The opinion is *Lowe v. DeBerry (In re DeBerry)*, 17-50315 (5th Cir. March 7, 2018).

Splitting with the Sixth Circuit, the Tenth Circuit BAP does not require equity to claim a homestead exemption.

Homestead Exemption Must Be Paid in Full Before a Sale Is Permitted, BAP Says

Laying the groundwork for a split of circuits, the Tenth Circuit Bankruptcy Appellate Panel built on *Czyzewski v. Jevic Holding Corp*., 137 S. Ct. 973 (2017), and *Law v. Siegel*, 134 S. Ct. 1188 (2014), by holding that a chapter 7 trustee cannot scheme with secured creditors to sell a home out from underneath a debtor without paying the homestead exemption in full, even when there is little or no equity in the property above secured debt.

If there is another appeal and the Tenth Circuit rules the same way, there will be a split with the Sixth Circuit on the question of whether a debtor can claim a homestead exemption without having any equity in the property. A split would also enable the Supreme Court to decide whether a trustee can sell a home without paying a homestead exemption in full.

Unless the Sixth Circuit reverses course or the Supreme Court takes up the issue, individuals who file chapter 7 petitions in four states are at risk of losing their homes even if the sale price will not pay their exemptions in full. Homeowners in six states are shielded from the same fate unless the Tenth Circuit reverses the BAP.

The Trustee's Scheme to Generate Fees at the Debtor's Expense

In two chapter 7 cases filed about the same time, the debtors each owned homes, which they scheduled as having values somewhat less than the sum of mortgages and tax liens on the properties. The debtors claimed homestead exemptions, however.

The trustee appointed in both cases found buyers who were offering to pay about $5,000 more than the encumbrances on both properties. The trustee also negotiated a stipulation with the Internal Revenue Service where the government consented to the sale of the properties and agreed to carve out $10,000 in each case for distribution to unsecured creditors. In addition, the IRS agreed to a further $60,000 reduction in the government's recovery on its tax liens in each case by allowing the trustee to pay his fees and the real estate broker's commissions from the sale proceeds.

If the sales had been approved, the debtors would have received nothing for their homestead exemptions, while the trustee and broker together would have taken home more than $60,000 for their services in each case. Unsecured creditors would have recovered only $10,000 in each case.

For the debtors, the proposed deal was worse than simply losing their homes without anything for their homestead exemptions. The government's agreement to carve out $10,000 for unsecured creditors and allow payment of the fees would have increased the debtors' nondischargeable tax debts and left them with no equity to apply toward the purchase of new residences.

The future looking bleak, the debtors both prevailed on the bankruptcy judge to convert their cases to chapter 13. Conversion mooted the trustee's incipient sale motions. In both cases, the bankruptcy judge upheld the debtors' homestead exemptions, over the trustee's objections. The conversion to chapter 13 mooted the trustee's appeals from the homestead exemption rulings.

Following conversion, the chapter 7 trustee filed applications for allowances of more than $30,000 in compensation in each case for himself and his counsel. In an encyclopedic opinion on Dec. 14, 2016, Chief Bankruptcy Judge R. Kimball Mosier of Salt Lake City ruled that a trustee cannot sell an individual debtor's home without paying the homestead exemption in full, in cash.

Citing Section 330(a)(4)(A), Judge Mosier denied the fee applications because the trustee's services were not necessary, did not benefit the estate, and "could work a substantial harm on the debtors if they were approved." In substance, he explained why he would not have approved the sales had the debtors not converted the cases to chapter 13. To read ABI's discussion of Judge Mosier's opinion, click here.

The trustee appealed to the Tenth Circuit BAP but lost again in a Nov. 30 opinion by Bankruptcy Judge Sarah A. Hall. The BAP reached the same result in barring a trustee from selling overencumbered property, albeit on somewhat narrower grounds than Judge Mosier.

Abandon, Don't Sell Without Equity

To determine whether the trustee was entitled to compensation, Judge Hall analyzed Section 330(a)(4)(A), which bars the allowance of compensation if the services "were not reasonably likely to benefit the debtor's estate [or] necessary to the administration of the case."

Regarding the necessity of the trustee's services, Judge Hall held that "abandonment of the homesteads would have better comported with a chapter 7 trustee's ultimate duties and responsibilities." The Bankruptcy Code, abundant caselaw, and the *Handbook for Chapter 7 Trustees* promulgated by the Office of the U.S. Trustee Program "emphatically" supported the bankruptcy court's decision, Judge Hall said.

Judge Hall cited the *Handbook* for the proposition that a trustee should abandon property when liquidation would not produce a "meaningful" distribution for unsecured creditors. Similarly, she cited caselaw holding that a sale of fully encumbered property is generally prohibited, to prevent trustees from generating fees for themselves in a sale that produces nothing for unsecured creditors.

With regard to the Bankruptcy Code, Judge Hall said that equity for unsecured creditors "is what authorizes a trustee to exercise his powers of sale under Section 363 in the first place, because liquidation should not be for the benefit of the estate's secured creditors." Although a carve-out for unsecured creditors might be appropriate in some circumstances, she said that an agreement with a secured creditor to create equity "is suspect and presents opportunities for collusion."

Since the proposed sale would have benefitted primarily the trustee and secured creditors, Judge Hall concluded that the services were not necessary in the administration of the estates.

Again unsuccessfully, the trustee contended that his services were nonetheless reasonably likely to benefit the estate.

On that issue, Judge Hall said that the bankruptcy court's finding of lack of benefit to the estate was not reversible error, "regardless of whether its legal determinations were correct or incorrect."

The trustee argued that his services benefited the estate, based on the notion that the debtors lacked equity and were not entitled to homestead exemptions.

Under Utah and federal law, exemptions must be liberally construed in favor of debtors, Judge Hall said. Under Utah law, she said that debtors are entitled to homestead exemptions even if they have no equity in their homes. The exemption, she said, arises from title and possession, although the exemption is limited in dollar amount.

Therefore, the trustee was not entitled to compensation under Section 330(a)(4)(ii) because there was no benefit to the estate, since the trustee should have abandoned the properties.

The trustee also argued there could have been benefit to the estate because he could have sold the properties under Section 363(f).

There was no *bona fide* dispute, and therefore no ability to sell under Section 363(f)(4), because, Judge Hall said, the bankruptcy court had upheld the debtors' homestead exemptions, among other things.

Similarly, there was no right to sell under Section 363(f)(5), which would have applied were the debtors compelled to accept monetary satisfaction for their interests.

The Utah exemption statute does not permit a sale unless the price would pay the exemption in full. The trustee therefore could not have sold under Section 363(f)(5), thus shutting the door to the idea that the trustee could have conferred benefit on the estate.

Judge Hall upheld the denial of all the trustee's requested fees by saying it made "no sense whatsoever to sell the homesteads and incur administrative expenses [of about $60,000 in each

case] in order to get only $10,000 to unsecured creditors and at the same time deny debtors their homesteads."

"All bankruptcy professionals," she said, "must exercise billing judgment."

Significant Circuit Splits in the Offing

If the trustee appeals again and if the Tenth Circuit affirms, there will be a split of circuits on two major issues.

In *Brown v. Ellmann (In re Brown)*, 851 F.3d 619 (6th Cir. March 20, 2017), the Sixth Circuit decided a strikingly similar case with a diametrically opposite result. In *Brown*, the debtor had owned an overencumbered home, but she did not initially claim a homestead exemption. Instead, she originally signaled her intention to surrender the house.

The trustee in *Brown* cobbled together a deal to sell the home for less than the first mortgage. The first mortgagee agreed to take a haircut on the senior mortgage, carve out $6,000 for the second mortgagee, and leave a small surplus for unsecured creditors. The debtor later claimed an exemption and opposed the sale, unsuccessfully.

The Sixth Circuit upheld the sale, holding that the debtor was not entitled to claim a homestead exemption under Michigan without equity in the property. Aside from the distinction that the two cases arose under the exemption laws of different states, the Tenth Circuit BAP split with the Sixth Circuit on the validity of a homestead exemption in the absence of equity in the property.

More fundamentally, the Sixth Circuit allowed selling a home out from underneath a debtor without paying the homestead exemption in full, whereas the Tenth Circuit BAP would not allow a sale under analogous circumstances.

Brown also widened a split in its own right by holding that a sale order is not automatically mooted by Section 363(m) if the appellate court can grant some relief without affecting the validity of the sale.

The Tenth Circuit BAP cited to *Brown* in passing, but without addressing in depth how the two cases reached fundamentally different results.

To read ABI's discussion of *Brown*, click here.

Jevic and *Siegel* Influence the BAP

The BAP buttressed its conclusions by referencing two recent Supreme Court decisions.

In a passing reference, the BAP said that "*Jevic* stands for the proposition that neither the parties, nor the courts, are free to circumvent the Bankruptcy Code's rules and policies regarding priorities and distributions through manipulation of substantive and procedural protections." The reference to *Jevic* in a footnote shows that the high court's decision on limiting structured dismissal informs the result in other contexts, such as exemptions.

The BAP also cited *Law v. Siegel* for the idea that homestead exemptions are "sacrosanct" and can be denied "only on statutory bases enumerated in the Bankruptcy Code."

Although the BAP case was not "strictly analogous" to *Law v. Siegel*, Judge Hall said the effect was the same: "to deprive debtors of their homestead exemptions on a basis other than one enumerated in the Code."

Moreover, she said, the debtors had not been accused of any fraudulent behavior, like the debtor in *Law v. Siegel*. The "scheme" to sell the homes by negotiating with the IRS was "nothing more than an attempt to do indirectly what the Bankruptcy Code and Utah exemption statutes prevent him from doing directly."

On behalf of the National Consumer Bankruptcy Rights Center and the National Association of Consumer Bankruptcy Attorneys, Tara A. Twomey submitted an *amicus* brief on behalf of the debtors.

The opinion is *Jubber v. Bird (In re Bird)*, 577 B.R. 365 (B.A.P. 10th Cir. Nov. 30, 2017).

Debtors have standing for a motion compelling a trustee to abandon.

Trustee Can't Evict Debtors in Advance of Selling Their Home, Sixth Circuit Rules

The Sixth Circuit established an important precedent protecting individual debtors by declaring they can't be evicted from their home simply because the trustee tenders a check representing the full value of the homestead exemption.

The circuit's decision on July 14 made law on seemingly obvious questions about the debtors' standing and the right to occupy a home before sale. Like here, there will sometimes be no direct precedent because no one previously will have had the temerity to raise questions with obvious answers.

A couple filed a chapter 7 petition, listing their home as worth $108,000, encumbered by a $91,500 mortgage. Alleging that the property was really worth about $200,000, the trustee filed a motion asking the bankruptcy judge to evict the couple, saying that he could not sell the property while they were living there.

The debtors cross moved for an order compelling the trustee to abandon the home on the theory that the home had inconsequential value for creditors. At the hearing on the dueling motions, the trustee tendered the debtors a check for $7,500, representing the full amount of their Tennessee homestead exemption.

Bankruptcy Judge Nicholas W. Whittenburg of Chattanooga, Tenn., held an evidentiary hearing and took appraisal testimony from both sides. He vouched for the debtors' appraisal, concluding that the property was worth only $108,000. He also said that the trustee had six months to find a buyer and that properties are often sold with tenants in residence. Judge Whittenburg therefore granted the debtors' motion to compel abandonment and denied the motion to evict.

The trustee appealed and lost again in district court. The trustee lost a third time in the Sixth Circuit, in an opinion authored by Circuit Judge Ronald Lee Gilman.

The trustee contended that the debtors lacked standing to compel abandonment. Using a result-oriented approach, Judge Gilman said that being allowed to keep their home gave them a "practical stake" in the outcome, thus conferring standing. He also said that their homestead exemption was not the debtors' only remedy in the face of a motion to evict, thus countering the trustee's argument that tendering the $7,500 check was the only relief to which they were entitled. The debtors' alternate remedy, he said, was to seek abandonment.

Judge Gilman said that the debtors also had Article III standing because evicting them “would surely constitute injury-in-fact.”

Turning to the merits, Judge Gilman found “no authority for the proposition that the trustee can tender the debtors the homestead exemption and cause them to ‘skedaddle.’” There was, he said, “no basis in precedent or in the Bankruptcy Code.”

On the question of value to support the conclusion of inconsequential value, Judge Gilman invoked the “clear error” standard and said the record was “replete with evidence” supporting the debtors’ valuation.

W. Thomas Bible, Jr. represented the debtors, while Tara A. Twomey of the National Consumer Bankruptcy Rights Center filed an *amicus* brief on behalf of the debtors.

The opinion is *Jahn v. Burke (In re Burke)*, 863 F.3d 521 (6th Cir. July 14, 2017); rehearing *en banc* denied Aug. 17, 2017.

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Automatic Stay

Ninth Circuit splits with the First on the interpretation of Section 106(a).

Circuits Split on Sovereign Immunity and Emotional Distress Damages for a Stay Violation

The waiver of sovereign immunity in Section 106(a) allows an individual to collect damages for emotional distress resulting from the government's willful violation of the automatic stay, according to the Ninth Circuit.

The Ninth Circuit created a split of circuits because the First Circuit had held in *U.S. v. Rivera (In re Rivera)*, 432 F.3d 20 (1st Cir. 2005), that Section 106(a) does not waive sovereign immunity for emotional distress damages resulting from a stay violation.

Daniel Geyser of Dallas, who prevailed in the Ninth Circuit on behalf of the debtors, told ABI that "Congress waived sovereign immunity to put the government on equal footing with private parties." The damage award, he said, "holds the government accountable for its actions — just as Congress intended."

The Debtor Wins and Loses Below

After a couple filed their chapter 13 petition, the Internal Revenue Service sent several notices demanding payment of back taxes and threatening to levy on their bank accounts. The bankruptcy judge held the IRS in contempt of the automatic stay and imposed $4,000 in damages for "significant emotional harm."

On appeal, the IRS conceded there was a stay violation but contended that the doctrine of sovereign immunity insulates the government from claims for emotional distress under Section 362(k). A district judge in Oregon agreed, reversed the bankruptcy court, and ordered the complaint dismissed. To read ABI's discussion of the district court opinion, click here.

The debtor appealed and won a reversal in an August 30 opinion written for the Ninth Circuit by District Judge Cynthia A. Bashant, sitting by designation from the Southern District of California.

The Relevant Bankruptcy Code Provisions

Section 106(a)(1) waives sovereign immunity "as to a governmental unit" with regard to 59 provisions in the Bankruptcy Code, including Section 362. Section 106(a)(3) enables the court to

"issue" an "order . . . or judgment" against a governmental unit, "including an order or judgment awarding a money recovery, but not including an award of punitive damages."

Section 362(k) provides that "an individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages."

Removing what otherwise would have been an issue on appeal, the Ninth Circuit had held in 2004 that "actual damages" in Section 362(k) includes damages for emotional distress. *See Dawson v. Washington Mutual Bank, F.A. (In re Dawson)*, 390 F.3d 1139, 1148 (9th Cir. 2004).

The Government's Argument

Urging the appeals court to uphold the district court, the government relied on *U.S. v. Nordic Village Inc.*, 503 U.S. 30 (1992), where the Supreme Court ruled that Section 106, as it was then written, did not unequivocally subject the government to claims for monetary relief. At the time, Section 106 only said that the term "creditor" when used in the Bankruptcy Code applies to "governmental units" and that "an issue arising under such a provision binds governmental units."

Congress responded to *Nordic Village* two years later by amending Section 106 to contain an explicit waiver of sovereign immunity. The government argued in the Ninth Circuit that the amendment only permits recovery of money unlawfully in the government's possession.

The Circuit's *Ratio Decidendi*

To analyze whether the waiver of sovereign immunity extends to damages for emotional distress, Judge Bashant began with the Supreme Court's rule that a waiver of sovereign immunity must be "unequivocally expressed." *U.S. v. Bormes*, 568 U.S. 6, 9–10 (2012) (quoting *Nordic Village*, 503 U.S. at 33–34).

Judge Bashant said that the government's argument based on *Nordic Village* "is not plausible in light of the [amended] statute's text." She said that Section 106(a) "plainly waives sovereign immunity for court-ordered monetary damages under the waiver's enumerated provisions, although the damages may not be punitive."

Emotional distress damages, Judge Bashant said, "are a form of monetary relief — compensatory damages — but they are not punitive." Given *Dawson*'s holding that emotion distress damages are permitted under Section 362(k), she held that "Section 106(a) waives sovereign immunity for emotional distress damages under Section 362(k)."

The Split with the First Circuit

Judge Bashant ended her opinion by explaining why the Ninth Circuit would not follow the First Circuit's decision in *Rivera*.

Based on the so-called temporal approach, the First Circuit pronounced a convoluted theory to immunize the government for emotional distress damages sought under Section 105 for a willful stay violation.

The First Circuit understood the 1994 amendments in Section 106 to waive sovereign immunity only as to forms of monetary relief that were understood to exist at the time. Since damages for a willful stay violation in 1994 had not been understood to include emotional distress damages, the First Circuit did not find a clear intent to waive sovereign immunity.

Judge Bashant declined to follow the First Circuit because she said the "plain language of the statute is dispositive."

The First Circuit also latched onto Section 106(a)(5), which provides that nothing in the section creates "any substantive claim for relief . . . not otherwise existing under this title, the Federal Rules of Bankruptcy Procedure, or nonbankruptcy law."

Judge Basant rejected the reliance on Section 106(a)(5), saying it did not "graft a temporal restriction onto the waiver's scope."

Judge Basant reversed the district court and remanded for the district court to consider the government's appeal on the merits.

Is the Issue '*Cert*-worthy'?

Since here is now a split of circuits, the government could file a petition for *certiorari* seeking review in the Supreme Court. The government may not bother because the issue seldom arises given that the IRS does not have a policy calling for violation of the automatic stay.

In view of the remand for the district court to analyze the merits, the judgment in the court of appeals is not a final order and thus may not warrant the granting of *certiorari*. However, the high court will sometimes review a non-final order that raises a pure issue of law not likely to be affected by remand.

All things considered, the Ninth Circuit's decision is not a compelling candidate for a grant of *certiorari*. In terms of a circuit split involving the automatic stay, the Supreme Court will have a far more consequential case in *Lorenzen v. Taggart (In re Taggart)*, 888 F.3d 438 (9th Cir. April 23, 2018) (petition for panel rehearing and rehearing *en banc* filed June 6, 2018). *Taggart* merits Supreme Court review because the First Circuit handed down contrary decision seven weeks later in *IRS v. Murphy*, 892 F.3d 29 (1st Cir. June 7, 2018).

Murphy and *Taggart* raise the question of whether good faith is a defense to sanctions for violating the discharge injunction. The Ninth Circuit held that good faith is a defense, while the First Circuit held it is not. The Ninth Circuit must deal with the petition for rehearing before there can be a *certiorari* petition. To read ABI's discussion of those cases, click here and here.

The opinion is *Hunsaker v. U.S.*, 16-35991 (9th Cir. Aug. 30, 2018).

Second Circuit approves a stay-violation defense in a nonprecedential opinion.

Simply Initiating Events that Later Violate the Stay Is Not a Stay Violation

Someone accused of indirectly violating the automatic stay has two lines of defense, thanks to a Jan. 25 opinion from the Second Circuit.

A creditor had a judgment against the soon-to-be debtor. When the 10-year lien of the judgment was about to expire, the creditor applied to state court before the debtor's bankruptcy for an order extending the lien. Although the court granted the extension, the order extending the lien was not docketed.

The judgment creditor did not know that the county clerk had never filed the extension order until the trustee sued to void the lien under the strong-arm powers.

According to the unsigned, nonprecedential summary opinion, the Second Circuit said that the creditor's counsel then contacted the county clerk "to inquire why the [creditor's] timely filed but inexplicably undocketed extension order did not appear" on the docket. In response to the inquiry, the state court clerk then entered the lien-extension order after the filing of the bankruptcy petition.

The bankruptcy court found the creditor in contempt for violating the automatic stay under Section 362(a)(4) as "any act to create, perfect, or enforce any lien against property of the estate."

The district court reversed in August 2016, setting aside the contempt finding and holding that the entry of the lien after filing was not "reasonably foreseeable." The district court said that the creditor "must intend or at least reasonably anticipate bringing about the consequences of his act." The district judge said that the "act must have as its purpose the creation of the lien, not just that the act gave rise to the lien as a collateral result of the act."

The Second Circuit upheld the district court's reversal of the contempt finding, saying, however, that the case did not turn on "reasonable foreseeability."

The appeals court said the creditor's counsel "merely asked the [state court clerk] what happened to his timely filed extension order." There was "no indication," the opinion says, that the creditor asked the clerk to correct the mistake, nor was there any evidence suggesting that the creditor "engaged in anything other than a simple factfinding inquiry."

The Second Circuit said that the automatic stay "does not prohibit all acts which coincidentally set in motion the creation" of a lien. Rather, there must be an act "to create, to perfect, or to enforce a lien."

"Because [the creditor] engaged only in factfinding and did not attempt to create, perfect, or enforce its lien, [the creditor] did not violate the stay."

To read ABI's discussion of the district court opinion, click here.

The opinion is *Pereira v. 397 Realty LLC (In re Heavey)*, 16-3227 (2d Cir. Jan. 25, 2018).

California judge won't bar the debtor from settling for more than the original $6 million in compensatory damages while forsaking $40 million in punitive damages earmarked for public interest groups.

Judge Refuses to Vacate Opinion Socking a Bank with $40 Million in **'Punies'**

In March, Bankruptcy Judge Christopher M. Klein of Sacramento, Calif., imposed more than $46 million in compensatory and punitive damages on a bank for foreclosing and evicting a couple from their home although the lender knew they had filed a chapter 13 petition expressly to halt foreclosure. The judgment included $40 million in punitive damages for what Judge Klein called a "Kafkaesque nightmare of stay-violating foreclosure." *Sundquist v. Bank of America NA*, 566 B.R. 563, 571 (Bankr. E.D. Cal. March 23, 2017).

Months later, the parties reached a confidential settlement requiring the judge to expunge his opinion from the public record. Judge Klein said the proposed settlement created a "hostage standoff" that he characterized as "a naked effort to coerce this court to erase the record."

In an opinion on Jan. 18, Judge Klein's response to vacating his opinion was "No chance. No dice."

The Genesis of the Settlement

The parties responded to the $46 million judgment with cross motions for rehearing. The bank claimed there was evidence justifying total exculpation. The debtors countered with arguments that they should be entitled to more than $9 million in compensatory damages.

Mediation ensued and resulted in a proposed settlement giving the debtors an undisclosed amount totaling considerably more than Judge Klein's $6 million judgment.

In his March opinion, Judge Klein had earmarked the $40 million in punitive damages for five California law schools and two nonprofit groups to "be used only for education in consumer law and delivery of legal services in matters of consumer law." The settlement called for the law schools and nonprofit groups to receive about $300,000.

There was a catch: The settlement would require Judge Klein to vacate his March opinion, which excoriated the bank for its contemptuous behavior. Although the parties could have settled between themselves without court approval, they needed the judge's blessing to vacate his opinion.

The intended recipients of the punitive damages opposed vacating the opinion but took no position on the settlement otherwise. Judge Klein took the settlement under submission in October, with the question of vacating his March decision being a primary sticking point.

Judge Klein handed down his decision on Jan. 18. He crafted an elegant solution designed to ameliorate the lender's legitimate concerns while leaving his opinion on the public record, available for citation by other judges in other cases.

The Hostage Standoff

As a result of his opinion in March, Judge Klein said "the situation is now bigger than the" debtors. The "public-interest component cannot be ignored" because "some things are not appropriate to sweep under the carpet."

Under *American Games Inc. v. Trade Products. Inc.*, 142 F.3d 1164 (9th Cir. 1998), Judge Klein said he had equitable discretion to vacate his opinion, or not. Once decisions have been entered after trial, he said that attempts to "'buy and bury' adverse judgments are viewed with caution."

In deciding how to exercise discretion, Judge Klein said the record did not suggest "that the facts constitute an anomalous or isolated incident that might unfairly besmirch an otherwise upstanding defendant." He said the lender had shown no remorse, made no apology, made no promise to reform, and had not accepted responsibility for its actions.

"To name and to shame [the lender] on the public record in an opinion that stays on the books serves a valuable purpose casting sunlight on practices that affect ordinary consumers," Judge Klein said. Under the circumstances, the proper method for erasing the opinion is to reverse it on appeal, he said.

The Solution

Releases in the agreement would alleviate any concern on the part of the bank that the debtors might mount another lawsuit after collecting the settlement. On the other hand, Judge Klein said the bank had legitimate concerns, although remote, that the doctrine of issue preclusion (sometimes called offensive collateral estoppel) might enable a third party to sue the lender and contend that some of the issues were decided in the $46 million judgment.

To contour a solution giving the bank the protection it legitimately needed, Judge Klein undertook an extensive analysis of the Restatement (Second) of Judgments. In that respect alone, his opinion is worth reading in full text.

To give the parties most of what they wanted, Judge Klein said he would vacate the portion of his judgment awarding damages to the debtors while closing the adversary proceeding "without dismissing the adversary proceeding and without erasing the opinion." Vacating the damage award would remove finality and preclude a third party from raising a claim of issue preclusion.

To add belt and suspenders, Judge Klein said his order on the motion to vacate the judgment would provide that the legal and factual issues were not "sufficiently firm to be accorded preclusive effect."

Judge Klein granted the parties' wish by keeping the terms of settlement secret. He did say that the debtors would receive a "substantial premium" over the original award of about $6 million.

The "public interest" component of the original punitive damage award would be "indirectly honored in the settlement" because the debtors obliged themselves to give about $300,000 to the consumer advocacy programs.

The opinion is *Sundquist v. Bank of America NA (In re Sundquist),* 14-2278, 2018 BL 17263 (Bankr. E.D. Cal. Jan. 18, 2018).

Circuits split on power of bankruptcy courts to impose punitive or criminal contempt sanctions.

Bankruptcy Courts Cannot Impose Punitive Contempt Sanctions, District Judge Says

Confronting an issue where the circuit courts are divided and the Second Circuit has been silent, Vermont's Chief District Judge Geoffrey W. Crawford decided that bankruptcy courts lack "statutory and inherent powers" to impose punitive contempt sanctions.

The Sanctions in Bankruptcy Court

In three chapter 13 cases, the bankruptcy court had imposed a total of $375,000 in sanctions on a mortgage servicer for billing debtors for fees without first filing the required notices under Bankruptcy Rule 3002.1(c). Previously, the servicer had been "chastised" by a bankruptcy judge in North Carolina for violating the rule. In one of the three cases, the servicer had already agreed to pay a $9,000 sanction for sending erroneous mortgage statements for three years, but it did not halt the practice.

The bankruptcy judge said that the $9,000 sanction two years earlier had failed to achieve its intended remedial effect of deterring the servicer from sending out "inaccurate account statements." Since she had given the servicer "an opportunity to bring its practices in line with the mandates of Rule 3002.1," the bankruptcy judge felt that "the time has come for 'the imposition of severe sanctions.'"

To read ABI's report on the bankruptcy court opinion, click here.

The servicer appealed and won in Judge Crawford's Dec. 18 opinion.

The Bankruptcy Court's Limited Powers

To arrive at an award of $75,000, the bankruptcy judge had relied on Bankruptcy Rule 3002.1(i)(2), which authorizes the court to "award other appropriate relief." For the remaining $300,000, the bankruptcy court used Section 105(a) and the court's inherent powers.

Addressing whether the bankruptcy court indeed possessed power, Judge Crawford said that the circuits "have been deeply divided for many years on the question of whether bankruptcy courts have power to punish criminal contempts or impose punitive sanctions." The Second Circuit, he said, has not addressed the question.

Judge Crawford then summarized the evolution of the bankruptcy court's contempt powers under the Bankruptcy Rules, as influenced by the Supreme Court's 1982 decision in *Northern Pipeline*. The current iteration of the rules governing contempt — Bankruptcy Rules 9020 and 9014 — impose procedural rules but "provide no source of substantive authority," the judge said.

On the question of power, Judge Crawford said "that the prevailing trend in the development of bankruptcy law over recent years has been to place ever-tightening limits on bankruptcy courts' contempt authority." He said that "the better-reasoned authorities favor the narrower construction of the bankruptcy court's statutory and inherent punitive sanction power."

Judge Crawford was persuaded by the Ninth Circuit, which "held that neither Section 105 nor the bankruptcy court's inherent authority were proper sources of authority for the imposition of a serious punitive sanction." *In re Dyer*, 322 F.3d 1178 (9th Cir. 2003). He also found favor with the Fifth Circuit's holding that bankruptcy courts lack constitutional power to exercise criminal contempt power. *In re Hipp Inc.*, 895 F.2d 1503 (5th Cir. 1990).

Judge Crawford found fault with the logic of the First and Eighth Circuits, which were more liberal in vesting punitive power in bankruptcy courts.

Although the bankruptcy court may lack power in itself to address serious misconduct, Judge Crawford ended his opinion by mentioning that the district court has power to impose criminal contempt sanctions.

On remand, Judge Crawford said the bankruptcy court may "refer the matter to the district court" if it determines "that exercise of that authority would be appropriate." Alternatively, he said, the bankruptcy court "may take steps to enforce its orders short of punitive sanctions of the scope and type imposed in these cases."

The opinion is *PHH Mortgage Corp. v. Sensenich*, 16-256, 2017 BL 452882 (D. Vt. Dec. 18, 2017).

Lender cannot hide behind a disclaimer to avoid sanctions for violating the discharge injunction, Ninth Circuit BAP holds.

BAP Upholds $119,000 in Contempt Sanctions; Tells Lender to Modify Its Forms

The Ninth Circuit Bankruptcy Panel used an opinion upholding $119,000 in compensatory damages to declare that a lender must change its standard forms for borrowers who have received a discharge, and that it cannot use a boilerplate disclaimer to disguise a willful violation of the discharge injunction.

The BAP also interpreted Ninth Circuit opinions to mean that a bankruptcy court can award punitive damages so long as they are "relatively mild."

The debtors owned a home that they scheduled for surrender to the lender. They moved out, the debtors received their discharges, and the lender later obtained an order modifying the automatic stay.

After the debtors received their discharges, the mortgage lender began calling and writing for the next two years, until the lender finally began foreclosure proceedings.

After two years of dunning letters and calls, the debtors reopened their case and filed a motion to hold the lender in contempt of the discharge injunction, employing Ninth Circuit law, which holds that someone who commits a knowing violation of the discharge injunction under Section 524(a)(2) can be held in contempt under Section 105(a).

At a hearing with witnesses, the lender conceded it was aware of the discharge. The remaining issues at trial were the lender's intent and damages.

Among other defenses, the lender contended it had no liability because some of the correspondence was required by state and federal regulations. Other correspondence included a disclaimer, which said that the lender was making no effort to collect if the debtor was in bankruptcy or had received a discharge.

One of the debtors testified that the lender called two or three times a day for a year after discharge and that she answered the call about 20 times. Based on documents and testimony, the bankruptcy judge found that the lender made 100 calls and sent 19 letters. The judge granted $119,000 in compensatory damages ($1,000 for each call and letter) for emotional distress based on the debtors' testimony, among other things, that the lender's attempts to collect caused physical ailments and almost broke up their marriage.

The bankruptcy court did not impose punitive damages. The judge said he "probably" would have imposed punitive damages but did not believe he had the authority under Ninth Circuit law.

The lender appealed to the BAP, and the debtors cross appealed the denial of punitive damages.

In a Dec. 22 opinion for the BAP, Bankruptcy Judge Robert J. Faris upheld the $119,000 damage award but reversed and remanded, with instructions allowing the bankruptcy judge to enter final judgment for "relatively mild noncompensatory fines," issue proposed findings for the district court on punitive damages, or refer the contempt issue to the district court.

Judge Faris held that the calls and letters were knowing and willful violations of the discharge injunction, despite the lenders' defenses. He recognized a tension between discharge and the lender's obligation to give the debtors notices of foreclosure.

To resolve the tension, Judge Faris said that the lender may communicate but "only to the extent necessary to preserve or enforce its lien rights, and may not attempt to induce the debtor to pay the debt." In that regard, he upheld the bankruptcy court's findings that the communications "went far beyond what was necessary" to protect lien rights and were "meant to induce" the debtors to make payments after discharge.

Even if some of the notices did not violate the discharge injunction, Judge Faris agreed that the bankruptcy court "correctly noted that the cumulative effect of all of the letters demanding money created the perception that [the debtors] needed to pay" the lender.

With regard to the disclaimer, Judge Faris saw no reason for the lender to obscure the fact, which it knew, that the debtors had received a discharge. He said the lender gave no reason why it sent "generic" notices when it knew the debtors were discharged. He said the lender "could and should prepare notices that are consistent with the known legal status of borrowers."

The failure to use proper notices, he said, reflected either incompetence, which he doubted, or "a deliberate effort to induce confused borrowers to pay discharged debts."

On the debtors' cross appeal, Judge Faris said that some bankruptcy judges have interpreted *Knupfer v. Lindblade (In re Dyer)*, 322 F.3d 1178 (9th Cir. 2003), to mean that bankruptcy courts may only impose "relatively mild noncompensatory fines."

Other bankruptcy courts have found power to impose punitive damages that are "relatively mild."

However, they are characterized, Judge Faris said the Ninth Circuit allows awards that are "relatively mild."

Without saying how the bankruptcy judge should rule, Judge Faris remanded with instructions to consider imposing a fine or punitive damages that are "relatively mild." Alternatively, the bankruptcy court could make proposed findings and recommend that the district court enter judgment for punitive damages or refer the matter to the district court to consider criminal contempt.

The opinion is *Ocwen Loan Servicing LLC v. Marino (In re Marino)*, 577 B.R. 772 (B.A.P. 9th Cir. Dec. 22, 2017).

Bankruptcy Judge Colleen A. Brown of Burlington, Vt., changes her position on Section 362(c)(3)(A).

A Convert Joins the Minority Interpretation of the Repeat-Filing Stay Termination

Twelve years ago, retired Bankruptcy Judge A. Thomas Small of Raleigh, N.C., said that Section 362(c)(3)(A) "stands out" among the "head-scratching opportunities" found in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, or BAPCPA. *In re Paschal*, 337 B.R. 274, 277 (Bankr. E.D.N.C. 2006).

For someone whose chapter 7, 11 or 13 case was dismissed within a year of a new filing, Section 362(c)(3)(A) calls for the automatic stay to terminate in 30 days "with respect to any action taken with respect to a debt or property securing such debt . . . with respect to the debtor."

At a hearing that must be held within the 30-day period on motion by the debtor or a party in interest, the bankruptcy court may continue the stay "as to any or all creditors" upon a showing that the new case was filed "in good faith as to the creditors to be stayed."

There are at least three interpretations of Section 362(c)(3)(A), which was designed to some greater or lesser degree (depending on your interpretation of the statute) to punish a repeat-filing debtor, and maybe also to punish the debtor's innocent creditors (intentionally or not).

According to a July 20 opinion by Bankruptcy Judge Colleen A. Brown of Burlington, Vt., the majority invoke what they contend is the plain meaning of Section 362(c)(3)(A) to conclude that the stay terminates only as to property of the debtor but not with respect to property of the estate.

In the case before Judge Brown, the third filing came within one year of dismissal of the second. Before the filing of the third petition, a mortgagee had initiated foreclosure. Had Judge Brown followed the majority, the automatic stay precluding foreclosure would persist because the home was property of the estate.

Judge Brown said that the majority's interpretation "would have scant practical effect in deterring repeat filings."

The minority, according to Judge Brown, believe that the stay automatically terminates in its entirety as to the repeat-filing debtor, the debtor's property and the property of the estate, but not as to the debtor's spouse in a joint case if the spouse is not a repeat filer.

Judge Brown cited Bankruptcy Judge Robert E. Grossman of Central Islip, N.Y., who found "an inherent flaw in both the majority and minority reasoning." Focusing on different parts of the statute, Judge Grossman terminated the stay as to the debtor, property of the debtor and property of the estate, but only if the creditor had begun judicial proceedings before bankruptcy. To read ABI's discussion of Judge Grossman's opinion, click here.

Judge Brown had taken sides with the majority in an opinion she had written less than two years after the adoption of BAPCPA. Nonetheless, she was persuaded by commentators and later decisions to change her approach.

To abandon her earlier interpretation of Section 362(c)(2)(A), Judge Brown analyzed the four Supreme Court decisions interpreting BAPCPA. She also considered the concept of *stare decisis*.

Setting aside her earlier ruling, Judge Brown now joins the minority because she believes that terminating the stay as to the debtor, the debtor's property and property of the estate "is consistent with congressional intent . . . because it meaningfully penalizes a debtor who files multiple bankruptcy cases . . . and fails to show a good faith basis for doing so."

Judge Brown also declined to follow Judge Grossman because his decision, in her view, "does not align as clearly with congressional purpose as the minority approach."

The opinion is *In re Goodrich*, 17-10500 (D. Vt. July 20, 2018).

Municipal Debt Adjustment & Puerto Rico

Two circuits and a BAP now invoke 'equitable mootness' to dismiss appeals from orders confirming chapter 9 municipal debt adjustment plans.

Eleventh Circuit Endorses the Applicability of **'Equitable Mootness' in Chapter 9**

Courts considering the issue are now unanimous: The doctrine of equitable mootness applies in chapter 9 just like it does in chapter 11 as the result of an August 16 Eleventh Circuit opinion in the wake of the Jefferson County, Ala., municipal bankruptcy.

The Jefferson County Chapter 9 Plan

Until Detroit sought chapter 9 protection in 2013, Jefferson County's filing in 2011 had been the largest-ever municipal bankruptcy. The county listed long-term debt of $4.23 billion, including about $3.2 billion in defaulted sewer bond debt where the bondholders could look only to the sewer system for payment. The county's chapter 9 plan, confirmed in November 2013, reduced sewer debt to about $1.8 billion from $3.2 billion.

To pay off the old sewer bondholders at a substantial discount, the county issued about $1.8 billion in new sewer bonds. The plan locked in rate increases to be paid by sewer customers every year for 40 years and gave the bankruptcy court continuing jurisdiction to compel the rate increases. The county implemented the plan a few days after confirmation, issuing new bonds in the process.

Ratepayers had objected to confirmation and appealed the confirmation order to the district court, but the county filed a motion to dismiss the appeal, arguing that the appeal should be dismissed on the grounds of equitable mootness.

District Judge Says No Equitable Mootness in Chapter 9

District Judge Sharon Lovelace Blackburn of Birmingham, Ala., wrote a 50-page opinion in September 2014 denying the motion to dismiss the appeal. She held that equitable mootness was not applicable in a chapter 9 municipal bankruptcy, although she said that "some parts of the confirmation order may be impossible to reverse," such as the validity of the newly issued bonds.

Still, reversal meant that she might later void the provisions in the plan locking in annual rate increases that had been included for the benefit of the purchasers of the new sewer bonds.

Judge Blackburn allowed an interlocutory appeal, resulting in the August 16 opinion by Circuit Judge Adalberto Jordan.

Eleventh Circuit Joins Two Other Courts

Judge Jordan said that the Supreme Court has neither endorsed nor rejected the concept of equitable mootness in chapter 11 cases. He said that every circuit to consider the issue has allowed some formulation of equitable mootness.

The Eleventh Circuit, Judge Jordan said, has applied equitable mootness in chapter 11 and "assumed without deciding that it applies in chapter 7 cases." The appeals court had not addressed the question in chapter 9, however.

Judge Jordan said the "correct result was to join the Sixth Circuit," which had upheld the use of equitable mootness in 2016 in the context of Detroit's municipal bankruptcy. Similarly, the Ninth Circuit Bankruptcy Appellate Panel employed equitable mootness in the Stockton, Calif., debt adjustment in 2015.

Seeing "no reason to reject the doctrine here," Judge Jordan said there was "no respect in which [the] principles [of equitable mootness] are bound to come into play any less in the chapter 9 context than in the contexts of chapters 11 or 13."

Indeed, he said, "these principles will sometimes weigh more heavily in the chapter 9 context precisely because many people will be affected by municipal bankruptcies."

Having decided that equitable mootness applied in chapter 9, Judge Jordan proceeded to rule that it required dismissal of the appeal in Jefferson County's case. He said that the ratepayers never sought a stay pending appeal and had not attempted to expedite the appeal, although those facts in themselves were not determinative.

The appeal had to be dismissed, according to Judge Jordan, because "the County and others have taken significant and largely irreversible steps in reliance on the unstayed plan." Even if the appellate court only struck the bankruptcy court's continuing jurisdiction, he said it "would seriously undermine actions taken in reliance on the confirmation order."

To bolster his conclusion, Judge Jordan "briefly" looked at the merits and saw no injustice in allowing the county to bind elected officials decades into the future. He noted how elected officials "can bind their successors . . . to all kinds of unavoidably long-lasting financial effects, sometimes irreversibly."

The opinion is *Jefferson County, Alabama v. Bennett*, 15-11690 (11th Cir. Aug. 16, 2018).

Puerto Rico's toll road bonds don't have statutory liens, circuit court rules.

First Circuit Gives Puerto Rico Bondholders a Second Bite at the Apple

In a pair of opinions on August 8, the First Circuit gave bondholders a second opportunity to prove they are being improperly denied revenue securing the bonds issued by Puerto Rico's instrumentalities. Alluding to two hurricanes that devastated the island commonwealth and its economy, the appeals court did not suggest how the district court should rule on remand but said in both opinions that circumstances have changed dramatically since the lower court ruled last year.

The PREPA Receivership Appeal

After the Supreme Court ruled that Puerto Rico was ineligible for chapter 9 municipal bankruptcy, Congress quickly adopted the Puerto Rico Oversight, Management, and Economic Stability Act, or PROMESA (48 U.S.C. §§ 2161 *et. seq.*), creating the Financial Oversight and Management Board of Puerto Rico. Exercising its exclusive authority several months later, the Oversight Board initiated court-supervised debt restructuring proceedings in the District of Puerto Rico for Puerto Rico and its instrumentalities, including the Puerto Rico Power Authority, known as PREPA.

The Chief Justice selected District Judge Swain of New York to oversee the PROMESA proceedings in Puerto Rico.

Holders of revenue bonds issued by PREPA alleged that the power authority breached a promise to raise rates enough to cover debt service. Under Section 362(d)(1) of the Bankruptcy Code, incorporated into PROMESA by 48 U.S.C. § 2161(a), they sought modification of the automatic stay so they could petition another court to place PREPA in receivership and seek a rate increase.

Judge Swain denied the motion in September 2017 on three grounds. With regard to two of them, she ruled in substance that Sections 305 and 306 of PROMESA, 48 U.S.C. §§ 2165 and 2166, precluded her from ceding authority or jurisdiction to another court. Alternatively, she concluded there was no "cause" to modify the stay because the balance of harm tipped in favor of Puerto Rico.

First Circuit Judge William J. Kayatta, Jr. reversed and remanded on the first two grounds and remanded on the third.

Section 305 of PROMESA is modeled after Bankruptcy Code Section 904, dealing with municipal bankruptcies. Section 305 precludes the court from interfering with the "governmental powers of the debtor."

To read Section 305 so broadly as to prohibit lifting the automatic stay, Judge Kayatta said, "would effectively wipe out" the ability to modify the automatic stay. Although Section 305 prohibits the bankruptcy court from interfering with governmental powers, he said it does not preclude the court from lifting "the stay to allow another court to do what the bankruptcy court cannot do."

Although Judge Kayatta agreed that allowing a "robust receivership" might have a "deleterious impact" on the ability to restructure Puerto Rico's finances, he said it "might be possible to grant tailored relief [so that] the receiver may only take specific steps to protect the creditor's collateral."

Next, he addressed Section 306 of PROMESA, which gives the court exclusive and original jurisdiction. That section, he said, is not unique to PROMESA. "Rather, it is the general rule for bankruptcies."

According to Judge Kayatta, the grant of exclusive jurisdiction "has to our knowledge never limited the bankruptcy court's power to allow others to act on the debtor's property with the permission of the bankruptcy court." He therefore reversed Judge Swain and held that Section 306 does not prevent the court from finding "cause" to lift the stay and permit the bondholder to petition for a receivership.

In what Judge Kayatta called a "brief section," Judge Swain had ruled alternatively that she would not modify the stay even if she had power to do so. He said that Judge Swain did not assess "the extent to which" bondholders "might be irreversibly harmed" or whether PREPA was adequately protecting the bondholders' interests. In sum, Judge Kaytatta wanted Judge Swain to give more detail explaining how she "weighed on each side the balance of the harms."

Since the "situation on the ground . . . has changed greatly" in the last year, "in the wake of Hurricanes Irma and Maria," Judge Kayatta said it was "best to allow the bondholders to file a new and updated request for relief from the automatic stay" so that Judge Swain could "focus on the merits of that request free of any thought that the request is categorically precluded."

The Toll Road Bondholder Appeal

Holders of $65 million in uninsured bonds issued by the Puerto Rico Highways and Transportation Authority mounted an adversary proceeding alleging that the authority was diverting toll revenue that is subject to their statutory lien.

The bondholders asserted a statutory lien evidently to avoid the operation of Section 552(a) of the Bankruptcy Code, which, with exceptions, cuts off security interests from attaching to property acquired after filing.

For the first time in their reply brief in bankruptcy court, the bondholders recognized what may have been a mistake and argued, alternatively, that they held a security interest. Invoking a local rule, Judge Swain barred the new argument and proceeded to rule that the bondholders did not have a statutory lien.

Because the statutory lien was the only basis for asserting lien rights, Judge Swain denied relief from the stay and denied the request for adequate protection. The bondholders appealed.

Writing the opinion for the First Circuit, Judge Kayatta concluded that Judge Swain did not abuse her discretion by disallowing arguments based on a security interest, although he said it was a "close call." He therefore proceeded to analyze whether the bondholders held a statutory lien.

Judge Kayatta described how the Bankruptcy Code creates three mutually exclusive categories of liens: security interests, judicial liens and statutory liens. Quoting Section 101(37) of the Bankruptcy Code, he said that a statutory lien arises "solely by force of a statute." He said that Puerto Rico's enabling statute permits the authority to secure bonds but does not "require that it do so." In the case of the toll road bonds, the pledge was voluntary and thus was not a statutory lien because the lien did not "attach automatically."

Since the statutory lien – which he found not to exist – was the only basis for the appeal, Judge Kayatta upheld the denial of a modification of the stay.

However, Judge Kayatta said the bondholders' waiver of an argument based on a security interest "is not permanent," as Judge Swain herself had observed. He granted the bondholders permission to file "any updated motions for relief," presumably to seek a modification of the stay and adequate protection based on the assertion of a security interest.

Judge Kayatta also dealt with Judge Swain's alternative decision to deny a modification of the stay. Because she had dealt with the issue "briefly," he said it was necessary for Judge Swain "to revisit these rulings anew" by identifying the "precise nature and extent" of the collateral, the value of the collateral at filing, and the amount required for the operation of the toll roads. As he did in his other Aug. 8 opinion, he said that "much has transpired since September 2017." He also said the circuit's opinion should not imply how Judge Swain should rule on remand.

The opinions are *Ad Hoc Group of PREPA Bondholders v. Financial Oversight and Management Board for Puerto Rico (In re Financial Oversight and Management Board for Puerto Rico)*, 17-2079, and *Peaje Investments LLC v. Financial Oversight and Management*

Board for Puerto Rico (In re Financial Oversight and Management Board for Puerto Rico), 17-2165 (1st Cir. Aug. 8, 2018).

PROMESA's authority is in the Territories Clause of the Constitution, District Judge Swain says.

Constitutionality of the Puerto Rico Oversight Board Upheld in District Court

The Puerto Rico Oversight, Management, and Economic Stability Act, or PROMESA (48 U.S.C. §§ 2161 *et. seq.*), does not violate the Appointments Clause of Article II, Section 2, Clause 2 of the U.S. Constitution, even though members of the Financial Oversight and Management Board of Puerto Rico were not nominated by the President and confirmed by the Senate, according to District Judge Laura Taylor Swain.

Aurelius Investment LLC and affiliates filed a motion in August 2017 seeking dismissal of Puerto Rico's debt arrangement proceedings, arguing that the filing of the petition on behalf of the Commonwealth of Puerto Rico by the Oversight Board under Title III of PROMESA violated the Appointments Clause.

Holders of Puerto Rico general obligation bonds joined Aurelius but were opposed by the Oversight Board, the official unsecured creditors' committee, and COFINA bondholders, among others.

Judge Swain held a hearing on the motion to dismiss in January. In her 35-page opinion on July 13, Judge Swain held that PROMESA and the Oversight Board were properly constituted under the Territories Clause of the Constitution, Article IV, Section 3, Clause 2.

The Constitution of the Oversight Board

In June 2016, the Supreme Court ruled 5-2 that Congress excluded Puerto Rico from chapter 9 municipal bankruptcy and precluded the island commonwealth from adopting local laws to deal with the insolvencies of its instrumentalities, such as municipal power and water companies. Within days, Congress adopted PROMESA to afford the island an ability to deal with its crushing debt burden.

After an initial effort at negotiating a compromise with creditors out of court, the Oversight Board commenced debt adjustment proceedings for the commonwealth and its instrumentalities beginning on May 3, 2017. Aurelius contended in its motion to dismiss that the requirements of Title III of PROMESA were not satisfied because the Oversight Board was allegedly an unlawful entity, since its members were appointed in violation of the Appointments Clause.

The Oversight Board, the only entity authorized to initiate debt adjustment proceedings, is "an entity within the government of Puerto Rico," Judge Swain said, but "it is not subject to the supervision or control by the Governor of Puerto Rico . . . or the Legislature of Puerto Rico."

The Oversight Board is constituted of seven members, one appointed at the sole discretion of the President and six selected from a list of candidates provided by leaders of Congress. If any members appointed by the President were not on the congressional list, Senate confirmation would be required. Since the six were all on the list, there was no Senate confirmation.

Judge Swain's Analysis

Rejecting arguments by Aurelius, Judge Swain's opinion is a lesson in history about the governance of territories of the U.S., citing Supreme Court opinions going back to the eighteenth century.

Judge Swain explained that the Appointments Clause prescribes methods for appointing "Officers of the United States." In turn, the clause distinguishes between "principal officers," who must be nominated by the President and confirmed by the Senate, and "inferior officers," who may be appointed by the President alone, or by courts or heads of departments.

For Judge Swain, the "principal question" was whether members of the Oversight Board had to be appointed under the Appointments Clause. She held, though, that "Congress has plenary powers under the Territories Clause to establish governmental institutions for territories . . . that would not comport with the requirement of the Constitution if they pertained to governance of the United States." She noted that Congress cited the Territories Clause as the sole authority for enacting PROMESA.

Judge Swain then proceeded to find "that neither Presidential nomination nor Senate confirmation of the appointees of the Oversight Board is necessary as a constitutional matter . . . because the members of the Oversight Board are not 'Officers of the United States' subject to the Appointments Clause."

In sum, Judge Swain said that "the Oversight Board is a territorial entity and its members are territorial officers." Therefore, she said, "Congress had broad discretion to determine the manner of selection of the Oversight Board."

Judge Swain summarized her analysis and holding by saying that the "Oversight Board is an instrumentality of the territory of Puerto Rico . . . , that its members are not 'Officers of the United States' who must be appointed" under the Appointments Clause, "and that there is accordingly no constitutional defect in the method of appointment provided by Congress for members of the Oversight Board."

Consequently, Judge Swain denied the motion to dismiss the PROMESA proceedings.

The opinion is *In re The Financial Oversight and Management Board for Puerto Rico*, 17-3283 (D.P.R. July 13, 2018).

Bondholders won a skirmish but may still lose the war with Puerto Rico.

Two Courts Seemingly Differ on the Nature of Puerto **Rico's PROMESA Proceedings**

Two federal courts handed down decisions, both on July 13, about the status of the Financial Oversight and Management Board of Puerto Rico and the nature of proceedings under the Puerto Rico Oversight, Management, and Economic Stability Act, or PROMESA (48 U.S.C. §§ 2161 *et. seq.*).

Whether the two decisions are in conflict is arguable, and it's an open question as to whether the decision handed down by the Court of Federal Claims, or COFC, might eventually disrupt Puerto Rico's court-supervised debt arrangement proceedings.

This week, we reported on *In re The Financial Oversight and Management Board for Puerto Rico*, 17-3283 (D.P.R. July 13, 2018), where District Laura Taylor Swain, sitting in the District of Puerto Rico, ruled on July 13 that the appointment of members of the Oversight Board did not violate the Appointments Clause of the U.S. Constitution. To read the story, click here.

Also on July 13, Chief Judge Susan G. Braden of the COFC ruled that she had exclusive jurisdiction over claims by bondholders that they are entitled to compensation from the U.S. government because actions taken under PROMESA deprived them of property in violation of the Due Process Clause of the U.S. Constitution. Judge Braden therefore denied the government's motion to dismiss the bondholders' lawsuit. In the process, she cast doubt on some of the underpinnings of Judge Swain's opinion.

Significantly, Judge Braden stayed further proceedings in her court pending "final judgment" in Judge Swain's case.

If it makes your head swim, you're not alone. Interpreting the ultimate effect of the two decisions is like trying to predict the outcome of a chess match after the first two moves.

Judge Swain's Ruling

After the Supreme Court ruled that Puerto Rico was ineligible for chapter 9 municipal bankruptcy, Congress quickly adopted PROMESA. Months later, the Oversight Board, exercising its exclusivity authority, initiated court-supervised debt restructuring proceedings for Puerto Rico and its instrumentalities in the District of Puerto Rico. The Chief Justice tapped District Judge Swain of New York to oversee the PROMESA proceedings in Puerto Rico.

In the case before Judge Swain, bondholders argued that PROMESA violated the Appointments Clause because the Oversight Board was not appointed by the President and confirmed by the Senate.

In her July 13 opinion, Judge Swain denied the bondholders' motion to dismiss the PROMESA proceedings, concluding that "the Oversight Board is a territorial entity and its members are territorial officers" and therefore not subject to the Appointments Clause.

The Suit in the Court of Federal Claims

Attacking PROMESA, bondholders had opened a different front in the COFC less than a month before the motion to dismiss in Judge Swain's court.

In the Washington, D.C.-based COFC, the bondholders alleged they had suffered an unconstitutional taking of property because the Oversight Board required the Puerto Rico legislature to pass a law depriving them of collateral for their bonds. In the COFC, the bondholders sought compensation from the government for the property they allegedly lost.

The U.S. government filed a motion to dismiss, contending that Judge Swain had exclusive jurisdiction over the claims raised in the COFC. Also on July 13, Judge Braden denied the motion to dismiss.

Jurisdiction in the COFC

Judge Braden explained that the Tucker Act (28 U.S.C. § 1491) gives the COFC exclusive jurisdiction over claims for "just compensation" under the Takings Clause of the Fifth Amendment. However, the statute provides that Congress may withdraw Tucker Act jurisdiction by showing its "unambiguous intention."

The government argued that Judge Swain had exclusive jurisdiction because Section 2126(a) of PROMESA gives exclusive jurisdiction to the District of Puerto Rico for any action "arising out of this chapter, in whole or in part."

Judge Braden disagreed, holding that the COFC has jurisdiction because Section 2126(a) of PROMESA does not demonstrate the required "unambiguous intention."

No PROMESA Preemption

The government argued that PROMESA preempted the Tucker Act.

Judge Braden rejected the argument, because she found no "comprehensive remedial scheme" in PROMESA to compensate creditors for unconstitutional takings of property.

Significantly Judge Braden held that "the Tucker Act and PROMESA are capable of 'coexistence,'" because bondholders can "seek adjudication against the United States for 'just compensation' in the [COFC] and declaratory relief, if requested, in the [District of Puerto Rico]."

If there is a potential flaw in Judge Braden's decision, it could be her finding of no "comprehensive remedial scheme" because PROMESA and the Bankruptcy Code are carefully crafted to protect and compensate creditors for their rights in collateral.

Oversight Board Is a Federal Entity

Because the Tucker Act applies to claims against the U.S., the government sought dismissal by arguing that the Oversight Board is an entity of Puerto Rico.

Even though PROMESA provides that the Oversight Board "shall not be considered a department, agency, establishment or instrumentality of the Federal Government," Judge Braden said that characterizations in federal statutes are not binding on courts when it comes to deciding whether an organization is a government entity.

Judge Braden concluded that PROMESA met the three tests for concluding that the bondholders' suit is a suit against the government.

In the process, Judge Braden rejected the government's argument that PROMESA was enacted "pursuant to Congress' Article IV plenary authority over the territories," the theory that Judge Swain used in ruling that the Appointments Clause did not apply to the Oversight Board.

Although conceding that Congress has "broad latitude" over territories, Judge Braden said "*that authority* does not supplant the role of federal courts in protecting fundamental constitutional rights." [Emphasis in original.]

Judge Braden said that "the Takings Clause claim is alleged against the Oversight Board, as a federal entity." Therefore, she ruled, "Congress authorized the [COFC] with jurisdiction to adjudicate that claim."

Takings Suit Is Stayed

At the end of her opinion, Judge Braden took note of two disputes pending before Judge Swain, including the motion to dismiss that Judge Swain denied on July 13. Should the bondholders prevail in those litigations, Judge Braden said that the "appropriate remedy" may call for declaring

that the actions by the Oversight Board were "unlawful," requiring the restoration of the bondholders' collateral.

Although Judge Braden denied the government's motion to dismiss for the reasons discussed above, she said that "the interests of justice require that this case be stayed, at least until a decision and final judgment is entered in each of the above-referenced cases" before Judge Swain.

What Does It All Mean?

Superficially at least, the two July 13 opinions seem inconsistent. One court concludes that the Oversight Board is a federal governmental entity, and the other says members of the board are "territorial officers."

The conclusions may not be inconsistent, however, because it's conceivable that both are correct. A territorial officer may fit the definition of a governmental officer for the purpose of a Takings Clause suit but not with regard to the applicability of the Appointments Clause.

Appeals will go to different circuits. The Puerto Rico PROMESA decision will be reviewed in the First Circuit, but the COFC decision would go to the Court of Appeals for the Federal Circuit. However, the COFC decision likely is not a final order, meaning there will be no immediate appeal absent leave to appeal.

Consequently, there may be an appeal to the First Circuit but no appeal on the related issue to the Federal Circuit. If there are appeals to both circuits, and if the two circuits' decisions seem inconsistent, the Supreme Court would be the final arbiter.

Will the differing decisions foster settlement talks or embolden either side? Can Puerto Rico afford to settle with the bondholders? If Puerto Rico and the bondholders want to settle, will other creditors allow them to if it means smaller recoveries for them?

Is litigation ever the best method for resolving a bankruptcy?

If both July 13 decisions stand, the PROMESA proceedings could proceed to an ordinary conclusion, because Judge Braden only denied a motion to dismiss. She did not even hint, one way or the other, at whether bondholders were deprived of property without due process. In other words, the suit in her court could proceed to conclusion, and Judge Braden might decide there was no Taking Clause violation because the bondholders' constitutional rights were protected under PROMESA.

Or, if Judge Braden finds there was an unconstitutional taking, she might fashion a recovery against the U.S. for bondholders' losses as a consequence of PROMESA. A valid claim against

the U.S. government doesn't necessarily mean that the PROMESA court cannot approve and implement a debt arrangement.

Also recall how Judge Braden said that the suit in her court and the PROMESA proceedings "are capable of 'coexistence,'" because bondholders can "seek adjudication against the United States for 'just compensation' in the [COFC] and declaratory relief, if requested, in the [District of Puerto Rico]." Likely as not, bondholders will raise Takings Clause claims in opposition to any arrangement proposed by Puerto Rico. Therefore, Judge Swain might make the declaratory judgment to which Judge Braden referred.

Reversal of Judge Swain's decision is another matter. If there was an Appointments Clause violation, the PROMESA proceedings could unravel, allowing bondholders to push Puerto Rico to the wall unless Congress fashions another statute.

It's a mess. That's all there is to say. That's what happens when two courts share jurisdiction over one pot of limited resources.

The opinion is *Altair Global Credit Opportunities Fund (A) LLC v. U.S.*, 17-970 (Ct. Fed. Cl. July 13, 2018).

Judge refuses to issue declaratory judgments about Puerto Rico's use of tax revenues.

No Quick Exit for Any Creditors from Puerto Rico's Financial Mess, Judge Says

The New York district judge overseeing Puerto Rico's debt restructuring in substance said that no one will hit a home run through litigation and take home all the marbles. Instead, the Jan. 30 opinion by District Judge Laura Taylor Swain has the effect of forcing creditors of all stripes to participate in mediation and slog through the process of plan negotiation and confirmation.

Since May will be the first anniversary of Puerto Rico's debt restructuring under the Puerto Rico Oversight, Management, and Economic Stability Act, or PROMESA (48 U.S.C. §§ 2161 *et. seq.*), some creditor groups have sought a quick exit, especially since Hurricane Maria destroyed the island's infrastructure last September, along with any progress toward debt adjustment.

The creditor group with perhaps the best odds of staging a quick victory was the holders of general obligation bonds, sometimes known as constitutional debt because the bonds carry the island commonwealth's full faith and credit. Holders of the bonds, known as GO bonds, contend they are entitled to full and timely payment, even "in times of economic scarcity."

The GO bondholders therefore filed an adversary proceeding in which they contended that certain tax revenue cannot be used for any purpose other than the payment of constitutional debt and must be segregated for them alone. In response, Puerto Rico filed a motion to dismiss, which Judge Swain granted in her 19-page opinion on Jan. 30.

Judge Swain divided the claims for relief into two categories: She dismissed about a third for failure to state a claim on which relief could be granted. She dismissed the remainder for lack of subject matter jurisdiction.

The first category includes claims for declaratory judgments that certain tax revenues cannot be used for any purpose other than the payment of constitutional debt and must be segregated. Although they arose from a live, otherwise justiciable controversy, Judge Swain said they ran afoul of Section 305 of PROMESA and therefore failed to state a claim.

Section 305 prohibits the court from interfering with any of Puerto Rico's governmental powers or income unless the "Oversight Board consent or the plan so provides." Granting declaratory relief with respect to segregating tax revenue, Judge Swain said, would "result in declarations and injunctions that would directly restrict" Puerto Rico's use of tax revenue.

Because there was no consent by the Board and no plan, Judge Swain dismissed that portion of the complaint for failure to state a claim because "Section 305's prohibition is not limited to remedies that are directly coercive," she said.

In the second category, the claims ask the judge to rule that certain tax revenue is not Puerto Rico's property; the island commonwealth is a mere conduit; constitutional debt is secured by statutory liens; certain tax revenues are "special revenues" that can be applied only in compliance with provisions of chapter 9 that are applicable under PROMESA; and using certain tax revenue other than in payment of constitutional debt would be an unconstitutional taking of property.

Judge Swain said the second group of claims did not pass constitutional muster and therefore failed to state a claim because there was no "case or controversy."

Although the bondholders were seeking declaratory judgments, not injunctions, Judge Swain explained that "even significant disagreement" by itself does not state a claim unless there is "a specific live controversy of sufficient immediacy and reality to warrant the issuance of a declaratory judgment."

According to Judge Swain, there is no case or controversy because those claims sought "abstract declarations of the parties' respective relationships to the subject revenues, without application of the relief to resolve any current concrete dispute." Thus, the judge said, they "seek advisory opinions and do not frame justiciable controversies."

On the claim about unconstitutional takings, Judge Swain said that Puerto Rico has not made any "final decision" about how to treat the taxes in question. The takings claim, she said, "is not ripe for adjudication."

Judge Swain therefore dismissed the claims in the second category for lack of subject matter jurisdiction given the absence of a constitutional case or controversy.

Since Judge Swain dismissed the adversary proceeding, the bondholders can appeal to the First Circuit. Even if Judge Swain was wrong about the second category and there is a live controversy, those claims might also run afoul of Section 305 because they could have the effect of tying up the commonwealth's tax revenue before a plan is approved.

The opinion is *ACP Master Ltd. v. Commonwealth of Puerto Rico (In re Financial Oversight and Management Board for Puerto Rico)*, 17-189 (D. P.R. Jan. 30, 2018).

Can plaintiffs sue Puerto Rico government officials in their individual capacities? Two district judges disagree.

District Judges Starkly Disagree on the Scope of the PROMESA Automatic Stay

Two district judges in Puerto Rico starkly disagree about the applicability of the automatic stay to "ordinary course" litigation against commonwealth officials.

On April 30, District Judge William G. Young of Boston, sitting in Puerto Rico by designation, held that the automatic stay under the Puerto Rico Oversight, Management, and Economic Stability Act barred a suit against a commonwealth governmental official in his individual capacity, even though Puerto Rico itself was not named as a defendant.

Saying he "disagrees" with Judge Young, Chief District Judge Gustavo A. Gelpí ruled on May 14 that the automatic stay does not apply. He allowed a plaintiff to recover a judgment against a government official in his individual capacity.

Although the two cases are procedurally distinguishable, the First Circuit may be tasked with deciding whether Puerto Rico can hide behind PROMESA to halt lawsuits having nothing to do with the island's insolvency.

The Newest Case

In Judge Gelpí's case, a prisoner sued non-governmental third parties for inadequate medical care. The defendants included Puerto Rico governmental officials in their official and individual capacities. Much later, the plaintiff accepted a $50,000 settlement without specifying how the settlement would be apportioned among the defendants. Two weeks before Puerto Rico initiated its financial restructuring under PROMESA (48 U.S.C. §§ 2161 *et. seq.*), Judge Gelpí directed the defendants to pay the $50,000 within 90 days.

When Puerto Rico began its restructuring on May 3, 2017, PROMESA imposed an automatic stay by incorporating Section 922(a) of the Bankruptcy Code. That section automatically enjoins a suit against a government "officer" that "seeks to enforce a claim against" the government.

In the process of paying $40,000 after commencement of the PROMESA proceedings, the non-governmental defendants said that Puerto Rico had agreed the pay the remaining $10,000. Puerto Rico did not object to the statement but filed a notice regarding the automatic stay.

Months later, the plaintiff filed a motion seeking to compel Puerto Rico to pay the remaining $10,000.

Judge Young's Earlier Case

Judge Young ruled on a suit by several individuals seeking money damages for wrongful incarceration in violation of the U.S. Constitution and local law. Knowing that PROMESA would bar suit for damages against the commonwealth, the plaintiffs only sued individuals in their personal capacities.

Admitting that a decision either way would be "unfair," Judge Young decided to apply the stay, saying the complaint was among "the types of suits contemplated by PROMESA that require an automatic stay because the defense is funded" by the government of Puerto Rico.

Judge Gelpí's Analysis

The statute underlying both cases was a commonwealth law giving Puerto Rico the right but not the obligation to defend and indemnify governmental officials sued in their individual capacities. In Judge Gelpí's case, Puerto Rico had agreed long before bankruptcy to defend and indemnify the one official who was still liable on the judgment in his individual capacity.

Puerto Rico argued that PROMESA's automatic stay applied because the commonwealth had indemnified the official for a judgment against him in his individual capacity. Judge Gelpí disagreed, holding that the stay "does not apply to individual capacity claims," even when Puerto Rico has agreed to defend and indemnify.

Judge Gelpí followed his decision from August 2017, where he held that PROMESA's automatic stay did not apply to a $2 million lawsuit against Puerto Rico's superintendent of police for a police shooting that was claimed to be "a reckless and grossly negligent use of excessive force." *Guadalupe-Baez v. Pesquera*, 269 F. Supp. 3d 1 (D.P.R. 2017).

Judge Gelpí bolstered his decision by reference to Puerto Rico's sovereign immunity under the Eleventh Amendment and First Circuit authority holding that defense of a suit is not a waiver of immunity. If Puerto Rico is not being sued when it defends an official, he theorized that "it is not liable for any awards or settlements." Since the government is not liable, the stay does not apply because the plaintiff is not collecting a claim against the commonwealth.

Judge Gelpí disagreed with Judge Young on two counts. First, he disagreed with the notion that PROMESA contemplates an automatic stay covering officials in their individual capacities. Second, he was not persuaded by the argument that recruiting government workers would be harmed by permitting individual-capacity suits to proceed. He said that the effect on recruitment

"is a matter for the Commonwealth to consider when agreeing to represent officials . . . and [settle] on their behalf." It is not a matter for the court to consider, he said.

Judge Gelpí therefore held that he had power to compel the individual to pay the judgment in his personal capacity because the indemnification agreement was between the official and the government, not between the government and the plaintiff. However, the judge conceded that he did not have power to compel the government to pay the settlement.

To read ABI's report on Judge Young's case, click here. For Judge Gelpí's decision from last year, click here.

The opinion is *Colon-Colon v. Negron-Fernandez*, 14-1300 (D.P.R. May 14, 2018).

On tough automatic stay cases, let the PROMESA judge decide.

Puerto Rico Judge Has a Third Answer to the PROMESA Automatic Stay Question

Since district judges in Puerto Rico disagree about the applicability of the automatic stay under the Puerto Rico Oversight, Management, and Economic Stability Act, one district judge came up with a solution: Impose the stay, but tell the plaintiff to move for modification of the stay in the court handling Puerto Rico's debt restructuring.

The opinion on May 16 by District Judge Francisco A. Besosa of San Juan included a hint that the PROMESA court should seriously consider modifying the stay to ensure protection of the plaintiff's constitutional rights.

In the case before Judge Besosa, a prisoner filed suit under 42 U.S.C. § 1983, alleging that the conditions of his confinement violated the Eighth Amendment because, as a potential witness, his life was in danger since he was being housed in the general prison population. He sought both an injunction and $3 million in monetary damages.

Twice before, Judge Besosa had refused to impose PROMESA's automatic stay in 42 U.S.C. § 2161, saying that a provision PROMESA, 42 U.S.C. § 2106, specifically provides that nothing in the statute will relieve Puerto Rico from complying with federal law. However, Puerto Rico filed a motion for rehearing and won.

Puerto Rico began its debt restructuring under PROMESA on May 3, 2017. Over the ensuing year, "the parameters of the automatic stay [became] more precise," Judge Besosa said. His opinion cites cases going both ways with regard to "ordinary course" litigation, noting that the stay has been held not applicable to petitions for *habeas corpus* and to suits seeking only injunctions and not monetary damages.

Reciting cases that have imposed the PROMESA stay, Judge Besosa concluded that "PROMESA and precedent from this district establish that the automatic stay encompasses [the plaintiff's] Section 1983 action."

Reflecting his point of view, Judge Besosa cited cases where the First Circuit had applied the PROMESA stay to appeals in Section 1983 suits. He also cited *Ruíz-Colón v. Rodriguez*, 17-2223, 2018 U.S. Dist. Lexis 74455 (D.P.R. April 30, 2018), where District Judge William G. Young imposed the stay on a prisoner's suit for violation of constitutional rights. For ABI's discussion of *Ruíz-Colón*, click here.

Judge Besosa concluded that the stay was invoked automatically because Puerto Rico was shouldering the expense of litigation and would be liable for judgments. Still, he was “mindful” that the plaintiff was seeking compliance with the Constitution.

Although he imposed the stay, Judge Besosa said the plaintiff could seek a modification of the stay from the district judge responsible for Puerto Rico’s financial restructuring under PROMESA.

Last week, ABI reported *Colón-Colón v. Negron-Fernandez*, 14-1300 (D.P.R. May 14, 2018), a decision by Chief District Judge Gustavo A. Gelpí. The decisions by Judges Besosa and Gelpí are difficult if not impossible to reconcile because Judge Gelpí seemed reluctant to impose the stay on ordinary course litigation, even in a case not involving the plaintiff’s constitutional rights. To read ABI’s discussion of Judge Gelpí’s decision, click here.

The opinion is *Betancourt-Rivera v. Vázquez-Garced*, 17-2040 (D.P.R. May 16, 2018).

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LAST TERM IN THE SUPREME COURT

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Supreme Court Narrowly Interprets the Safe Harbor, Overrules the Majority of Circuits

Merit Management Group LP v. FTI Consulting Inc., 138 S. Ct. 883, 200 L. Ed. 2d 183, 86 U.S.L.W. 4088 (Sup. Ct. Feb. 27, 2018).

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A False Statement About One Asset Isn't Grounds for Nondischargeability, Supreme Court Rules

Lamar, Archer & Cofrin LLP v. Appling, 138 S. Ct. 1752, 201 L. Ed. 2d 102, 86U.S.L.W. 4362 (Sup. Ct. June 4, 2018).

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Supreme Court Says Insider Status Is Reviewed for Clear Error; Hints Existing Test Is Wrong

U.S. Bank NA v. The Village at Lakeridge LLC, 138 S. Ct. 960, 200 L. Ed. 2d 218, 86U.S.L.W. 4121 (Sup. Ct. March 5, 2018).

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THIS TERM IN THE SUPREME COURT

High Court to Decide Whether FDCPA Applies to Nonjudical Foreclosure

Obduskey v. McCarthy & Holthus LLP, 17-1307 (Sup. Ct.); Obduskey v. Wells Fargo, 879 F.3d 1216 (10th Cir. 2018).

THIS TERM IN THE SUPREME COURT (MAYBE)

‘*Cert*’ Petition Asks Supreme Court to Overrule *Lubrizol* on Trademark Licenses

Mission Product Holdings Inc. v. Tempnology LLC, 17-1657 (Sup. Ct.); *Mission Product Holdings Inc. v. Old Cold LLC (In re Old Cold LLC)*, 879 F.3d 376 (1st Cir. Jan. 12, 2018).

Materials pages 18 & 30.

First Circuit Splits with the Ninth over Good Faith Defense to Discharge Violation

IRS v. Murphy, 892 F.3d 29(1st Cir. June 7, 2018); *Lorenzen v. Taggart (In re Taggart)*, 888 F.3d 438 (9th Cir. April 23, 2018), rehearing denied Sept. 7, 2018; *RESS Financial Corp. v. Beaumont 1600 LLC (In re The Preserve LLC)*, 17-1357 (B.A.P. 9th Cir. Sept. 7, 2018).

Materials pages 140 & 145 and Rochelle's Daily Wire Sept. 11.

Tenth Circuit Direct Appeal to Decide Whether the Automatic Stay Is Really Automatic

*Davis v. Tyson Prepared Foods Inc. (In re Garcia), (*10th Cir. 17-3247); argument held Sept. 26, 2018.

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Circuit Split Narrows on the New Value Defense to a Preference

Kaye v. Blue Bell Creameries Inc. (In re BFW Liquidation LLC), 17-13588, 2018BL 289591 (11th Cir. Aug. 14, 2018).

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NOT THIS TERM IN THE SUPREME COURT

Arbitration and Executory Contracts ‘*Cert*’ Petitions Denied

Credit One Bank NA v. Anderson, 17-1652 (Sup. Ct. *cert*. denied Oct. 1, 2018); *Noble Energy Inc. v. ConocoPhillips Co.*, 17-1438 (Sup. Ct. *cert*. denied Oct. 1, 2018).

Materials page 171 and Rochelle’s Daily Wire June 24, 2018.

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District Court Finds Constitutional Power to Grant Releases in Confirmation Orders

Opt-Out Lenders v. Millennium Lab Holdings II LLC (In re Millennium Lab Holdings II LLC), 17-1461 (D. Del. Sept. 21, 2018).

New Case; Rochelle's Daily Wire Sept. 25, 2018.

CHAPTER 11 PLANS & CONFIRMATION

Ninth Circuit Holds that One Accepting Class in Joint Plan Is Sufficient

JPMCC 2007-C1 Grasslawn Lodging LLC v. Transwest Resort Properties Inc. (*In re Transwest Resort Properties Inc.*), 881 F.3d 724 (9th Cir. Jan. 25, 2018).

Materials page 70.

AUTOMATIC STAY

A Convert Joins the Minority Interpretation of the Repeat-Filing Stay Termination

In re Goodrich, 17-10500, 2018 BL 259156 (Bankr. D. Vt. July 20, 2018).

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FDCPA Applies to Debt Collectors Even if They Own the Debt

Tepper v. Amos Financial LLC, 17-2851, 2018 BL 280483, 2018 Us App Lexis 21907 (3d Cir. Aug. 7, 2018).

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Homestead Exemption Must Be Paid in Full Before a Sale Is Permitted, BAP Says

Jubber v. Bird (In re Bird), 577 B.R. 365 (B.A.P. 10th Cir. Nov. 30, 2017).

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CHAPTER 13 PLANS AND CONFIRMATION

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District Court Allows 401(k) Contributions in Chapter 13 Up to the IRS Limits

Miner v. Johns, 17-879, 2018 BL 183240 (W.D. La. May 23, 2018).

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Politicians in Washington, D.C., are coalescing around a financial plan to rescue Puerto Rico, just weeks before an expected major default on bond payments that

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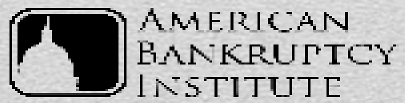

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9th Circuit

September 1, 2017

Fourth Circuit Conflicts with the Fifth on Loss of Chapter 7 Exemptions after Filing

By The Numbers

- Total cases in system : 646
- Business Cases : 223
- Consumer Cases : 284

Chapter 13 and Student Loans
The First Annual Connecticut Bankruptcy Conference
October 4, 2018

Charles A. Maglieri, Law Office of Charles A. Maglieri, Bloomfield, CT

Eugene S. Melchionne, National Association of Consumer Bankruptcy Attorneys, Waterbury, CT

Roberta Napolitano, Chapter 13 Standing Trustee, District of Connecticut

Carl T. Gulliver, Coan Lewendon Gulliver & Miltenberger LLC, New Haven, CT

Introduction--Charles Maglieri and Gene Melchionne

Plan related issues— pay outside the plan as a schedule J line item expense relative to cram down projected disposable income test

1. Separate classifications for plan and confirmation requirements—Roberta Napolitano

2. Modification of rights of holder of the claims—Charles Maglieri

3. Pay outside the plan as a schedule J line item expense relative to cram down projected disposable income test—Charles Maglieri

Non-bankruptcy strategies and chapter 13

4. Non-Bankruptcy programs such as ICRP options / Drafting a plan to ensure that a debtor remains in specialized student loan programs—Gene Melchionne

Filing strategy / Means Test issues

5. Means test issues i.e. marital adjustment deductions; special circumstances and effect on DMI calculations—Charles Maglieri

6. Are the value of student loan debts a factor in the Section 109(e) eligibility calculus—Carl Gulliver

Discharging Student Loans

7. Brunner Test vs. the First Circuit's Totality of Circumstances / application in 13—Carl Gulliver

Proposed law changes

8. Legislative highlights—Gene Melchionne

I. Plan related issues—

A. Separate classifications for plan and confirmation requirements

1. Relevant portions of statutes

   a. 11 U.S.C. § 1322(b)(1):

Subject to subsections (a) and (c) of this section, the plan may—(1) designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated; however, such plan may treat claims for a consumer debt of the debtor if an individual is liable on such consumer debt with the debtor differently than other unsecured claims;

   b. 11 U.S.C. § 1122(a):

Except as provided in subsection (b) of this section, a plan may place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class.

   c. 11 U.S.C.A. § 1129(b)(1):

Notwithstanding section 510(a) of this title, if all of the applicable requirements of subsection (a) of this section other than paragraph (8) are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan notwithstanding the requirements of - such paragraph if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.

2. Factors examined in determining unfair discrimination.
3. "Somewhere between total whim and an Act of God lies the answer to what justification is needed to hew out a particular class of unsecured creditors and

distinguish it from other unsecured creditors." *In re Orawsky*, 387 B.R. 128, 141 (Bankr. E.D. Pa. 2008).

4. *Leser* Test (allowed favorable treatment of child support obligation):
    a. "By allowing for separate classes of unsecured claims, Congress anticipated some discrimination, otherwise separate classes would have no significance. It is only unfair discrimination that is prohibited." *In re Leser*, 939 F.2d 669, 671–72 (8th Cir. 1991).
    b. Referred to an "overwhelming public policy in favor of providing for support of children." *Leser* at 672.
    c. Test: (1) whether the discrimination has a reasonable basis; (2) whether the debtor can carry out a plan without the discrimination; (3) whether the discrimination is proposed in good faith; and (4) whether the degree of discrimination is directly related to the basis or rationale for the discrimination. *Ibid*.
5. *Bentley* ("Baseline")Test [*In re Bentley*, 266 B.R. 229, 240 (B.A.P. 1st Cir. 2001)]:
    a. Test:
        1. Equality of distribution – unless the Code confers priority, unsecured creditors should share equally in any dividend. The burden of justification is on those who propose plans to the contrary (implying it can be done). *Bentley* at 240.
        2. Non-priority of student loans- a debt doesn't acquire priority just because it can't be discharged. *Bentley* at 241.

3. Contributions- mandatory v. voluntary. Debtors propose only a minimum, mandatory payment, which enhances the position of the student loan creditors, who are assured of payments after the plan is consummated because of the nondischargeability of their debts. Remaining unsecured creditors will receive nothing more. *Bentley* at 242-3.
4. Fresh Start – doesn't mean a debtor will emerge completely free of student loan obligations. *Bentley* at 242.

b. Examination of fairness involves three parties – the debtor, the preferred class, and the class discriminated against. *Bentley* at 239.

c. Establishing a favored class for student loans transfers the burden from the Debtor to unsecured creditors. "In the balance of burdens and benefits that the Code establishes as a baseline, the postbankruptcy balance due on student loans should be paid by the Debtors out of assets that they are not required to commit to the plan, not by general unsecured creditors out of their share of the Debtor's minimum contribution." *Bentley* at 243.

6. *In re Genco Shipping & Trading Ltd.*, 513 B.R. 233 (Bankr. S.D.N.Y. 2014):

a. Chapter 11 Case

i. Test:

1. there is a reasonable basis for discriminating,
2. the debtor cannot consummate the plan without the discrimination,

3. the discrimination is proposed in good faith, and

4. the degree of discrimination is in direct proportion to its rationale.

ii. *Genco* at 242.

7. _*In re Strausser*, 206 B.R. 58 (Bankr. W.D.N.Y. 1997)

a. Issue: could debtor pay single cosigned consumer debt in full and five percent of debt of remaining unsecured creditors?

b. Issue:

i. Adds a prong to test similar to the one used in *Genco*:

1. there is a rational basis for discriminating,

2. the classification is necessary to the debtor's rehabilitation under Chapter 13,

3. the discrimination is proposed in good faith, and

4. there is a meaningful payment to the class discriminated against and

5. the difference between what the creditors discriminated against would receive and the amount they would receive if there were no separate classification.

8. Applications:

a. *In re Quinn*, 586 B.R. 1 (Bankr. E.D. Mich. 2018) - Court rejected various tests and considered "totality of circumstances" in refusing to confirm Debtor's plan treating student loan claims more favorably. "The Debtors argue that if their plan is confirmed, they will owe $215.78 less

on their student loan debt at the end of the plan's sixty month term, but if the Trustee's objection is sustained, they will owe $6,006.22 more on their claim. The Court finds that this slight benefit to Debtors does not offset the discrimination against the remaining unsecured creditors." Quinn at 6.

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

    i. Test - *Bentley* with broader discussion of separate classifications to accurately reflect facts of case. *Engen* at 538.

    ii. Public interest considerations:

        1. First day orders which disturb the priority of the Code are available in Chapter 11. *Engen* at 535.

        2. The rationale behind every other nondischargeable debt under Section 523 of the Code is to punish undesirable conduct or curtail rewards for "socially undesirable behaviors." Student loan debt is the only debt incurred for "socially beneficial purpose." *Engen* at 540-541.

        3. Congressional intent in making student loans nondischargable was the preservation of the government's fiscal health as guarantor or lender of these loans; therefore, it would further a legitimate public policy to favor them. Amendment making loans nondischargeable came as part of a federal budget balancing package which

suggests purpose was to serve a societal interest in maximizing payments. Engen at 541-7.

4. "The massive shift of the skyrocketing costs of college education to the middle class over the last three decades has replaced the decreased government subsidization of public colleges and universities. It is accurate to classify student loan debt as singular in identity since borrowers are in effect compensating for the reduced tax revenue allocated to post-secondary education. Adjusted for inflation, the cost to attend a four-year public university has increased 331% since 1983.[213] This societal tax burden has created what is in effect individual taxation to the public university attendee, much of which is funded by student loan borrowing." Engen at 548.
5. "It is this Court's experience that many consumer bankruptcies are filed by desperate individuals, who are financially, emotionally and physically exhausted. Sometimes lost in the discussion that the bankruptcy discharge provides a fresh start to honest but unfortunate debtors is that, perhaps as importantly, it provides a commensurate benefit to society and the economy: People are freed from emotional and financial burdens to become more energetic, healthy participants. Of course, this

beneficial effect is properly curtailed by the existence of debts that are excepted from discharge. Here, the Debtors do not seek to escape their liability for the Student Loan Claims, but to the contrary, they seek to pay them." *Engen* at 550.

iii. Above/below median debtor: Above, but projected monthly income would have generated a zero percent dividend to unsecured creditors. *Engen* at 526-7.

iv. Unusual fact pattern: Debtors participated in a Debt Management Plan ("DMP") and paid down approximately 83% of their unsecured debt. However, participation in the DMP caused the debtors to default on their mortgages, and incur priority tax debt of about $25,000.00. *Engen* at 527. Debtor is co-borrower for son on one treated loan. *Engen* at 526. Co-Debtor inherited an IRA more than 180 days after filing with a balance of $73,269.34 which was used to fund the plan. *Engen* at 526.

9. *In re Mason*, 456 B.R. 245 (Bankr. N.D.W. Va. 2011) –

   a. Court is mindful of all circumstances.

   b. "Finding that a basis exists to treat student loan debts more favorably than other unsecured creditors, however, does not necessarily afford a license to a debtor to pay student loan creditors all their Chapter 13 actual, disposable income while not making any payments to other unsecured creditors—even assuming that the best interest of creditor test

of § 1325(a)(4) would otherwise be met by a 0% payout. A debtor must be able to articulate a reason why the discriminatory treatment is being proposed, and be able to demonstrate that a lesser discriminatory means of treatment is not advisable."

c. Public policy considerations: Student loans are "critical to the general welfare and prosperity of the United States." *Mason* Va. at 248.

d. Unusual circumstances: None. However: "For example, if the 72% distribution will prevent the unwarranted accrual of interest and/or penalties during the term of the Chapter 13 plan, the court is likely to find the discrimination acceptable. *Mason* Va. at 253, ft. 8.

10. *Orawsky* – plan must maintain *equity* among creditors of equal priority (*emphasis* added):

a. Finds *Bentley* test helpful as a framework for determining "fairness" under Section 1322(b)(1). The Court confirmed plan which paid $100 a month for the benefit of unsecured creditors and allowed deduction of $217 a month in current student loan payments from projected disposable income.

b. "Fair" ≠ "*pro rata*." Mandating *pro rata* distribution in every situation is contrary to Section 1322(b)(1)'s express authorization for **separate** classification. *Orawsky* at 146.

c. Public interest considerations: Public interest in promoting solvency of educational loan programs may provide a foundation for favored treatment of student loan claims. *Ibid*.

d. Above/below median debtor: Below median debtor whose plan payments the Court characterized as "voluntary." *Orawsky* at 148.

e. Unusual fact pattern: None.

11. *In re Mason*, 300 B.R. 379 (Bankr. D. Kan. 2003).

    a. Court applies a hybrid of *Leser*, *Bentley*, and test in *In re Colfer*, 159 B.R. 602 (Bankr. D. Me. 1993).

    b. "Even if debtor's plan were confirmed as submitted, and all of the payments under the plan were made, some 83 percent of the student loan obligations would remain unpaid at discharge and nondischargeable. This does not compare favorably to the 93 percent that would remain were the discrimination provision dropped. The unsecured creditors are unduly burdened to benefit the holders of nondischargeable student loan debt. No coherent reason to approve this discriminatory treatment is given. As the debtors will only benefit marginally and the creditors will be unduly harmed, the Court concludes that the proposed treatment discriminates unfairly against the general unsecured creditors." *Mason KS* at 388.

12. *In re Belton*, No. CV 16-03040-JW, 2016 WL 7011570 (Bankr. D.S.C. Oct. 13, 2016)

    a. Streamlined test: (1) Is there a good faith, rational basis for the separate classification; (2) Is the separate classification necessary to the debtor's rehabilitation under Chapter 13; and (3) Is there a meaningful payment to the discriminated class.

b. Below median debtor.

c. "Curing the debtor's default under student loan provided a good faith, rational basis for the proposed separate classification because would make her future employment more likely, the separate classification was necessary to her rehabilitation, and unsecured creditors would receive a meaningful distribution." *Belton* at 1.

B. Modification of rights of holder of the claims**:** To what extent does Section 1322(b)(2) allow for the modification of the rights of the holder of an allowed student loan claim?

1. The Permissive Plan provisions of Section 1322(b) provides in sub-part (2) that the debtor may modify the rights of holders of allowed secured claims, other than claims secured only by a security interest in real estate which is the debtor's principal residence **or** of "holders of unsecured claims,..". Assuming that the student loan claim in question is an "allowed unsecured claim" then this section also allows for the modification of the rights of the holder of the student loan claim as one can likewise modify the rights of a holder of a secured claim.

2. In what respect can the rights of such a holder be modified? One must look to the terms of the promissory note and the rules and regulations pertaining to the creation, enforcement and interpretation of such claims.

3. The rights afforded to such claim holders pursuant to Title 11 cannot be modified.

4. Section 1322(a) sets forth those mandatory plan provisions requirements which can't be modified relative to certain claims. However, student loan claims as "non-priority" unsecured claims are not covered by Section 1322(a) other than as

to sub-part (3) relative to the treatment of those claims as set forth in allowed classes of claims.

5. The Section 1322(b)(2) powers of modification are subject to the mandated limitations of Section 1322(a).
6. Since no such limitation set forth in Section 1322(a) pertain to student loan claims, other than that which pertain to treatment of individual claims within a specified class, then in this respect, it would appear that the rights of holders of allowed student loan claims are indeed subject to "modification".
7. However, said proposed modifications are likewise limited by the mandatory requirements of Section 1325(a)(4) which requires that said unsecured claims receive no less than the Chapter 7 liquidation test amount or the so called "Best Interests Test".
8. Accordingly, those rights which are apparently subject to modification must necessarily pertain to the contract rights as set forth in the note relative to: a.)debt amortization, b.) loan term, c.) schedule of payments due, d.) allocation of payments to interest and principal, e.) subordination, f.) terms of default and curing of same, g.) accrual of and rates of interest charged; h.) how interest is calculated and assessed, i.) penalties assessed and charged, j.) collection rights and remedies, including the rights of US Treasury Offset and k.) generally all rights relative to enforcement, modification, and collection.
9. Relative to the areas of possible ways to propose a modification of rights of holders of allowed unsecured student loan claims, those proposed modifications must also be drafted taking into account the provisions for permissive plan terms

as set forth in Section 1322(b)(1)-(11). Of special interest, in this regard, are sub-parts (10) and (11).

10. Sub-part (10) allows for the plan to pay interest on those debts which cannot be discharged under Section 1328(a) but only after payment in full is made to all other allowed unsecured claims. A plain reading of this section would seem to allow for the payment of interest to student loan claims in the situation where other unsecured claims are paid in full but not paid together with interest, but interest being paid only to the holders of student loan claims. This allowed treatment seems to identify the situation whereby the debtor is **not deemed to be solvent** but where one's DMI is sufficient to justify paying 100% to all claims or where the Chapter 7 test provides for the same dividend.
11. Sub-part (11) provides that the Debtor may provide for any other "appropriate" plan provision not otherwise inconsistent with the provisions of Title 11.
12. Based upon the foregoing review of the permitted scope of the power to modify the rights of holders of allowed unsecured claims, taken together with those mandatory plan provisions set forth in Section 1322(a) and the confirmation requirements of Section 1325(a), one can see that the ability to modify rights of holders of student loan claims is provided for by the Code in various sections and under certain specified circumstances.
13. <u>Examples of modifications for consideration:</u> a.) change of interest rates and how calculated; b.) deferral of collection rights; c.) reallocation of payments made as to reducing principal and/or interest; d.) payments being placed in

deferment during the life of the plan; e.) how non-payments are to be reported on one's credit report; f.) maintaining work out plans allowed pre-petition as a term of the Chapter 13 plan to be confirmed; g.) modification of penalty and/or forfeiture clauses, if any; h.) waiver of interest accrual during deferment periods (*subject to argument that any such accrued interest may not be discharged, hence not subject to waiver); i.) Exercise of collection rights against co-obligors; j.) Limitations imposed upon creditor's right to elect certain remedies.

14. The ultimate modification of the rights of holders of allowed student loan claims comes not by the provision of Section 1322(b)(2) but by the operating provisions of Section 1327(a)-(c) Effect of confirmation, and the effect of such a creditor in not objecting to any such plan term setting forth a proposed modification or any other plan term which affects the rights of the holder. See, United Student Aid Funds, Inc. v. Espinosa, 559 U.S. 260, 130 S.Ct. 1367, 176 L.Ed.2d 158 (2010).
15. Further means by which rights of holders of such claims can be modified is to seek strict enforcement of the terms of the claims as represented by the individual Proof of Claims submitted by the holder. Should such a claim contain erroneous information and no objection is filed by the Debtor and the POC is relied upon and incorporated into the plan which is ultimately confirmed, then the claim is paid as provided for by the allowed POC pursuant to Section 502 Allowance of Claims.

C. Pay outside the plan as a schedule J line item expense relative to cram down projected disposable income test: Whether or not monthly student loan payments

coming due during the Plan term can be taken as an allowed Schedule J line item household expense for purposes of defending a Section 1325(b)(1)(B) Objection to Confirmation alleging that all disposable income has not been committed to plan for the Applicable Commitment Period.

1. Schedule J mandates that all household expenses be listed on the form; a student loan payment not in deferment is an expense that requires payment by the debtor and must be listed.
2. Maintaining the payment as a household expense but not providing for payment of the claim pro rata with all other allowed unsecured claim will diminish available Projected Disposable Income (“PDI") to be used to pay allowed unsecured claims generally.
3. An objection filed by Trustee or holder of an allowed unsecured claim under Section 1325(b)(1) implicates a challenge to confirmation.
4. To overcome the challenge the Debtor must either pay allowed claims 100% per sub-part A or prove that Debtor has submitted all "PDI" for the duration of the Applicable Commitment Period ("ACP") to pay holders of allowed unsecured claims under sub-part B of Section 1325(b).
5. Must Debtor include student loan claims in the plan even if the loan payments are current? How is this fair to the Debtor if one is forced to either default on the payments or place the loan on deferment and thereafter incur interest for the duration of the plan term?
6. Does Section 1322(b)(1) allow for a separate classification to provide for disparate treatment of student loan claims?

7. If so, then objection to confirmation can be rebutted and the cram down standard can be met if the classification allows for the payment of the claim outside of the plan as a Schedule J expense; the plan may simply provide for a separate classification for student loan claims which essentially states that some or all of these claims will be paid as a line item expense on Schedule J.
8. If loan is paid outside of plan to keep it current then those payments reduce the Disposable Income (“DI") available to pay claims as that term is defined by Section 1325(b)2).
9. DI is defined differently depending upon whether the Debtor's household income is Above the Median Income (“AMI”) or Below the Median Income (“BMI”) for the relevant household size of the Debtor.
10. To overcome objection to confirmation where debtor can't pay 100% of unsecured claims the debtor must establish that all available PDI is being allocated over the ACP for payment to unsecured creditors.
11. But PDI is determined in accordance with the definition set forth in Section 1325(b)(2) and varies depending upon if Debtor is "AMI" or “BMI".
12. If a Debtor is BMI, then disposable income is defined by Section 1325(b)(2) and is committed for 36 months.
13. If Debtor is an AMI then it is defined by Section 1325(b)(3) relative to the calculations set forth on Official Form 122C-2 Chapter 13 Calculation of Your Disposable Income per the means test and is committed for 60 months.
14. Calculation of PDI for the 60-month ACP Debtor is a function of the Means Test calculation set forth on line 45 of form 122C-2.

15. Calculation of the PDI for the 36-month ACP Debtor is calculated in accordance with Exhibit A attached hereto, which is not simply a function of using Official Forms I and J.
16. For the BMI Debtor the student loan payment must be allowed under Section 1325(b)(2) as a deduction from CMI as an expense for the maintenance or support of the Debtor or a dependent of the Debtor, or as a Domestic Support Obligation ("DSO") or as a Charitable contribution or if the debtor is self-employed whether the loan payments qualify as a business expense necessary for the continuation, preservation and operation of the business.
17. The applicable commitment period of the Debtor is calculated pursuant to Section 1325(b)(4) depending upon one's household size.
18. Accordingly, one's PDI will differ depending upon whether the debtor has an ACP of 36 or 60 months both in terms of duration of commitment and monthly amount.
19. If Student Loan claims are included in the plan and paid as an allowed unsecured claim, how can that claim be separately classified from other unsecured claims and be paid more than what is being paid to other classes of unsecured claims?
20. How does one justify the different treatment relative to Section 1122 directive that the plan may not "discriminate unfairly" against any class so designated?
21. Disparate treatment of classes of claims where one class is for student loan claims must also meet the Confirmation Requirement of Section 1325(a)(4) whereby each such claim, however classified, must receive that dividend payment which would be paid in a hypothetical Chapter 7 Liquidation case. As

long as payment for each class of claims meets the Chapter 7 Best Interest Test and all class of claims are paid the Debtor's Best Effort, can a plan be confirmed that proposes that a class of student loan claims be paid a higher percentage than other classes of claims?

22. Does disparate treatment of a class of student loan claims constitute a per se discrimination so that the "good faith filing of plan" confirmation requirement of Section 1325(a)(3) is plainly violated?

23. Should the plan be confirmed based upon the Debtor's showing that all PDI is committed to the payment of allowed unsecured claims over the term of the ACP, that the separate classifications are allowed under Section 1322(b)(1) and where each unsecured claim receives the Chapter 7 equivalent? If so, then does the disparate treatment of student loan claims become a routine matter for plan drafting techniques thus constituting "fair discrimination" relative to other classes of claims?

24. What constitutes "unfair discrimination"? : a.) Must have a rational basis for the separate class; b.) the proposed class must be necessary to the debtor's rehabilitation under the Chapter 13; c.) the proposal of the discrimination is made in good faith; d.) there is a meaningful payment provided to the classes discriminated against; e.) the difference paid among the classes discriminated must be compared to the amount they would receive if not discriminated. (See, In re Strausser, 206 B.R. 58 (Bankr. W.D. N. Y. 1997).

25. If the plan sets forth a separate classification for the treatment of Student Loans pursuant to Sections 1322(b)(1) and 1122 of Chapter 11 so that the payments

continue outside the plan, can the monthly payments be taken on the Means Test since they will be itemized on Schedule J?

26. If there is more than one obligor on the Student Loan claim does not Section 1322(b)(1) provide that such claims may be classified and treated differently than other "consumer debts"?
27. Is a student Loan claim a "consumer debt"? “Consumer debts” are defined in Section 101(8) as…” a debt incurred "primarily for a personal, family, or household purpose."
28. If Student loans are incurred as a Consumer Debt, as defined, then how can such a payment be deducted as a marital adjustment if it is in fact an expense of the "household"?
29. See Attachment A – Calculation for disposable income for below median income debtors.

D. Deferment of payment while in chapter 13

II Non-Bankruptcy programs such as ICRP options / Drafting a plan to ensure that a debtor remains in specialized student loan program

A. Student Loans in chapter 13 – See Attachment B
B. Berry Order—Federal Loan Servicing – See Attachment C
C. Chapter 13 Plan nonstandard template for IDR plans – See Attachment D
D. Sample Order Confirming Plan – See Attachment E

III. Filing strategy / Means Test issues—

A. Means test issues i.e. marital adjustment deductions; special circumstances, and what effect on DMI calculations: Whether or not the AMI Chapter 13 Debtor can claim monthly student loan payments on the Means Test?

1. Can such payments be allowed for the Debtor as a line item deduction as a secured claim if the US Treasury Offset right makes the claim a "secured claim" if not otherwise secured?
2. As a non-priority unsecured claim can it be allowed on the Means test as a special circumstance or otherwise?
3. If Debtor is in a workout program entered into prior to filing the Chapter 13 case i.e. an Income Contingent Repayment Plan ("ICRP" or similar accommodation), can the modified monthly plan payment be a line item deduction anywhere on the Means Test including as a special circumstance?
4. Can the student loan payments of a non-filing spouse be allowed on the Means Test of the filing spouse as a "Marital Adjustment Deduction"? How does such a payment contribute to the support of the debtor, dependents or the household thus disqualifying such payments as an allowed marital deduction?
5. If payments are allowed for either the Debtor or non-filing spouse then the result is that the PDI set forth on Line # 45 of Schedule 122C-2 is reduced by the amount of the payments deducted.
6. If so allowed, then any objection filed under Section 1325(b)(1) can be successfully rebutted by the AMI Debtor consistent with the definition of PDI.

7. The definition of PDI must be read relative to the definition of DI as set forth in Section 1325(b)(3) which incorporates Means Test expenses allowed under Section 707(b) relative to the applicable household size.
8. Should the student loan payment be allowed by the court as a separate class of claims and the treatment provided to that class results in the payment of the claim being taken as a line item Schedule J expense, then should not that budget item be allowed on the Means Test as a "special circumstance" deduction?
9. Should the Debtor or the non-filing spouse be subject to a Family Court Order obligating one or the other spouse to pay for a child's college education then is it not possible that the student loan payment can be deducted as a "DSO" obligation on line 19 of Form 122C-2?
10. What of the situation whereby the Student Loan obligation is incurred to pay for the education of another attending a Religious Institution of Higher Education and the Debtor committed to the loan as a Charitable Contribution for the student attending the school who must upon graduation commit to missionary services sponsored by the school? (*An example of a situation from a real case not yet filed!!).

B. Section 109(e) and student loan debt

1. Chapter 13 eligibility limited to debtor with less than $394,725 of noncontingent, liquidated, unsecured debt. 11 USC §109(e)
   a. "[A] debt is contingent if it does not become an obligation until the occurrence of a future event…." *In re Mazzeo*, 131 F.3d 295, 303 (2d Cir. 1997)

(Unsecured debts for §109(e) calculations include personal liability asserted against Chapter 13 debtor-officer for business taxes)

b. A debt is unliquidated if its value is unknown and not readily ascertainable or calculable. *Mazzeo,* 131 F.3d at 304.

c. See generally exhaustive compilation on application of terms in 109(e) at 95 A.L.R. Fed. 793

2. Could a student loan on Income Based Repayment be contingent or unliquidated?

   a. Respecting an educational loan in IBR, "It is the possibility of forgiveness that is contingent, not the debt itself." *In re Pratola,* 578 BR 414, 420 (Bankr.ND Ill. 2017), *rev'd on other grounds, Stearn v. Pratola (In re Pratola),* 2018 W.L. 4181498 (N.D.Ill. Aug. 31, 2018)

3. Could a parent guarantee on a child's student loan be contingent? Unliquidated?

4. § 109(e) is about Eligibility for chapter 13… not jurisdictional.

   a. *In re Zarnel,* 619 F.3d 156 (2d Cir.2010)

      i. "…we find that the restrictions of § 301 and § 109(h) are not jurisdictional, but rather elements that must be established to sustain a voluntary bankruptcy proceeding. **Restricting whether an individual may be a debtor either under the Bankruptcy Code in general or under a given chapter does not speak in jurisdictional terms or invoke the jurisdiction of the district court**, delineated in 28 U.S.C. §1344 as discussed above. Certainly, consideration of these limitations after other decisions on the merits have taken place would be wasteful and unfair…." *Zarnel,* 619 F.3d at 169 (emphasis added)

5. Must court dismiss case where education loans push debt over §109(e) limits?

    a. No statutory penalty for violation; Not a stated grounds for dismissal in 1307

        i. But 1307 list is illustrative, not exhaustive

        ii. Dismissal is discretionary

            1. In interest of creditors? Isn't some payment, in a court-monitored program, better than none?

            2. Does dismissal serve purposes of chapter 13?

            3. Does dismissal lead to an absurd result—forcing a strictly consumer debtor into ch. 11 where overwhelming administrative expense will sap the small estate, and confirmation may be impossible with an overwhelming DOE debt?

        iii. See the discussion in bankruptcy decision of *In re Pratola,* 578 BR 414 (Bankr.ND Ill. 2017); however, the decision was reversed by the District Court August 31: *Stearn v. Pratola (In re Pratola),* 2018 W.L. 4181498 (N.D.Ill. Aug. 31, 2018)

            1. *Case summary:* Trustee requests dismissal of chapter 13 case where unsecured debt exceeds §109(e) limit of $394,725. Debtor scheduled student loans of $569,000 and credit cards of $22,000. The bankruptcy court cites legislative history showing §109 debt limits were enacted to keep debtors with large business debt from filing chapter 13 with its more limited creditor rights compared to those allowed creditors in chapter 11. Where debt limit is exceeded due to educational loans, dismissal will not advance the

rationale for debt limits. The bankruptcy court allowed the chapter 13 to proceed despite the excess of debt. The District Court, however, overturns, addressing each argument of bankruptcy court, and holds that failure to dismiss chapter 13 case with student loan debt in excess of §109(e) limit is abuse of discretion.

b. 3 cases cite the *Pratola* Bankruptcy Court decision prior to reversal:

   i. *In re Fishel*, 583 BR 474 (Bankr. WD Wis. 2018) is the only case presently citing the *Pratola* bankruptcy court decision with approval. *Fishel* court also notes lack of clarity as to the amount of student loans. Court exercises discretion to allow case to proceed.

   ii. *In re Petty*, 2018 WL 1956187 (Bankr. ED Tex. 2018) "…student loan debts must be included in the calculation of noncontingent, liquidated, unsecured debts for purposes of determining §109(e) eligibility. Further, the plain terms of the Bankruptcy Code preclude the debtors from continuing in a chapter 13 and obtaining relief for which they are ineligible." *Petty* at *2.

   iii. *In re Bailey-Pfeiffer*, 2018 WL 1896307 (Bankr. WD Wis.) "The soundest policy arguments do not trump the statutory language,…the plain terms of the Code…preclude the court from allowing a person who is ineligible to be a chapter 13 debtor from continuing in chapter 13." *Bailey-Pfeiffer* at *4.

IV. Discharging Student Loans

A. Section 1328(a) does not include debt "of the kind specified in" § 523(a)(8)

B. Section 523(a)(8)—Debt for "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 any other" qualified educational loan" per IRC §221(d) shall not be dischargeable "unless excepting such debt from discharge…would impose an undue hardship on the debtor and the debtor's dependents…."

   1. IRC § 221(d)(1) Qualified education loan. --The term "qualified education loan" means any indebtedness incurred by the taxpayer solely to pay qualified higher education expenses—
      a. which are incurred on behalf of the taxpayer, the taxpayer's spouse, or any dependent of the taxpayer as of the time the indebtedness was incurred,
      b. which are paid or incurred within a reasonable period of time before or after the indebtedness is incurred, and
      c. which are attributable to education furnished during a period during which the recipient was an eligible student.
   2. Such term includes indebtedness used to refinance indebtedness which qualifies as a qualified education loan. 26 U.S.C. §221(d)

C. Student loans cannot be discharged by declaration in plan. *United Student Aid Funds, Inc. v. Espinosa*, 130 S.Ct. 1367 (2010), but *Espinosa* clearly assumes a chapter 13 debtor is empowered to bring adversary proceedings to determine dischargeability of an education debt. *Id.* at 1378; *See also*, *Matter of Ottaviano*, 68 B.R. 238, 240 (Bankr. D. Conn. 1986)(Krechevsky, B.J.)(Chapter 13 debtor can bring avoidance action under Ottaviano,

though a matter subject to later dispute in other jurisdictions, *See,e.g., In re Ryker*, 315 B.R. 664 (Bankr. D. NJ 2004).

D. The timing of adjudication of the complaint—at the commencement of the chapter 13 or upon completion of plan payments—may be subject to disagreement. *See, e.g*., *In re Pair*, 269 B.R. 719, 721 (Bankr. N.D. Ala. 2001).

E. 2nd Circuit Brunner standard for determination of "undue hardship"—*Brunner v. New York State Higher Educ. Services Corp*., 831 F.2d 395 (1987)[applied by most of country]—requires 3-part showing:

    1. Based on current income and expenses debtor cannot maintain a "'minimal' standard of living" for self and dependents if forced to repay the student loans,
    2. "Additional circumstances" indicate the inability to maintain minimal standard of living "is likely to persist for a significant portion of the repayment period of the student loans" AND
    3. "Debtor has made good faith efforts to repay the loans."

F. 1st and 8th Circuits' Totality of the Circumstances standard—Undue hardship found where debtor cannot maintain a minimal standard of living AND pay the student loans based on

    1. Debtor's past, present, and reasonably reliable future financial resources,
    2. Debtor's and dependents' reasonably necessary living expenses, and
    3. Other relevant facts or circumstances unique to the case.
    4. *Long v. Educ. Credit Mgmt. Corp. (In re Long),* 322 F.3d 549, 554 (8th Cir. 2003); *In re Bronsdon* 435 B.R. 791, 798 (B.A.P. 1st Cir 2010). In other words, "Can the debtor now and in the foreseeable future, maintain a

reasonable, minimal standard of living for the debtor and the debtor's dependents and still afford to make payments on the debtor's student loans?" *Hicks v. Educ. Credit Mgmt. Corp. (In re Hicks),* 331 B.R. 18, 31 (Bankr. D. Mass. 2005).

G. Does *Brunner* set the bar too high?

1. "Requiring the debtor present additional evidence of 'unique' or 'extraordinary circumstances amounting to a 'certainty of hopelessness' is not supported by the text of §523(a)(8)." *Hicks,* 331 B.R. at 27-28
2. Requirement of good faith is "without textual foundation." *Id.*
3. The party opposing the discharge should have the burden of proving bad faith, not the debtor. *Bronsdon,* 435 B.R. at 800.

H. Determination of student loan dischargeability in chapter 13 proceeding

1. *United Student Aid Funds, Inc. v. Espinosa,* 559 U.S. 260 130 S.Ct. 1367 (US 2010)
2. *Educational Credit Management Corp v Buchanan*, 276 B.R. 744 (N.D.W.Va.2002) (Debtor fails to meet Brunner test burden of proof in adversary proceeding to freeze student loan interest during 5-year period of chapter 13 proceeding.)
3. Partial Discharge? *See, In re Miller,* 377 F.3d 616, 621-22 (6th Cir. 2004)(chapter 7 proceeding. "…we stress that the requirement of undue hardship must always apply to the discharge of student loans in bankruptcy-regardless of whether a court is discharging a debtor's student loans in full or only partially."); *In re Pair* 269 B.R. 719(Bankr. N.D. Ala. 2001).

Date :___________

Client's name: _________________

Case No._____________________

Calculation for Disposable Income Pursuant to
Section 1325 (b)(2): Below Median Income Debtors

		Amounts
(1)	Income: CMI (Sec.101(10A) and Line 14 Form 122C of means test)	$_______________
	Less:	
	(i) Child Support payments received b(2)	$_______________
	(ii) Foster Care received b(2)	$_______________
	(iii) Non-Social Security Disability payments for dependant b(2)	$_______________
	(iv) Self-employment expenses b(2)(B) *(Do not double count these expenses. They have already been deducted from calculations performed on 122C)	$_______________
	(v) Payroll expenses from wages per 6 month Means Test (less 401(k))	$_______________
	Adjusted CMI amount	$_______________
	Plus over withholding	$_______________
(2)	Adjusted CMI from above:	$________________
	Less:	
	(i) DSO becoming due post-petition b(2)(A)(i)	$________________
	(ii) Charitable contributions not exceed 15% per annum b(2)(A)(ii)	$________________
	(iii) Schedule J Expenses with 36 month Plan payment added for secured, priority and Trustee commission. b(2)(A)(i) (less charitable deductions)	$________________
	(vi) 401(k)loan repayment (see: 1322(f) and 362(b)(19))	$________________
	(vii) 401(k) or other qualified plan contributions (Section 541(b)7))	$________________

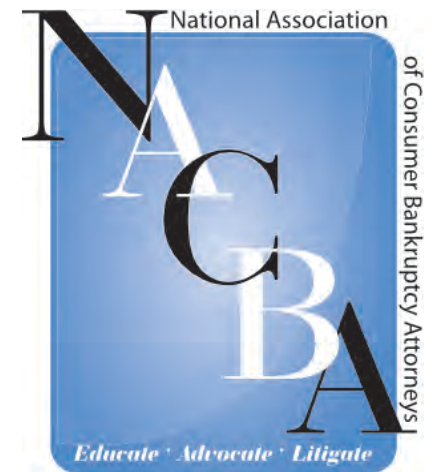
(3) Result = Total Disposable Monthly Income (TDMI) for Section 1325 (b)(2) $__________________

(4) TDMI x 36 month ACP = Total Disposable Income for Applicable Commitment Period. $__________________

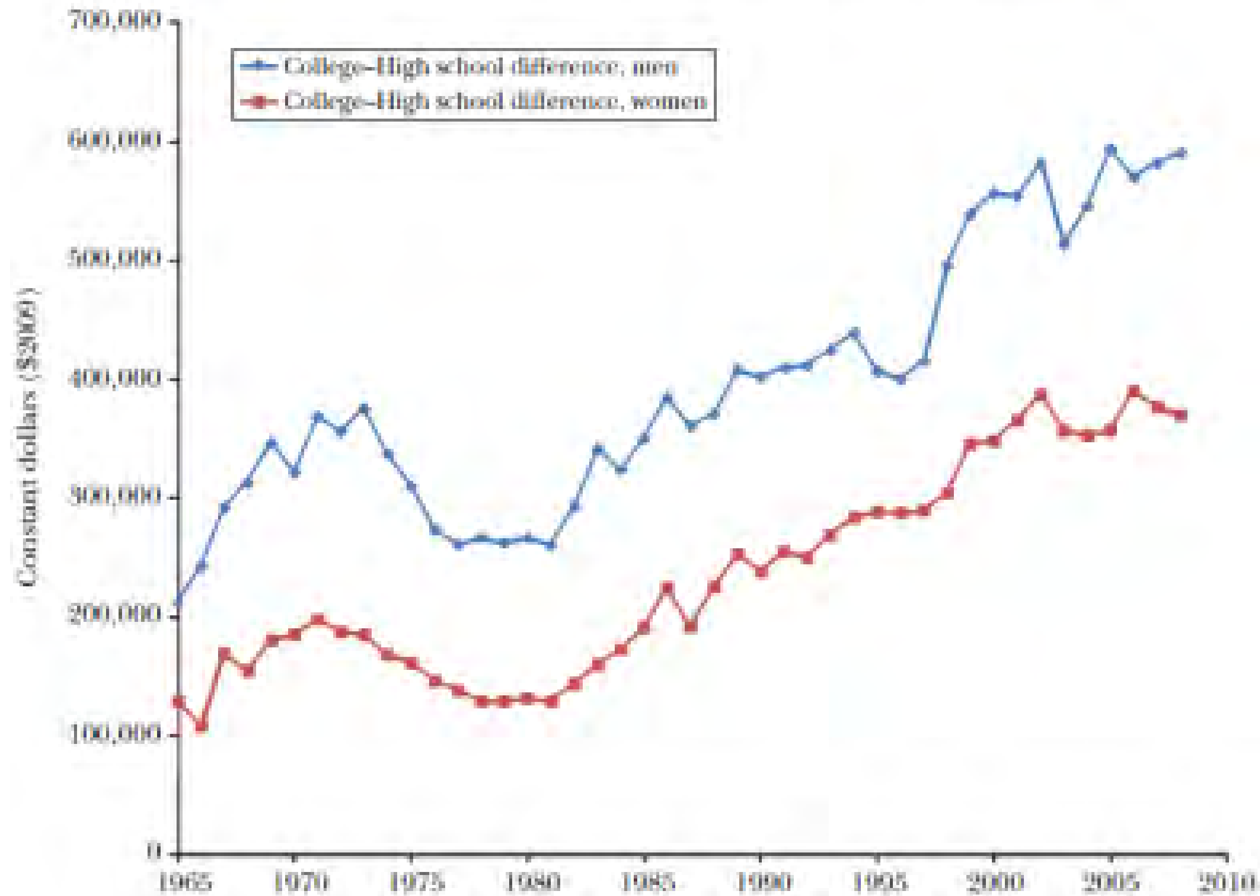
(5) TDMI from Schedule J x 36 month ACP available for allowed unsecured claims Sec. 1325(b) (1)
*Do not include excluded CMI types $___________________

Student Loans in Chapter 13

Eugene S. Melchionne
Waterbury, CT



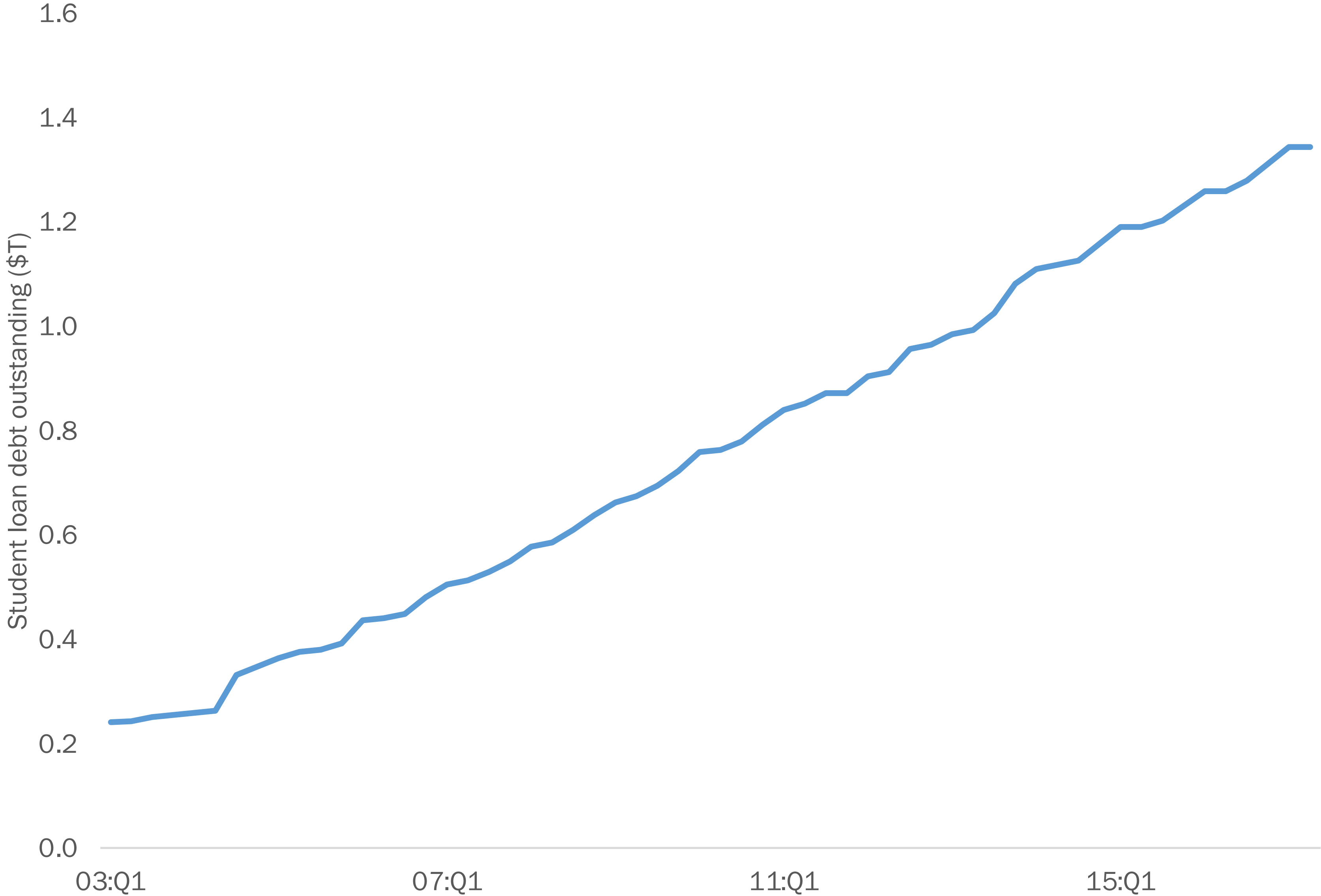
College is (still) a great investment for the average student



- But college comes with risk
- Returns differ across students, schools, and majors

Source: Avery & Turner (2012).

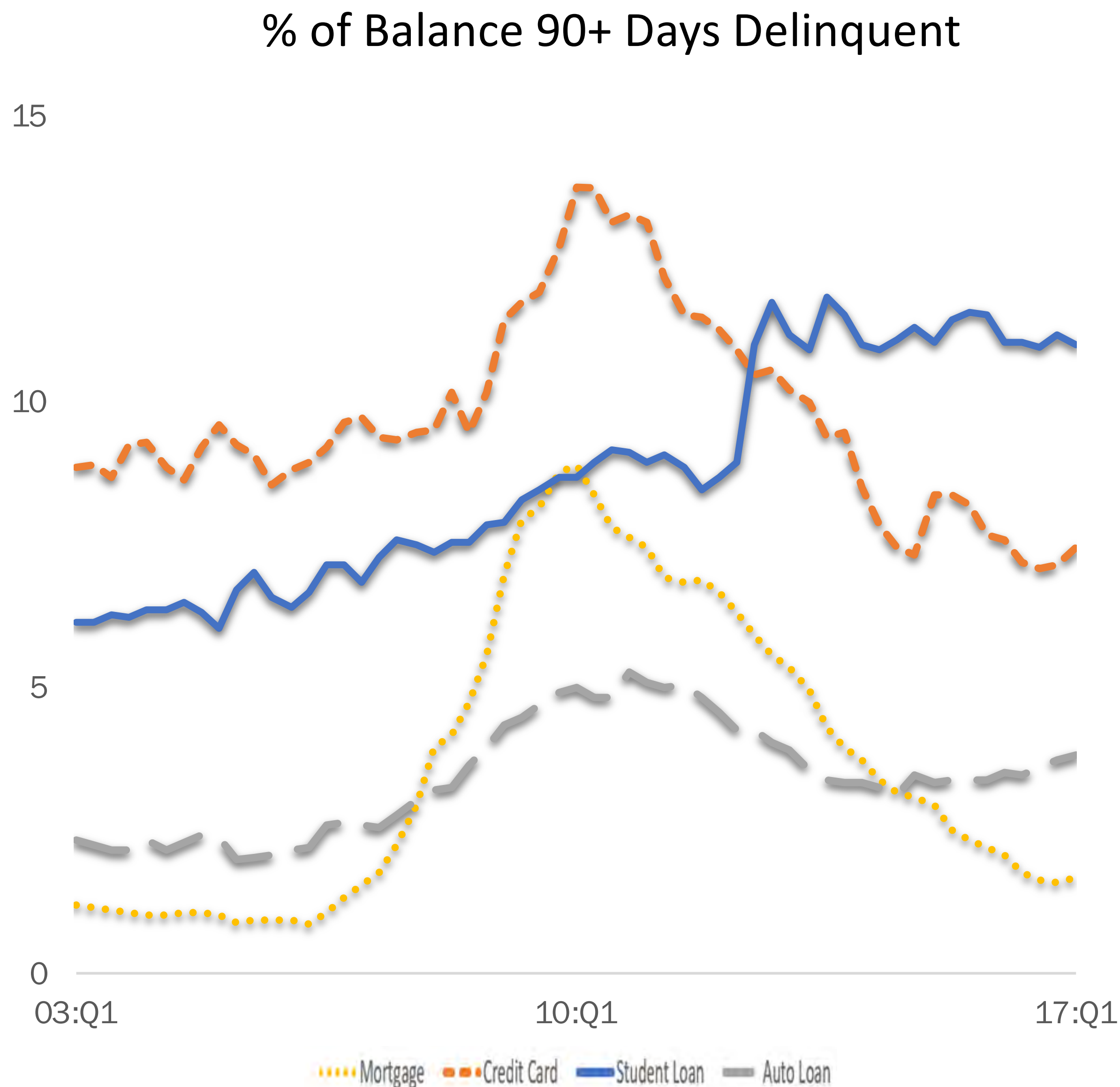
Student loan debt outstanding is on the rise



Sources: New York Fed Consumer Credit Panel/Equifax 2017Q1.

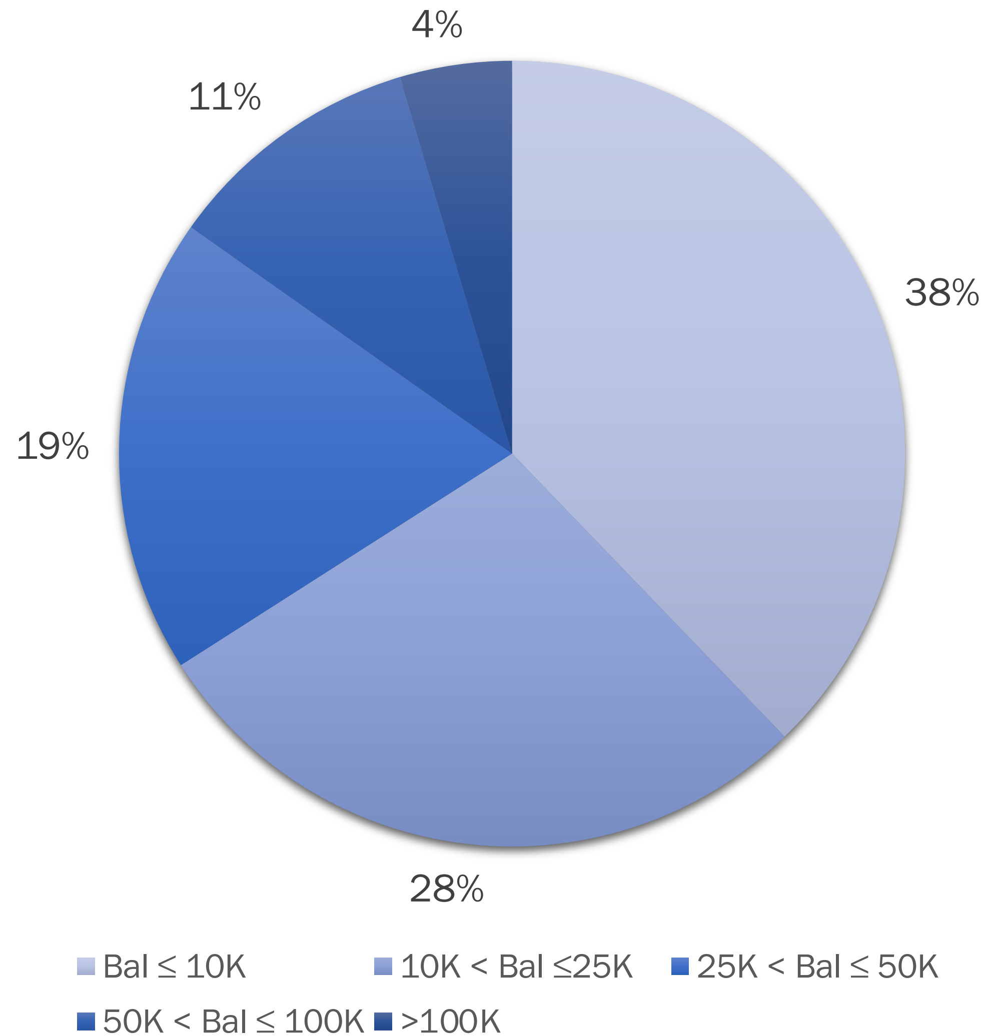
Repayment is the key student loan issue

- Default is costly to the debtor
- Default is costly to the lender & servicer
- Default is costly to taxpayers



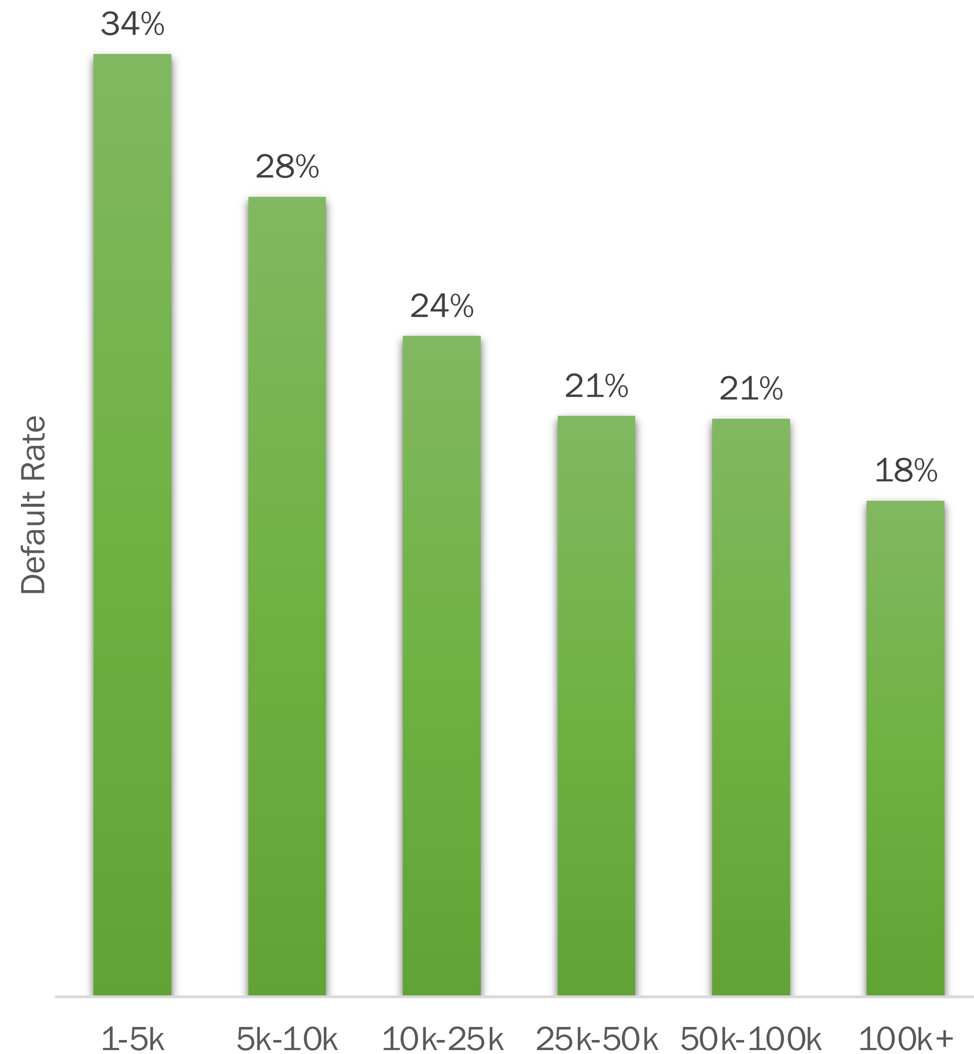
Source: New York Fed Consumer Credit Panel/Equifax 2017Q1.

>95% of student loan debtors have <$100K student loan debt



Source: New York Fed Consumer Credit Panel/Equifax .

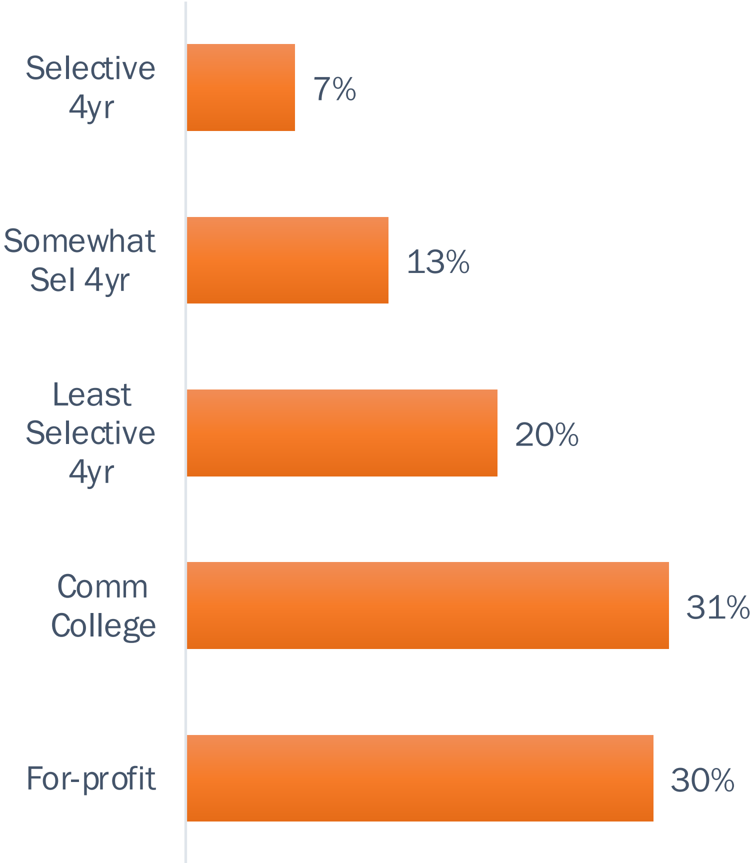
Debtors with <$5K debt nearly 2X more likely to default than those with >$100K debt



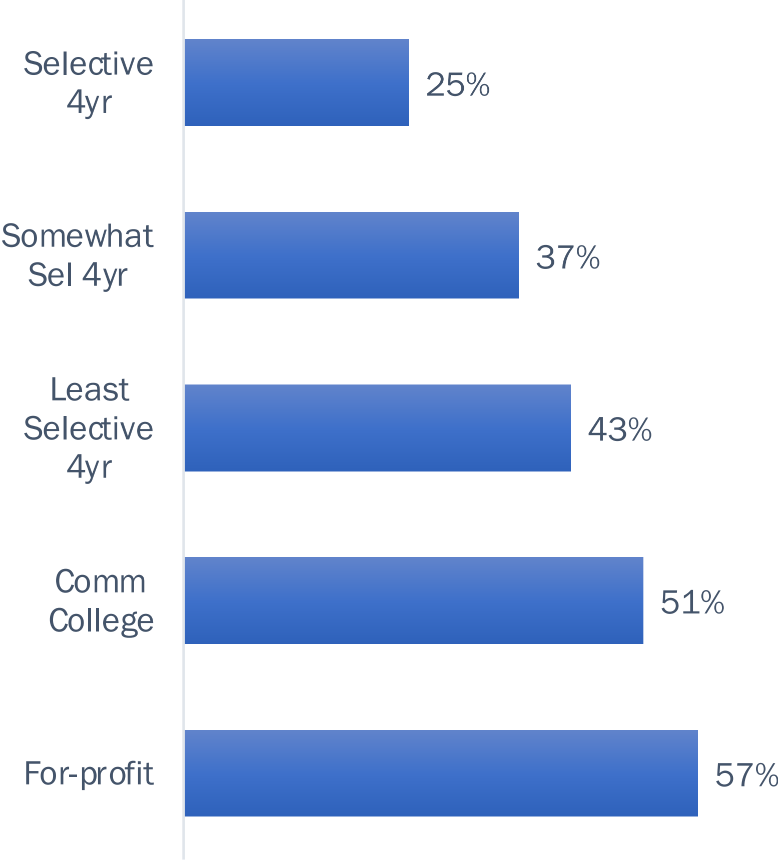
Note: Share of borrowers entering repayment in 2009 who had every defaulted by 2014. Debt based on balance upon leaving school. Source: New York Fed Consumer Credit Panel/Equifax.

Default & student characteristics vary by college

Default rates



% first generation students



Note: 3 year cohort default rates for 2011 cohort. % first-generation is 2011 cohort. Source: National Student Loan Data System data from Looney & Yannelis (2015).

Why Separately Classify?

- Reasons for classifying student loan debts separately from other unsecured creditors:
  - Stay current on income driven repayment plans (IBR, PAYE, etc.)
  - Give debtor better chance at fresh start by maximizing payment toward non-dischargeable student loans
  - Avoid accrual of postpetition interest
- Alternative: file "chapter 20?"

Separate Classification

§ 1322. Contents of plan

* * *

(b) Subject to subsections (a) and (c) of this section, the plan may—

(1) designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated; …

The Courts Weigh In

- Legal standard: *In re* Leser, 939 F.3d 669 (8th Cir. 1991)
- First Circuit B.A.P. (*In re* Bentley):
  - "… we understand '**discriminate**' to have no pejorative connotation here … treatment need only be different"
  - "'**fair**' in the abstract is too indefinite, and therefore prohibitively difficult, to define and apply…"
- Confusing multi-part tests often provide little guidance on what is a confirmable plan
- Courts reconsidering tests in student loan context
  - *In re* Kindle, 580 B.R. 443(Bankr. D. S.C. 2017)
  - *In re* Belton, 2016 WL 7011570 (Bankr. D. S.C. Oct. 13, 2016)
  - *In re* Engen, 561 B.R. 523 (Bankr. D. Kan. 2016)

Can You Treat as Long-Term Debt?

- Is classification for long-term debt under § 1322(b)(5) subject to unfair discrimination test under § 1322(b)(1)?
- What is the impact of the BAPCPA amendment in § 1322(b)(10)?

How About Using Excess Projected Disposable Income?

- Separate classification where funds used for direct payment to student loan creditors are in excess of projected disposable income
  - Above-median debtor pays student loan from "discretionary" income earned in excess of PDI
  - Below-median debtor extends plan to five years

IDR in Chapter 13 Cases

- How to incorporate an Income-Driven Repayment Plans (IDR) into Chapter 13 plans?
- Executive Office for U.S. Attorneys and Dept. of Education have developed template with standard plan language that can be added to Chapter 13 plans or submitted as an agreed order.
- If plan confirmed, the plan language or agreed order permits debtors who are not in default to remain on or enroll in an IDR.

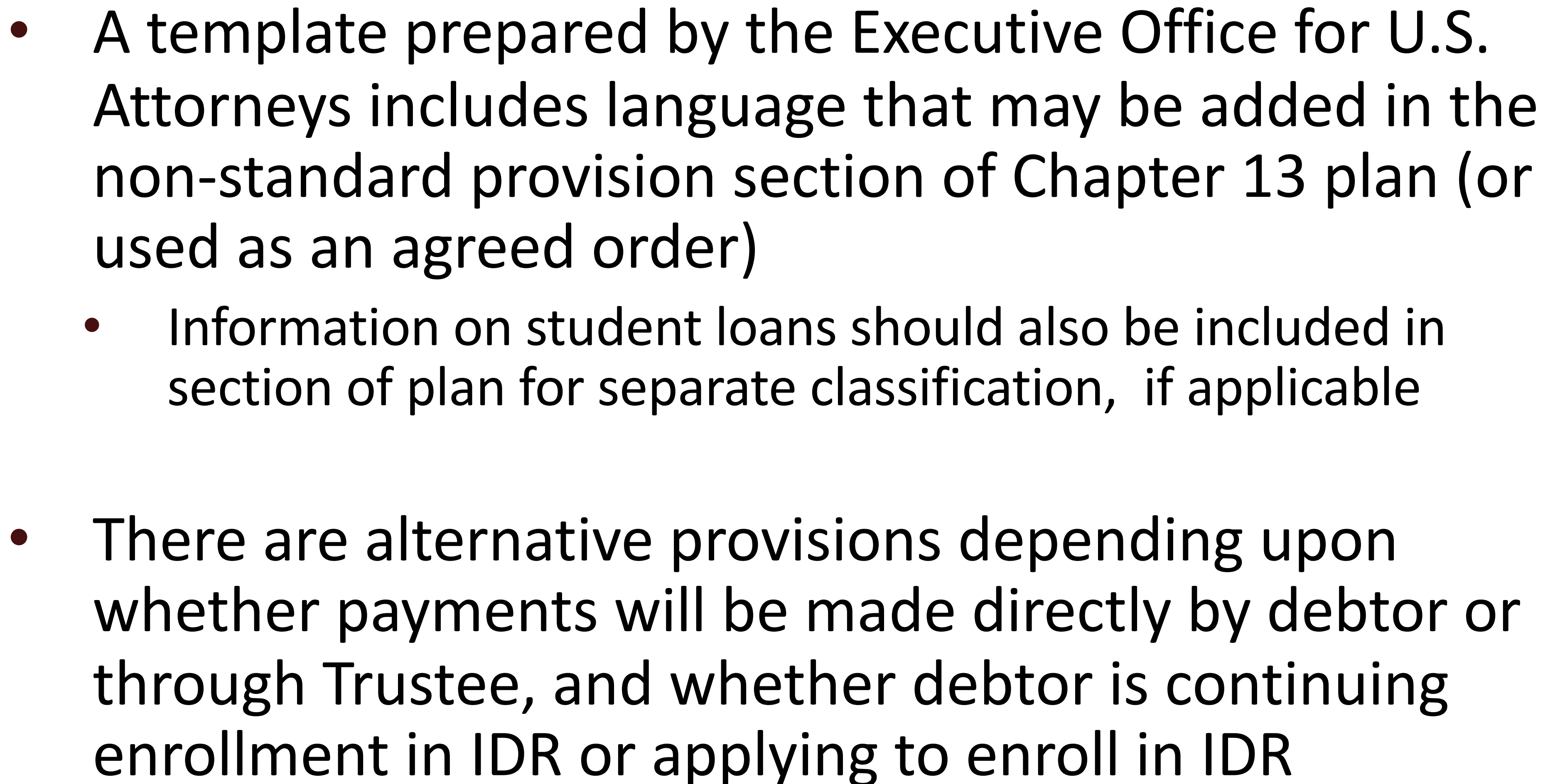
First Steps: Get Information

- Information about debtor's federal student loans is available on National Student Loan Data System (NSLDS), at www.nslds.ed.gov.
  - To access student loan in NSLDS, debtors must use their FSA ID.
  - Debtor may use the "MyStudentDataDownload" button within NSLDS to download their data into a plain text, readable file.
- Debtors can access information about repayment options on the Federal Student Aid website, www.studentaid.gov.
- Attorneys can also use ED's online calculator, the "Repayment Estimator," at: https://studentaid.ed.gov/sa/repay-loans.

First Steps: Get Out of Default

- Determine if loans are in default by having debtor check NSLDS
- If in default, debtor should pursue loan rehabilitation or consolidation before filing Chapter 13 case
- This may depend upon types of student loans, whether debtor is subject to administrative garnishment, or whether debtor has previously rehabilitated or consolidated loans

IDR Chapter 13 Standard Language



IDR Chapter 13 Standard Language

- Standard language in the template addresses following topics:
  - Identification of federal student loans;
  - Filing of proof of claim;
  - Payment disbursement (trustee or debtor)
  - Timing of payments, pre- and post-confirmation;
  - Notifications to trustee and court
  - Annual recertification of IDR
  - Discontinuance of IDR participation
  - Application of automatic stay

IDR After Chapter 7

- While Chapter 7 case is pending, debtor's student loans will be placed in forbearance even if debtor is enrolled in IDR and not in default.

- In order to ensure payments will be counted towards time period for forgiveness, debtor will need to re-enroll in IDR after a Chapter 7 discharge.

What about Private Student Loans?

- Private student loans are subject to claim objections based on statute of limitations and standing defenses
- Private student loans must satisfy test under section 523(a)(8)(B) to be nondischargeable
  - 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.

UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF SOUTH CAROLINA

IN RE: LaDeidra Antoinette Berry, Debtor(s).	C/A No. 16-01460-JW Chapter 13 **ORDER**

This matter comes before the Court upon the Motion to Determine Award of Attorney's Fees and Application for Fees Pursuant to the Equal Access to Justice Act ("Motion") filed by LaDeidra Antoinette Berry ("Debtor"), which seeks an award of attorney's fees and costs under 11 U.S.C. § 105 and the Equal Access to Justice Act.[1] Pennsylvania Higher Education Assistance Agency d/b/a FedLoan Servicing ("FedLoan Servicing") filed a response to the Motion, and a hearing was held on the matter.[2] The Court has jurisdiction of this matter pursuant to 28 U.S.C. §§ 157 and 1334. Pursuant to Fed. R. Civ. P. 52, which is made applicable to this matter pursuant to Fed. R. Bankr. P. 7052 and 9014(c), the Court makes the following findings of fact and conclusions of law.[3]

FINDINGS OF FACT

1. Debtor is obligated on a student loan ("Debtor's Loan") held by the United States Department of Education ("DOE") and serviced by its agent FedLoan Servicing.

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[1] Further references to the United State Bankruptcy Code (11 U.S.C. § 101, *et al.*) shall be by section number only.

[2] Despite being named as a party, the United States Department of Education (the "DOE") did not file an objection to the Motion.

[3] To the extent the following findings of fact are conclusions of law, they are adopted as such, and to the extent the following conclusions of law are findings of fact, they are so adopted.

2. In order to pay Debtor's Loan, prior to filing the above-captioned case, and continuing at times post-petition, Debtor was enrolled in both the Public Service Loan Forgiveness Program ("PSLF Program"), which allow a borrower employed full-time in a public service position to obtain forgiveness of student loan debt after making 120 monthly payments, and an income-driven repayment plan ("IDR"), which permits a student loan borrower to make payments in amounts based on the income earned by the borrower.[4]

3. On March 25, 2016, Debtor filed a petition for relief under Chapter 13 of the Bankruptcy Code.

4. Upon receiving notice of Debtor's bankruptcy case, FedLoan Servicing placed Debtor's Loan in an administrative forbearance. Upon placing the loan in forbearance, FedLoan Servicing stopped collection efforts against Debtor, and discontinued applying Debtor's payments in accordance with the PSLF Program or her IDR plan.

5. On March 25, 2016, Debtor proposed a chapter 13 plan ("First Plan"), which provided the following treatment for Debtor's Loan:

> F. Student Loan Claims: As indicated on Schedule J, the Debtor will pay this creditor directly, this creditor will not share in pro rata distribution from the Trustee: Fed Loan Servicing. If this claim is filed by any other entity or account number: Debtor will be responsible to notify the Trustee or Trustee may make disbursement on the claim pursuant to IV.E. above.
>
> Debtor agrees that if she signs a certification of plan completion, she will be certifying that all contractual payments that came due to this creditor have been made through the date of certification.

(Emphasis added). Through this provision, it appears Debtor intended to maintain and continue her contractual student loan payments to FedLoan Servicing through direct payments and under

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[4] The Court observes that the parties interchangeably use the term "income-based repayment plan" ("IBR") with the term "income-driven repayment plan." It is the Court's understanding that Debtor was enrolled in an IBR plan, which is a type of IDR plan.

the programs under which she had qualified and was performing at the time of the filing of her petition and the First Plan.

6. Debtor served the First Plan on FedLoan Servicing at PO Box 69184, Harrisburg, PA, 17106-9184, which is the same post office box that was indicated for notices in the proof of claim filed by FedLoan Servicing in this case.

7. After no objections were filed, the Court entered an Order Confirming the First Plan on May 9, 2016.

8. On June 14, 2016, FedLoan Servicing filed a proof of claim on behalf of the DOE, indicating that Debtor owed $97,009.87 on Debtor's Loan. The proof of claim indicated all notices and payments during the bankruptcy case should be sent to FedLoan Servicing.[5]

9. On July 27, 2016 and August 30, 2016, FedLoan Servicing responded by letters to concerns raised by Debtor's counsel that FedLoan Servicing was not complying with the terms of the confirmed First Plan, including timely crediting Debtor's payments towards the PSLF program and IDR plan.[6] The letter states the following in response to Debtor's inquiries:

> [Debtor's] request, as we understand it, is for information pertaining to the Public Service Loan Forgiveness (PSLF) program. Unfortunately, until we receive notice from the courts that the bankruptcy has concluded, her loans will not be eligible for the PSLF program. Per the Department's guidelines, qualifying payments must be made for the full scheduled monthly installment amount on an Income Driven Repayment Plan, a 10 year Standard Repayment Plan, or another Direct Loan Program repayment plan with an amount equal to that of a 10 year Standard Repayment Plan.
>
> Due to the active bankruptcy, Ms. Berry is not being billed for a monthly installment. Any payments made would be at her sole discretion and would not be a result of a required scheduled payment. Therefore, under the criteria from the Department, these payments would not count as qualifying payments. Once the

[5] The proof of claim indicated that notices should be sent to "U.S. Department of Education c/o FedLoan Servicing" at P.O. Box 69184, Harrisburg, PA 17106-9184.

[6] The August 30, 2016 letter was submitted into evidence by Debtor without objection.

bankruptcy concludes and billing resumes, Ms. Berry could continue to make qualifying payments.

10. In response, Debtor filed an amended plan on October 3, 2016 ("Second Plan"),[7] which provided the following treatment for Debtor's Loan:[8]

> F. Student Loan Claims: As indicated on Schedule J, the Debtor will pay this creditor directly; this creditor will not share in the pro rata distribution from the Trustee: FedLoan Servicing. If this claim is filed by any other entity or account number, Debtor will be responsible to notify the Trustee or Trustee may make disbursements on the claim pursuant to IV.E. above.
> Debtor agrees that if she signs a certification of plan completion, she will be certifying that all contractual payments that came due to this creditor have been made through the date of certification.
>
> The Debtor is not seeking nor does this Plan provide for any discharge, in whole or in part of her student loan obligations.
>
> *The Debtor shall be allowed to seek enrollment, or to maintain any pre-petition enrollment, in any applicable income-driven repayment ("IDR") plan with the U.S. Department of Education and/or other student loan servicers, guarantors, etc. (Collectively referred to hereafter as "Ed"), including but not limited to the Public Service Loan Forgiveness program, without disqualification due to her bankruptcy. Any direct payments made to the Debtor to Ed since the filing of her petition shall be applied to any IDR plan in which the Debtor was enrolled pre-petition, including but not limited to the Public Service Loan Forgiveness program.*
>
> Ed shall not be required to allow enrollment in any IDR unless the Debtor otherwise qualifies for such plan.
>
> The Debtor may, if necessary and desired, seek a consolidation of her student loans by separate motion and subject to subsequent court order.
>
> Upon determination by Ed of her qualification for enrollment in an IDR and calculation of any payment required under such by the Debtor, the Debtor shall, within 30 days, notify the Chapter 13 Trustee of the amount of such payment. At such time, the Trustee or the Debtor may, if necessary, file a Motion to Modify the

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[7] The Second Plan included a coversheet which indicated, in bold font, the changes made to the First Plan, including "Amended to include additional language regarding the Debtor's student loan claims in Section IV.F."

[8] According to § 1329(b)(2), a confirmed plan may be modified and the plan as modified becomes the plan, unless the modification is disapproved. Therefore, for the purposes of this Order, the First Plan and Second Plan may be collectively referred to as the "Plan."

> Chapter 13 Plan to allow such direct payment of the student loan(s) and adjust the payment to other general unsecured claims as necessary to avoid any unfair discrimination.
>
> *The Debtor shall re-enroll in the applicable IDR annually or as otherwise required and shall, within 30 days following a determination of her updated payment, notify the Chapter 13 Trustee of such payment.* At such time, the Trustee or the Debtor, may if necessary file a Motion to Modify the Chapter 13 Plan to allow such direct payment of the student loan(s) and adjust the payment to other general unsecured claims as necessary to avoid any unfair discrimination.
>
> *During the pendency of any application by the Debtor to consolidate her student loans, to enroll in an IDR, direct payment of her student loans under an IDR, or during the pendency of any default in payment of the student loans under an IDR, it shall not be a violation of the stay or other State or Federal Laws for Ed to send the Debtor normal monthly statements regarding payments due and other communications including, without limitation, notices of late payments or delinquency. These communications may expressly include telephone calls and e-mails.*
>
> In the event of any direct payments that are more than 30 days delinquent, the Debtor shall notify her attorney, who will in turn notify the Chapter 13 Trustee, and such parties will take appropriate action to rectify the delinquency.
>
> The Debtor's attorney may seek additional compensation by separate applications and court order for services provided in connection with the enrollment and performance under an IDR.

(Emphasis added). It appears this plan provision was intended to more definitely describe Debtor's proposed treatment of Debtor's Loan to maintain her prepetition enrollment in the IDR plan and PSLF program via direct payments to FedLoan Servicing, as well as to permit her to apply for and requalify each year for those programs. It further provided for the application of all post-petition payments made to FedLoan Servicing directly by Debtor.

11. According to its certificate of service, the Second Plan was properly served on the United States Attorney for South Carolina,[9] the DOE,[10] the United States Department of Justice,[11] and FedLoan Servicing. The address listed for FedLoan Servicing was the same address that FedLoan Servicing listed for notices on the loan's proof of claim.

12. No objections were filed to the Second Plan, and on January 20, 2017, the Court entered an Order Confirming Plan.[12]

13. Also on January 20, 2017, Debtor filed a certificate of service, which indicated that the January 20, 2017 confirmation order was served on the FedLoan Servicing on behalf of the U.S. Department of Education at the address listed for notice in the proof of claim.

14. On April 27, 2017, Debtor filed a Motion to Enforce Plan ("Motion to Enforce"), which sought to enforce the Plan against FedLoan Servicing and the DOE as payments on Debtor's Loan were still not being applied in accordance with the terms of the confirmed plan. The Motion to Enforce also sought an award of attorney's fees and costs from FedLoan Servicing and the DOE.

15. On May 22, 2017, the DOE filed an Objection to the Motion to Enforce. However, FedLoan Servicing did not file an objection to the Motion to Enforce.

16. After the filing of the Motion to Enforce, Debtor's counsel received a letter dated June 15, 2017 from American Education Services,[13] which appears to be an entity related to FedLoan Servicing. The June 15, 2017 letter stated:

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[9] Debtor served the United States Attorney for South Carolina at the Wells Fargo Building, 1441 Main Street, Suite 500, Columbia, S.C. 29201.

[10] Debtor served the U.S. Department of Education at 400 Maryland Avenue, SW, Washington D.C. 20202.

[11] Debtor served the U.S. Department of Justice at 950 Pennsylvania Avenue, NW, Washington D.C. 20530.

[12] For the purposes of this Order, the confirmation orders that confirmed the First Plan and Second Plan may be collectively referred to as the "Confirmation Order."

[13] The June 15, 2017 letter was admitted into evidence without objection.

> Because we did not receive a request for IDR recertification after receiving the [Notice of Meeting of Creditors], Ms. Berry's installment went from a Partial Financial Hardship (PFH) installment of $129.09 to a Permanent Standard installment of $897.97 on April 7, 2016. On May 24, 2017, Ms. Berry contacted our office regarding recertifying for the IDR plan. She was advised that the bankruptcy status must be ended before she may recertify her current IDR. Unfortunately, this information is not entirely accurate. Please accept our apologies for any confusion or inconvenience that this situation may have caused Ms. Berry.
>
> As long as Ms. Berry is only recertifying the current Income Based Repayment (IBR) plan, she may complete the enclosed application or recertify electronically . . . .

17. On July 14, 2017, in response to certain discovery requests made by Debtor as part of the Motion to Enforce, FedLoan Servicing filed a Motion to Quash, in Part, Subpoena of Debtor.

18. On August 29, 2017, the Court received and entered a Consent Order Resolving Motion to Enforce ("Consent Order"), which was agreed to by Debtor, FedLoan Servicing and the United States of America on behalf of the DOE. Therein, FedLoan Servicing and the DOE agreed to apply Debtor's post-petition payments to her IDR plan and the PSLF program, providing in part that "her loan balance will be recalculated accordingly including but not limited to removing any post-petition capitalization of interest" and "her payments as they were made to date will be accepted as if the payment amount due under the prior annual period continued to be in effect . . . ." The Consent Order expressly reserved Debtor's right to seek attorney's fees from the DOE and FedLoan Servicing under § 105, the Equal Access of Justice Act, and other statutes. The Consent Order also mooted FedLoan Servicing's Motion to Quash.

19. On September 28, 2017, Debtor filed the Motion seeking an award of attorney's fees and costs from FedLoan Servicing and the DOE under § 105 and the Equal Access of Justice Act for the parties' failure to comply with the terms of the confirmed Plan.

20. On October 19, 2017, FedLoan Servicing filed a response to the Motion. The DOE did not file a response to the Motion.

21. On October 23, 2017, Debtor filed correspondence with the Court indicating that she had reached a settlement with the DOE on the Motion. At the hearing on the Motion, it was indicated that the DOE agreed to pay Debtor $6,000 for her attorney's fees and costs.[14] This agreement was memorialized in a consent order entered by the Court. The consent order between Debtor and the DOE specifically provided that it constituted a full settlement between the DOE and Debtor only, and expressly recognized and preserved Debtor's right to pursue further relief against FedLoan Servicing.

22. Thereafter, the Court held a hearing on the Motion. At the hearing, Debtor sought relief under § 105.[15] At the hearing, a representative of FedLoan Servicing, Katelynn Bias, testified about Debtor's Loan and the guidelines regulating FedLoan Servicing's collection of the loan. After hearing arguments from the parties' counsels, the Court took the matter under advisement.

CONCLUSIONS OF LAW

Debtor seeks an award of attorney's fees and costs under 11 U.S.C. § 105 for FedLoan Servicing's failure to comply with the terms of the confirmed Plan. Specifically, Debtor alleges that FedLoan Servicing failed to timely and properly apply payments in accordance with the confirmed Plan and Confirmation Order, which resulted in Debtor incurring attorney's fees and costs in connection with the filing of the Motion to Enforce, related negotiations and entry of the Consent Order, and the filing and arguing of the present Motion.

Section 105(a) of the Bankruptcy Code provides that:

> The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court

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[14] This amount appears to be approximately half of the attorney's fees and costs requested by the Debtor in her Motion ($12,574.80).

[15] Debtor's arguments under the Equal Access of Justice Act were mooted because she reached a settlement with the DOE.

> from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.

Both this Court and other courts have held that an award of attorney's fees under § 105 may be appropriate when a party violates the terms of a chapter 13 plan and the court's confirmation order. See, e.g., Fla. Dep't of Rev. v. Rodriguez (In re Rodriguez), 367 F. App'x 25 (11th Cir. 2010) (upholding a bankruptcy court's finding that an award of attorney's fees was appropriate when the State of Florida violated the terms of the debtor's confirmed plan and was in contempt of the confirmation order); In re Crawford, 532 B.R. 645, 655 (Bankr. D.S.C. 2015) ("[The Court's] authority to enforce its orders, including a confirmation order, under § 105(a) must necessarily include the ability to award fees to a debtor who is forced to bring an action, and thus incur attorney's fees, to compel a creditor's compliance with the binding plan and the order confirming the plan."); In re Ford, 522 B.R. 842, 848–49 (Bankr. D.S.C. 2015) (requiring a creditor to pay debtor's attorney's fees when the creditor's conduct constituted a violation of the confirmation order); FNB Bank v. Carlton (In re Carlton), C/A No. 10-40388-JJR-13, Adv. Pro. No. 10-40054-JJR, slip op., 2011 WL 3799885 (Bankr. N.D. Ala. Aug. 26, 2011) ("A willful violation of a chapter 13 confirmation order may be contemptuous, as it was in this case, and § 105(a) provides statutory authority for a bankruptcy court to award monetary sanctions to compensate a debtor for the resulting harm, and at the court's discretion, to further award attorney's fees incurred in successfully achieving enforcement of the offended order.").

Furthermore, the Court of Appeals for the Fourth Circuit has held that through § 105(a), Congress gave bankruptcy courts the statutory authority to hold parties in contempt for failing to comply with the Court's prior orders. See Burd v. Walters (In re Walters), 868 F.2d 665, 669 (4th Cir. 1989) ("We think an order holding [Debtor's counsel] in contempt for his failure to comply

with the previous order of the court was appropriate in carrying out the administration of the estate, and thus was authorized by 11 U.S.C. § 105(a)."); Workman v. GMAC Mortgage LLC (In re Workman), 392 B.R. 189, 194 (Bankr. D.S.C. 2007) (noting that "[b]ankruptcy courts within this Circuit have previously held creditors in civil contempt for violating a confirmation and a discharge order"). The District Court of South Carolina has held that "[i]t is clear from the very terms of [§ 105(a)] that Congress gave the Bankruptcy Court broad inherent discretionary powers to ensure that the motions made and issues raised before it are managed efficiently and justly[,]" including the authority to award attorney's fees. GE Capital Mortgage v. Asbill (In re Asbill), C/A No. 3:99-0773-19, slip op. at 3–4 (D.S.C. Feb. 23, 2000).

As an initial matter, to determine if an award of attorney's fees under § 105(a) is appropriate, the Court must determine the conclusive effect of the confirmed Plan in this case.

Violations of the Confirmed Plan

Debtor alleges that FedLoan Servicing is bound by her confirmed Plan and has violated the terms of the Plan under § 1327 and the Supreme Court's holding in United Student Aid Funds, Inc. v. Espinosa, 559 U.S. 260, 130 1367, 176 L.Ed.2d 158 (2010). Section 1327 of the Bankruptcy Code provides that "[t]he provisions of a confirmed plan bind the debtor and each creditor, whether or not the claim of such creditor is provided for by the plan, and whether or not such creditor has objected to, has accepted or has rejected the plan." The Supreme Court in Espinosa held that a confirmed plan is a binding final judgment, which generally stands "'in the way of [a party] challenging [the plan's] enforceability.'" Id. at 269, 130 S. Ct. at 1376 (quoting Travelers Indemnity Co. v. Bailey, 557 U.S. 137, 140, 129 S.Ct. 2195, 2198, 174 L.Ed.2d (2009)). In Espinosa, the Supreme Court, addressing a plan that contained a legal error, determined that when there is proper service and otherwise sufficient due process, the confirmation order "remains

enforceable and binding on [the party] because the [creditor] had notice of the error and failed to object or timely appeal." Id. at 276, 129 S.Ct. at 1380. In other words, if a party was properly served with the chapter 13 plan, and that party does not object to the plan, the order confirming that plan is broadly binding on the party, regardless of whether the party agreed to that treatment and even if that treatment may otherwise constitute a legal error.

In the present matter, the Plan identifies FedLoan Servicing as the creditor or party acting for the creditor on Debtor's Loan.[16] Further, the Plan provided for Debtor to maintain her enrollment in the IDR plan and PSLF program and also provided clear instruction regarding how her loan payments should be applied. The language in the Plan regarding Debtor's Loan was clear and unequivocally applied to FedLoan Servicing. In addition, the language was highlighted to provide adequate notice of the proposed treatment of Debtor's Loan, with the applicable section header titled "Student Loans," and was the only section of the Plan that was in bold and italicized font.

The Plan was properly served on FedLoan Servicing and no party objected to confirmation.[17] The Plan was confirmed and the Confirmation Order became final as no party filed a motion to reconsider under Fed. R. Civ. P. 59 or 60 or appealed. Further, FedLoan Servicing does not dispute that it received copies of the Confirmation Order. Therefore, upon confirmation,

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[16] On Schedule J, Debtor lists "Student Loan" as one of her expenses that she will pay directly. Debtor's Schedule E/F also indicates that FedLoan Servicing is the creditor for her student loan.

[17] At the hearing on the Motion, FedLoan Servicing raised for the first time that it records do not reflect that it received a copy of the Second Plan. However, under Fed. R. Bankr. P. 9006(e), service "by mail is complete on mailing." Debtor's certificate of service for the Second Plan indicates it was served on the address indicated for notices by FedLoan Servicing in the proof of claim for Debtor's Loan. This Court has held that mailing creates a presumption of receipt, and the party who disputes receipt must demonstrate that the document was not properly mailed. See In re De Weerd, C/A No. 16-05655-JW, slip op. at 5–6 (Bankr. D.S.C. Mar. 16, 2017). FedLoan Servicing has not raised any allegations or presented any evidence that the Second Plan was not properly mailed. Therefore, the Court must conclude from the evidence that the Second Plan was properly served on FedLoan Servicing.

FedLoan Servicing was bound to the terms of the Plan pursuant to § 1327 and according to the holding in Espinosa.[18] By failing to comply with the terms of the Plan, despite notice and Debtor's demand, FedLoan Servicing was in violation and contempt of the Court's Confirmation Order.[19]

Due to FedLoan Servicing's actions, Debtor was required to file the Motion to Enforce in order to compel compliance with the terms of the Plan, which resulted in her incurring additional attorney's fees and costs. As a result of the efforts of Debtor's counsel, the Motion to Enforce was settled between the parties, with the settlement recognizing the Plan's requirements of Debtor's continuing participation in the IDR plan and the PSLF program, and the proper application of all her post-petition payments to those programs. Not only did the parties agree that Debtor's Loan be treated as required by the terms of the Plan, but, in addition, they specifically anticipated and reserved Debtor's right to seek attorney's fees and costs for violations of the Plan.[20]

It does not appear that the fees and costs associated with the Motion to Enforce and this Motion would have been incurred if FedLoan Servicing has properly complied with the Plan and Confirmation Order. Therefore, the Court finds that an award of attorney's fees and costs to the

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[18] As part of its argument at the hearing, FedLoan Servicing indicated that the Plan, on its face, violated law as it was contradictory to federal regulations regarding the servicing of student loans when the borrower has filed bankruptcy. As such, FedLoan Servicing argued that under Espinosa, the Court had a duty to not confirm the Plan, and therefore, the plan is not binding. However, the Court notes that FedLoan Servicing's own pleadings indicate that the asserted applicable regulations are conflicting, and "do not specifically identify . . . how a student loan that is subject to a pre-petition IBR plan should be administered during the course of a bankruptcy proceeding . . ." Furthermore, this Court should not be expected to know each industry's specific guidelines and regulations without it first being called to the Court's attention. Regardless, the holding in Espinosa is clear that, according to federal statute, a plan confirmed (after proper notice to the creditor and no objections filed) remains binding on the parties, even if the plan contains a legal error. Espinosa, 559 U.S. at 276, 129 S.Ct. at 1380. Therefore, this argument is without merit and overruled.

[19] The Court has also considered the factors for civil contempt as set forth by the Fourth Circuit Court of Appeals in Ashcraft v. Conoco, Inc., 218 F.3d 288 (4th Cir. 2000).

[20] It does not appear that the fees and costs associated with the Motion to Enforce would have been incurred if FedLoan Servicing had properly complied with the Confirmation Order when it was first entered.

Debtor is appropriate under § 105. While this holding concludes the issue, the Court will nonetheless consider the defenses raised by FedLoan Servicing in its objection.

FedLoan Servicing's Defenses

In its objection to the Motion and the Joint Statement of Dispute, FedLoan Servicing primarily argues two defenses for its non-compliance: (1) its contract with the DOE did not provide it with the authority to comply with the Plan and Confirmation Order, and (2) it did not act in bad faith because it was following applicable federal regulations.

Limited Authority Defense

FedLoan Servicing argues that it is only the servicer for Debtor's Loan on behalf of the DOE, and that the contract between it and the DOE limited the action it could take.[21] Specifically, FedLoan Servicing asserts that upon a borrower's bankruptcy filing, it is limited to the following actions: placing the loan in bankruptcy status (*i.e.* forbearance status, which defers collection activity), preparing a proof of claim, and providing any additional support needed to defend the loan against a bankruptcy discharge. In other words, FedLoan Servicing asserts that its non-compliance with the Plan and Confirmation Order should be excused because of its contract with and limited authorization from the DOE.

The Court disagrees.

First, the Court notes that, both prepetition and post-petition, FedLoan Servicing was designated and acted as the authorized representative of the DOE for purposes of servicing Debtor's Loan, communicating with Debtor, and managing and applying the student loan payments. It further appears from FedLoan Servicing's July 27 and August 30, 2016 letters that it made determinations, in fact incorrect determinations, regarding Debtor's qualification for her

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[21] A copy of this contract was admitted into evidence without objection.

continued enrollment in the PSFL Program and IDR Plan. It considered Debtor disqualified because of her bankruptcy filing—even though Debtor provided for continued direct payments in the confirmed Plan in an effort to keep current on her loans.[22]

A review of the contract between the DOE and FedLoan Servicing demonstrates that FedLoan Servicing's responsibilities included among other things to: (1) "respond to written and email questions and requests timely and accurately[;]" (2) "respond and resolve customer complaints; and create and execute a plan to escalate complaints to [the DOE] and the Ombudsman[;]" and (3) "provide a means for [DOE] to make a final determination on eligibility of borrowers for entitlements, such as discharge due to Closed School, Death, etc., and compromise offers." See FedLoan Servicing Ex. 1, Servicing Contract at Attachment A-2, p. 11–12.

Furthermore, a review of FedLoan Servicing's internal bankruptcy procedural guides shows that FedLoan Servicing reviews all of the bankruptcy documents filed in a case on behalf of the DOE, including both initial and amended chapter 13 plans to determine if the plan includes "any objectionable language (such as student loan dischargeability) toward [FedLoan Servicing and the DOE] . . . ."[23]

In the Court's view, the contract and guides presented by FedLoan Servicing indicates that it had sufficient authority to comply with the requirements of the Plan and Confirmation Order or ensure that the DOE provided it with the necessary authority or instruction to ensure compliance.

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[22] There may also be a substantial question whether FedLoan Servicing's action on behalf of the DOE discriminated against Debtor in violation of 11 U.S.C. § 525(a) or (c). See 4 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy ¶ 525.02 (16th ed. rev. 2016) (noting that "the list of discriminatory acts that is included in section 525(a) is not meant to be exhaustive" and indicating that "[p]erhaps the clearest and most easily detectable type of discrimination prohibited by section 525 is discrimination based upon the commencement of the bankruptcy case itself" as it "obviously frustrates the purpose of Congress to make the fresh start or reorganization benefits provided by the Code freely available to debtors who may need them").

[23] The guides provided to the Court do not outline what is objectionable language.

Regardless, upon its receipt of the Plan, if FedLoan Servicing felt unable to comply, it should have objected. It did not. Nor was there any evidence that it reported the Plan's provisions to the DOE for action. Instead, FedLoan Servicing seeks immunity due to the alleged insufficiencies in its own servicing contract and asserts that its hands were tied. To accept FedLoan Servicing's arguments would allow it and other similarly situated creditors or parties-in-interest to escape the consequences of a duly noticed confirmed plan and § 1327 by simply limiting its or its agents' responsibility. As a matter of statutory construction and public policy, such a defense cannot be accepted.[24]

Bad Faith

FedLoan Servicing also alleges that an award of attorney's fees is not appropriate because it asserts that it did not act in bad faith as it believed it was following federal regulations when it did not comply with the confirmed Plan and Confirmation Order.

As an initial matter, the Court finds that bad faith is not a requirement for the Court to take action pursuant to § 105.[25] Section 105 provides a sweeping grant of authority to "issue any order, process or judgment that is necessary or appropriate to carry out the provisions of" the Bankruptcy

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[24] When a court orders an agent of an entity to take certain actions, the agent who has notice of the court's order may be held in contempt of court if the agent violates the order. See 17 C.J.S. Contempt § 57 (Dec. 2017 update) ("It is usual, in an order directed against a corporation, to lay the restraint or command, not only on the corporation itself, but also on its officers, agents, and servants, so that in the case of its violation not only the corporation itself is amendable to punishment, but also its officers, agents and servants, whether or not parties to the proceeding, provided they have knowledge of the terms of the order and disobey it willfully.").

[25] FedLoan Servicing cites to McGahern v. 1st Citizens Bank & Trust Co. (In re Weiss), 111 F.3d 1159 (4th Cir. 1997) for support of its arugment that the Court must find bad faith prior to awarding attorney's fees under § 105. However, in Weiss, the court addresses an award of attorney's fees under its inherent authority to regulate the litigants that appear before it, not a bankruptcy court's statutory authority under § 105. See Hardee v. Mitchell (In re Hardee), C/A No. 96-1968, slip op., 1998 WL 766699 at *3 (4th Cir. Oct. 20, 1998) (unpublished) (noting that bankruptcy courts have several avenues, in addition to "the inherent power to regulate litigants' behavior," for the authority to sanction, including the court's authority under § 105(a) as recognized in In re Walters, 868 F.2d 665, 670 (4th Cir. 1989)).

Code, including ensuring that parties comply with the terms of a confirmed chapter 13 plan under § 1327(a), and is not limited to bad faith conduct.

Secondly, the regulation on which FedLoan Servicing relies, 34 C.F.R. § 682.402(f)(2), does not appear to limit FedLoan Servicing or the DOE from complying with the terms of a confirmed chapter 13 plan or otherwise insulate it from respecting the Court's orders. This section of the federal regulations indicates that "[i]f the lender is notified that a borrower has filed a petition for relief in bankruptcy, the lender must immediately suspend any collection efforts *outside* the bankruptcy proceeding against the borrower . . . ."[26] 34 C.F.R. § 682.402(f)(2) (2017) (emphasis added). First, the Court notes that direct payments made pursuant to a confirmed plan are part of the bankruptcy proceeding. See In re Dowey, C/A No. 12-02002-JW, slip op. at 8 (Bankr. D.S.C. Feb. 9, 2017) (holding that post-petition payments made directly to a mortgage creditor that were included in a chapter 13 plan were payments under the plan). Second, the plain reading of this regulation does not prevent the acceptance and application of payments pursuant to the specific terms of a confirmed chapter 13 plan.[27]

The fallacy of FedLoan Servicing's argument is demonstrated by a portion of its objection:

> An inherent conflict exists within the regulations themselves, and between the regulations and the Bankruptcy Code, that suggests that a borrower cannot be both in bankruptcy and an [IDR] repayment plan at the same time. The federal regulations regarding [IDR] do not mesh with the provisions of Chapter 13 regarding the proposal and confirmation of a Chapter 13 plan, and the regulatory agencies have not taken appropriate steps to specifically consider how [IDR] plans should be treated in bankruptcy.

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[26] It appears to the Court that the purpose of this regulation is to prevent possible violations of the automatic stay under § 362 due to affirmative demands for payment or other violation activity after a bankruptcy case is filed, rather than to indicate a policy that all student loans in which the borrower is in bankruptcy must be placed in an administrative forbearance for the entirety of the bankruptcy case, regardless of the terms of a confirmed plan.

[27] Certainly, by the filing of a proof of claim, FedLoan Servicing requested and expected payments to be made on Debtor's Loan after confirmation.

> Under Espinosa, the [] Plan is not binding on DOE because the [] Plan contained provisions that were contrary to the existing federal regulations that govern a loan such as [Debtor's] Loan that was in [IDR] pre-petition.

FedLoan Servicing Objection at 17, Oct. 19, 2017, ECF No. 56.

The language of § 1327 and the holding in Espinosa provide the opposite.[28] Furthermore, FedLoan Servicing's agreement in the Consent Order dated August 29, 2017 to allow Debtor to continue under the PSLF Program and IDR Plan from the petition date is directly contrary to this argument.

Under the circumstances of this case, it is necessary and appropriate for the Court to award Debtor's attorney's fees so as to enforce and implement its orders and to prevent an abuse of process.

Amount of Attorney's Fees and Costs

Debtor's attorneys submitted to the Court the time records in this matter, indicating attorney's fees and costs in the amount of $22,317.30. These fees include the time counsel spent contacting FedLoan Servicing to enforce the Plan and Confirmation Order through the filing of the Motion to Enforce and Motion, negotiating settlements for the motions, preparing for and attending the hearing on the Motion, and other related services. FedLoan Servicing did not challenge the amount of the Debtor's counsel's fees and costs, the rates charged or the nature and extent of services in its objection or the joint statement of dispute.[29] Based on a review of the time

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[28] In addressing a Fed. R. Civ. P. 60(b)(4) motion to void a confirmed plan, the United States Supreme Court in Espinosa emphasized the binding effect of a confirmed chapter 13 plan after notice and an opportunity to object: "Where, as here, a party is notified of a plan's contents and fails to object to confirmation of the plan before the time for appeal expires, that party has been afforded a full and fair opportunity to litigate, and the party's failure to avail itself of that opportunity will not justify Rule 60(b)(4) relief." Espinosa, 559 U.S. at 276, 130 S.Ct. at 1376.

[29] At the hearing, FedLoan Servicing briefly argued that attorney's fees should not be awarded for the failure to comply with the First Plan because the language of that plan was too general, and did not specifically mention the PSLF Program and IDR Plan. However, that argument was not made in its written objection to the Motion, nor was it set forth or preserved in the Joint Statement of Dispute filed according to Chambers Guidelines. The Chambers

records of Debtor's counsel, the Court finds that the rate of Debtor's counsel, the number of hours spent, and the costs asserted to be reasonable. In making this determination, the Court considered the guiding factors in determining a reasonable attorney's fee award under the precedent set by the Court of Appeals for the Fourth Circuit.[30] See Barber v. Kimbrell's Inc., 577 F.2d 216, 226 n.28 (4th Cir. 1978) (setting forth a twelve-factor test for the court to consider whether an attorney's fee award is reasonable).

As Debtor has reached a settlement with the DOE for payment of $6,000.00 in attorney's fees and costs in this matter, the Court finds that the award of attorney's fees and costs against

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Guidelines prohibit a party submitting a Joint Statement of Dispute from reserving the right to materially alter or supplement the Joint Statement, and binds them to the positions and disclosures contained therein.

In addition, according to the evidence presented at the hearing, it appears that FedLoan Servicing did not apply Debtor's direct payments referenced by the First Plan because it held an erroneous belief that the filing of the bankruptcy case disqualified Debtor from continuance in and qualification for the PSLF Program and IDR Plan until "the bankruptcy concludes." See Debtor Ex. 3, FedLoan Servicing Letter dated Aug. 30, 2016 at 2; Debtor Ex. 6, American Education Services Letter dated June 15, 2017 at 1.

[30] The following factors under Barber favor a finding that counsel for the Debtor's attorney's fees and costs are reasonable:

(1) The time and labor expended: This was a prolonged matter that took more than a year to resolve between the parties.
(2) The novelty and difficulty of the questions raised: This matter presented the violation of a confirmation order in the context of student loan debt, which has not been previously presented to this Court.
(3) The customary fee for like work: The Court finds that counsel for the Debtor's fee is a customary rate for litigation within a chapter 13 consumer bankruptcy case.
(4) The time limitations imposed by the circumstances: Because of the urgency to continue Debtor's enrollment in her IDR plan and PSLF Program, Debtor' counsel was under certain time limitations to seek the relief sought by the Motion to Enforce.
(5) The amount in controversy and the results obtained: Debtor's counsel was successful in obtaining the relief sought in the Motion to Enforce as reflected by the terms of the settlement between the parties.
(6) The experience, reputation and ability of the attorney: The Court finds Debtor's counsel to have significant experience and ability and an excellent reputation among the bar.
(7) Attorney's fees awarded in similar cases: In reviewing this Court's prior orders awarding attorney's fees for a creditor's violation of confirmation orders, the fees requested by Debtor's counsel are on par with the fees awarded in those matters.

As to the remaining factors, the Court finds that those factors do not weigh against the Court's finding that the attorney's fees and costs requested by Debtor's counsel are reasonable.

FedLoan Servicing should be reduced by this amount. Therefore, the Court hereby orders that FedLoan Servicing shall pay $16,317.30 in attorney's fees and costs to Debtor as a result of FedLoan Servicing 's failure to comply with the terms of the Plan and Confirmation Order.

CONCLUSION

The Court hereby orders FedLoan Servicing to pay $16,317.30 in attorney's fees and costs to Debtor. FedLoan Servicing shall make payment of this amount to Debtor's counsel and file a certification of compliance with this Order (including proof of payment) no later than 14 days after the entry of this Order.

AND IT IS SO ORDERED.

Columbia, South Carolina
February 2, 2018

FILED BY THE COURT
02/02/2018

Entered: 02/02/2018

US Bankruptcy Judge
District of South Carolina

Chapter 13 Plan Non-Standard Section Template for
Student Loan IDR Plans During Bankruptcy

For use by a debtor not in default on Federal student loans who wants to enroll in or remain in an IDR repayment plan while in a Chapter 13 bankruptcy plan.

Part 8 [or Insert Local Chapter 13 Plan Section Number] **Nonstandard Plan Provisions**

1) Student Loan Debt Non-Dischargeable
In accordance with 11 U.S.C. § 523(a)(8), this Chapter 13 plan of reorganization ("Chapter 13 Plan") cannot and does not provide for a discharge, in whole or in part, of the Debtor's federal student loan debt authorized pursuant to Title IV of the Higher Education Act of 1965, as amended ("Federal Student Loan(s)").

2) Identification of Federal Student Loan Debt

a) Only Federal Student Loans that are currently in an income-driven repayment ("IDR") plan, or which Debtor is eligible to repay under an IDR plan during the pendency of this Chapter 13 case, are listed in subsection (2)(b), below. Debtor could owe other student loan obligations. The special provisions contained in this ___ [Insert "Part 8" or Plan Section Number] of the Chapter 13 Plan only apply to the Federal Student Loans listed in subsection (2)(b), below.

b) As of [Insert date bankruptcy petition was filed], the Debtor's Federal Student Loan debt includes the following Title IV Student Loans:

Title IV Loan Holder	Date Loan Obtained	Type of Loan (Direct, FFEL, Subsidized, Unsubsidized)	Original Loan Amount

c) The Federal Student Loans identified in subsection (2)(b), above, are held by the United States Department of Education ("Education") and / or [insert here other Title IV Student Loan Holders if applicable], pursuant to Title IV of the Higher Education Act of 1965, as amended, 20 U.S.C. 1070, et seq. Hereinafter, Education and other Title IV Student Loan Holders are referred to individually and collectively as "Title IV Loan Holder."

3) Federal Student Loans not in Default
As of [Insert date bankruptcy petition was filed], the Debtor is not in default, as defined in 34 CFR 682.200(b) or 685.102, as applicable, on any Federal Student Loans listed in subsection (2)(b) of this Section.

4) Proof of Claim
The Debtor affirms that a timely proof of claim has been filed with the Bankruptcy Court for each Federal Student Loan listed in subsection (2)(b) of this Section. If a Title IV Loan Holder has not filed a proof of claim for a Federal Student Loan listed by the Debtor in subsection 2(b), the Debtor will file a proof of claim for that Federal Student Loan within fifteen (15) days in advance of the date scheduled for the §1324 confirmation hearing on this Chapter 13 Plan. Such proof of claim is subject to later amendment by the Title IV Loan Holder.

5) Continuation of Pre-Petition Federal Student Loan IDR Plan

a) During the course of this Chapter 13 bankruptcy case until its dismissal or closure, the Debtor may continue participating in the IDR plan in which the Debtor participated pre-petition and for which Debtor otherwise continues to be qualified as determined by the Title IV Loan Holder.

i) The Debtor's monthly IDR plan payment is, as of the date of Debtor's bankruptcy petition, $_______________.

ii) The Debtor's monthly IDR plan payment is due to the Title IV Loan Holder on the [Insert day of the month] day of each month.

b) Debtor's Monthly Payments for Pre-Petition IDR Plan [use if Debtor will make IDR plan payment directly to Title IV Loan Holder]

i. Until confirmation of this Chapter 13 Plan, the Debtor will make full and timely IDR plan payments directly to the Title IV Loan Holder identified in subsection (2)(b) of this Section.

ii. Following confirmation of this Chapter 13 Plan, the Debtor will make full and timely IDR plan payments directly to the Title IV Loan Holder identified in subsection (2)(b) of this Section, outside of the Debtor's scheduled plan payments to the Chapter 13 Trustee.

ALTERNATIVE Subsection 5(b) [use if Debtor will make IDR plan payment through Chapter 13 Trustee's office]

b) Debtor's Monthly Payments for Pre-Petition IDR Plan

i. Until confirmation of this Chapter 13 Plan, the Debtor will make full and timely IDR plan payments directly to the Title IV Loan Holder identified in subsection (2)(b) of this Section.

ii. In order for the Chapter 13 Trustee to transfer timely the Debtor's first post-confirmation payment on the IDR plan, the Debtor must remit that IDR plan payment to the Chapter 13 Trustee *in advance* of the first post-confirmation payment due date, and in good funds (money order, bank check, TFS payment, or payroll deduction), so as not to delay the Chapter 13 Trustee's transfer of those funds to the Title IV Loan Holder.

iii. The Title IV Loan Holder will be paid through the Chapter 13 plan as a Class _____ Creditor.

iv. Following confirmation of this Chapter 13 Plan and in addition to the Debtor's scheduled Chapter 13 Plan payment to the Chapter 13 Trustee's office, the Debtor will remit to the Chapter 13 Trustee the monthly IDR plan payment. The Chapter 13 Trustee will transfer the IDR plan payment funds to the Title IV Loan Holder.

v. The Debtor must remit each post-confirmation IDR plan payment to the Chapter 13 Trustee *in advance of the IDR payment due date*, and in good funds (money order, bank check, TFS payment, or payroll deduction), so as not to delay the Chapter 13 Trustee's transfer of the IDR plan payment to the Title IV Loan Holder.

vi. If the Debtor does not timely or fully remit sufficient funds to the Chapter 13 Trustee for Debtor's monthly IDR plan payment, the Chapter 13 Trustee is not required or responsible to transfer funds to the Title IV Loan Holder from the Debtor's general bankruptcy estate for that monthly payment. The Chapter 13 Trustee is not responsible for the Debtor's late or missing IDR plan payments caused by Debtor's failure to remit funds to the Chapter 13 Trustee for transfer of the IDR plan payment by the Chapter 13 Trustee's office.

vii. Upon request of the Chapter 13 Trustee, the Debtor will request the Title IV Loan Holder modify Debtor's monthly IDR plan payment due-date to accommodate the Chapter 13 Trustee's disbursement schedule.

viii. The Chapter 13 Trustee may request the Title IV Loan Holder establish an automated clearinghouse (ACH) account with the Chapter 13 Trustee's office for deposit of the Debtor's monthly IDR plan payment directly into the Title IV Loan Holder's account.

ALTERNATIVE Paragraph 5 (use if Debtor will apply to and enroll in an IDR plan during Debtor's Chapter 13 plan)

5) Initial Participation in an IDR Plan

a) During the course of this Chapter 13 bankruptcy case until its dismissal or closure, the Debtor may submit an application for participation in any IDR plan for which the Debtor is otherwise qualified to any Title IV Loan Holder pursuant to 34 CFR 685.208, 34 CFR 685.209, 34 CFR 685.221 or 34 CFR 682.215.

b) The Title IV Loan Holder is not required to place the Debtor in an IDR plan.

c) The Debtor will provide notice to the United States Bankruptcy Court for the __________ District of ____________ ("Bankruptcy Court") and the Chapter 13 Trustee of Debtor's application for participation in an IDR plan.

d) If the Debtor submits an application for participation in an IDR plan and the Title IV Loan Holder determines the Debtor is qualified under the standard terms for participation specified in 34 CFR 685.208, 34 CFR 685.209 34, CFR 685.221, or 34 CFR 682.215, the Title IV Loan Holder may place the Debtor in an IDR plan while this Chapter 13 case is open.

(i) If the Title IV Loan Holder places the Debtor in an IDR plan, it is expressly understood and agreed by the Debtor that the Debtor's monthly IDR plan payments will be due to the Title IV Loan Holder while this Chapter 13 case is open, and will continue to be due monthly for a set period of time that extends beyond the Bankruptcy Court's entry of a Chapter 13 discharge and / or an order closing this Chapter 13 case.

(ii) If the Title IV Loan Holder places the Debtor in an IDR plan, it is expressly understood and agreed by the Debtor that the Debtor's full IDR plan monthly payments must be received timely by the Title IV Loan Holder.

(e) Within thirty (30) days of Debtor's receipt of a notice that the Title IV Loan Holder has determined Debtor's qualification for participation in an IDR plan and calculated

Debtor's monthly IDR plan payment, the Debtor shall notify the Chapter 13 Trustee of the IDR participation and the amount of the IDR plan monthly payment. Debtor is responsible to file with the Bankruptcy Court a motion to modify the Chapter 13 Plan to permit monthly payment under the IDR plan, indicating whether the payments will be made directly by the Debtor or through the Chapter 13 Trustee's office, and adjusting the Chapter 13 plan dividends, if necessary.

(f) [Use for Direct IDR Payment to Title IV Loan Holder]
The Debtor will make full and timely IDR plan payments directly to the Title IV Loan Holder outside of the Debtor's scheduled plan payments to the Chapter 13 Trustee.

ALTERNATIVE SUBSECTION (f)
[Use for IDR Payments Inside the Chapter 13 Plan]

The Debtor will remit to the Chapter 13 Trustee the monthly IDR plan payment for the Chapter 13 Trustee to transfer to the Title IV Loan Holder.

In order for the Chapter 13 Trustee to transfer Debtor's monthly IDR plan payment to the Title IV Loan Holder timely, the Debtor must remit each IDR plan payment in full to the Chapter 13 Trustee *in advance of the IDR payment due date*, and in good funds (money order, bank check, TFS payment, or payroll deduction).

i. The Title IV Loan Holder will be paid through the Chapter 13 Plan as a Class _____ Creditor.

ii. If the Debtor does not timely or fully remit sufficient funds to the Chapter 13 Trustee for Debtor's monthly IDR plan payment, the Chapter 13 Trustee is not required or responsible to transfer funds to the Title IV Loan Holder from the Debtor's general bankruptcy estate for that monthly payment. The Chapter 13 Trustee is not responsible for the Debtor's late or missing IDR plan payments caused by Debtor's failure to remit funds to the Chapter 13 Trustee for transfer of the IDR plan payment by the Chapter 13 Trustee's office.

iii. Upon the request of the Chapter 13 Trustee, the Debtor will request the Title IV Loan Holder modify Debtor's monthly IDR plan payment due date in order to accommodate the Chapter 13 Trustee's disbursement schedule.

iv. The Chapter 13 Trustee may request the Title IV Loan Holder establish an ACH account with the Chapter 13 Trustee's office for deposit of the Debtor's monthly IDR plan payment directly into the Title IV Loan Holder's account.

6) Waivers

a. Debtor expressly acknowledges and agrees that regarding an application for initial participation and/ or continuing participation in an IDR plan while this Chapter 13 case is open, Debtor waives application of the automatic stay provisions of 11 U.S.C. § 362(a) to all loan servicing, administrative actions, and communications concerning the IDR plan by the Title IV Loan Holder, including but not limited to: determination of qualification for enrollment in an IDR plan; loan servicing; transmittal to the Debtor of monthly loan statements reflecting account balances and payments due; transmittal to the Debtor of other loan and plan documents; transmittal of correspondence (paper and electronic) to the Debtor; requests for documents or information from the Debtor; telephonic and live communications with the Debtor concerning the IDR plan application, payments, or balances due; transmittal to the Debtor of IDR participation documentation; payment information; notices of late payment due and delinquency; default prevention activities; and other administrative communications and actions concerning the Debtor's IDR plan.

b. Debtor expressly waives any and all causes of action and claims against the Title IV Loan Holder for any alleged violation of the automatic stay under 11 U.S.C. § 362(a) with regard to and in consideration of the benefits of enrollment and participation in an IDR plan.

7) Annual Certification of Income and Family Size

Pursuant to 34 CFR 685.209, 34 CFR 685.221, or 34 CFR 682.215, as applicable, the Debtor shall annually certify (or as otherwise required by the Title IV Loan Holder) the Debtor's income and family size, and shall notify the Chapter 13 Trustee of any adjustment (increase or decrease) to the Debtor's monthly IDR plan payment resulting from annual certification.

a. Debtor expressly acknowledges and agrees that while this Chapter 13 case is open, Debtor waives application of the automatic stay provisions of 11 U.S.C. § 362(a) to all loan servicing, administrative actions, communications, and determinations concerning the certification of income and family size taken or effected during and for the certification process by the Title IV Loan Holder, including but not limited to: administrative communications and actions from the Title IV Loan Holder for the purpose of initiating certification; requests for documentation from the Debtor; determination of qualification for participation; and any action or communication listed in subsection (6) above, which is incorporated herein by reference.

b. Debtor expressly waives any and all causes of action and claims against the Title IV Loan Holder for any alleged violation of the automatic stay under 11 U.S.C. § 362(a) associated with the IDR plan certification process, in consideration of the voluntary participation of and benefits to the Debtor of continued participation in an IDR plan.

c. If Debtor's annual certification of income and family size for an IDR plan results in changes to the Debtor's required monthly IDR plan payment amount, the Debtor will notify the Chapter 13 Trustee within seven (7) days of Debtor's receipt of notice from the Title IV Loan Holder of the revised monthly IDR plan payment amount. Either the Debtor or the Chapter 13 Trustee may file an 11 U.S.C. §1329(a) motion to modify this Chapter 13 plan to reflect the Debtor's revised monthly IDR plan payment.

d. If the Debtor fails to satisfy the requirements for annual certification for continued participation in the IDR plan, the Title IV Loan Holder will recalculate the monthly repayment amount according to the requirements of the IDR program.

(i) Debtor expressly acknowledges and agrees that while this Chapter 13 case is open the Title IV Loan Holder's recalculation of the Debtor's repayment amount does not violate the automatic stay provisions of 11 U.S.C. § 362(a) as set forth in subsections (6) and (8) of this Section.

(ii) Debtor expressly waives any and all causes of action and claims against the Title IV Loan Holder for any alleged violation of the automatic stay under 11 U.S.C. § 362(a) with regard to the recalculation of Debtor's Federal Student Loan repayment obligation while this Chapter 13 bankruptcy case is open.

8) <u>Discontinuation of Participation in IDR</u>

a. If during the course of this Chapter 13 case the Debtor no longer desires to participate in the IDR plan and seeks administrative forbearance status on the Federal Student Loans identified in subsection (2)(b) of this Section, the Debtor must contact the Title IV Loan Holder in writing by letter to inform the Title IV Loan Holder of this decision.

b. If during the course of this Chapter 13 case the Debtor ceases making payments on the Federal Student Loan, Debtor shall contact and inform the Title IV Loan Holder in writing by letter. Based on the Debtor's information, the Title IV Loan Holder will place the Federal Student Loan into an appropriate status, such as administrative forbearance, and will stay collection action until after this Chapter 13 case is closed.

c. If during the course of this Chapter 13 case the Debtor ceases making payments on the Federal Student Loan without notice to the Title IV Loan Holder, Debtor will incur a

delinquency and may default on the Federal Student Loan as defined in CFR 34 CFR 682.200(b) and 685.102.

i. Debtor expressly acknowledges and agrees that while this Chapter 13 case is open the Title IV Loan Holder's administrative communication and actions on the defaulted debt, which are the routine administrative processes that occur upon delinquency and default on Federal Student Loans, do not violate the automatic stay provisions of 11 U.S.C. § 362(a) as set forth in subsections (6) and (8) of this Section.

ii. The Title IV Loan Holder's administrative communication and actions do not include any form of active debt collection.

d. Debtor expressly waives any and all causes of action and claims against the Title IV Loan Holder for any alleged violation of 11 U.S.C. § 362(a) with regard to the default status of Debtor's Federal Student Loan based on Debtor's non-payment while this Chapter 13 case is open, including communications with, correspondence to, or transmittal of statements to the Debtor, and telephonic and email contact with the Debtor, concerning and resulting from Debtor's Federal Student Loan default.

9) Opportunity for Title IV Loan Holder to Cure
Debtor first shall give notice to the Title IV Loan Holder in writing by letter of any alleged action by the Title IV Loan Holder concerning the Federal Student Loans and IDR plan that is contrary to the provisions of this Section and or 11 U.S.C. § 362(a). Debtor shall not institute any action in the Bankruptcy Court against the Title IV Loan Holder under 11 U.S.C. § 362(a) and (d) until after the Title IV Loan Holder has been given a reasonable opportunity to review, and, if appropriate, correct such actions. Notices provided to the Title IV Loan Holder under this subsection must include a description or identification of the actions that Debtor alleges to be in violation of this Section of the Chapter 13 Plan and/or 11 U.S.C. § 362(a).

10) Notice
Any Notice required to be given to the Title IV Loan Holder under this Section must include the Debtors' name(s), Debtor's bankruptcy case number and Chapter 13 designation, and identification of the Federal Student Loans, and must be made in writing by letter to:

[Title IV Loan Holder Name]
c/o The United States Attorney's Office
[_____DISTRICT of ______]
[Mailing Address]

ordered by the court, **in addition to the aforementioned monies, the Debtor(s) must commit all tax refunds, beginning with tax year 2017 to the plan each year during the applicable plan period. Said refunds must immediately (upon receipt of) be turned over to the Chapter 13 Trustee, in a certified check or money order <u>(Debtor(s) should not sign their IRS Refund Check and send it to the Trustee. All money sent to the Trustee needs to be in the form of a certified check or money order)</u> made payable to Jon M. Waage, Chapter 13 Trustee, with complete information as to what tax year the refund represents and send to our payment address, at PO Box 260, Memphis TN 38101-0260. Additionally, the Debtor(s) must provide complete copies of all tax returns to the Trustee's office no later than April 15th of each year for the preceding year's taxes.**

31. The NONCONFORMING PROVISIONS of Debtors' Plan (paragraph 9) is hereby stricken. The Debtor(s) shall be permitted to pay her Federal Student Loan(s)/U.S. Department of Education Loans outside of the plan. Claim(s) 14-1 of Navient Solutions, LLC and Claim(s) 15-1 of Navient Solutions, LLC shall be allowed, however claimant shall not receive any distributions by the Chapter 13 Trustee under the confirmed plan. The Debtor(s) shall not be entitled to discharge in whole or in part of any student loans. The Debtor(s), is/are currently in an Income-Dependent Repayment Program ("IDRP"). The Debtor(s) shall continue to pay his/her Federal Student Loan(s)/U.S. Department of Education Loans pursuant to the IDRP separately and outside of the Plan without disqualification due to the bankruptcy. Federal Student Loan(s)/U.S. Department of Education Loans shall not place the student loans into a deferment or forbearance because of the filing of the Chapter 13 bankruptcy case. For so long as the student loans are paid outside of the plan, it shall not be a violation of 11 USC 362 or any other applicable law or regulation for Federal Student Loan(s)/U.S. Department of Education Loans to communicate directly with the Debtor by mail, telephone or email. In the event that a different IDRP is offered by Federal Student Loan(s)/U.S. Department of Education Loans, which offers more favorable repayment options, the Debtor(s) shall be permitted to seek participation in such IDRP without disqualification due to this bankruptcy and

without further permission of the court. Debtor(s) may recertify under the applicable IDRP annually or as otherwise required and shall within thirty (30) days following a determination of his monthly payment due pursuant to such recertification file an amended budget to reflect such change. Federal Student Loan(s)/U.S. Department of Education Loans shall not be required to enroll Debtor(s) in any IDRP unless Debtor(s) otherwise qualifies for such IDRP.

Trustee Jon M. Waage is directed to serve a copy of this order on interested parties and file a proof of service within 3 days of entry of the order.

JMW/br

THIRD-PARTY RELEASES IN CHAPTER 11 PLANS

For:

Connecticut Bar Association
Commercial Law and Bankruptcy Section

The First Annual Connecticut Bankruptcy Conference
Water's Edge Resort and Spa
1525 Boston Post Road
Westbrook, Connecticut 06498
October 4, 2018

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I. INTRODUCTION

In bankruptcy parlance, a "third-party release," sometimes called a "nondebtor release,"[1] refers to "[a] release provision in a chapter 11 plan [that] relieves the identified nondebtor parties of any liability for any claims or causes of action that third parties might hold against them."[2] Examples of the beneficiaries of such a release, the "releasees" or "released parties" as plans often refer to them, are the debtor's officers and directors, a creditors' committee and its members and professionals, a nondebtor plan proponent or plan funder, the debtor's secured lender or exit-financing lender, or others who have in some way contributed to the chapter 11 process. A related, but different type of plan release is a release by the debtor, reorganized debtor or any estate representative of claims held by the debtor against nondebtor third parties. These type of releases, which are beyond the scope of this presentation, are statutorily based upon 11 U.S.C. §1123(b)(3)(A) and are evaluated under the business judgment rule.[3]

Over the past 15 years or so, third-party releases have become a common feature of chapter 11 plans, and as aggressive and creative plan proponents have "pushed the envelope" in proposing them, the caselaw on the subject has become highly developed, although markedly fractured. Circuit courts differ, for example, on whether third-party releases are ever permissible in the absence of consent, and among those courts that permit third-party releases, a significant distinction has been drawn for analytical purposes between "consensual" and "nonconsensual" releases.

[1] *See In re Metromedia Fiber Network, Inc.,* 416 F.3d 136, 141 (2d Cir. 2005).

[2] ABI Commission to Study the Reform of Chapter 11, AMERICAN BANKRUPTCY INSTITUTE, Final Report and Recommendations, at 253.

[3] *In re DBSD North America, Inc.,* 419 B.R. 179, 217 (Bankr. S.D.N.Y. 2009), *aff'd* 2010 WL 1223109 (S.D.N.Y. Mar. 10, 2010), *aff'd in part, rev'd in part on other grounds* 627 F.3d 496 (2d Cir. 2010), *opinion issued* 634 F.3d 79 (2d Cir. 2011).

The issue with "consensual" releases centers on what is sufficient to manifest creditor consent. With nonconsensual releases, at least in those jurisdictions which hold they are permissible, the criteria used for determining whether they should be approved varies by Circuit, but for the most part, are similar.

Exculpation provisions are the first cousins of third-party releases[4] and typically limit the liability of the major constituents in a chapter 11 case for acts taken or conduct engaged in while undergoing the chapter 11 process. In general, they are less controversial and more accepted by the courts, as long as they are confined to exculpating acts or conduct related to the chapter 11 case and process and except out willful misconduct or gross negligence. The distinction between a third-party release and an exculpation provision is that "[a] release is generally a relinquishment of claims and causes of action that the debtor and third parties may have against certain nondebtor parties," whereas "[a]n exculpatory clause is more akin to limited immunity for the identified parties for conduct during the chapter 11 case."[5]

II. EXCULPATION PROVISIONS

A typical exculpation provision will protect the debtor's directors, officers, employees, advisors and professionals and an official committee's members and professionals from incurring any liability to creditors or equity security holders for any act or omission relating the chapter 11 case or process. The following is an example of an exculpation provision:[6]

[4] *In re DSDB North America, Inc.,* 419 B.R. 179, 217 (Bankr. S.D.N.Y. 2009) (finding third-party releases to be the "first cousins" of exculpation provisions), *aff'd* 2010 WL 1223109 (S.D.N.Y. Mar. 24, 2010), *aff'd in part, rev'd in part* 627 F.3d 496 (2d Cir. 2010).

[5] ABI Commission to Study the Reform of Chapter 11, AMERICAN BANKRUPTCY INSTITUTE, Final Report and Recommendations, at 250.

[6] Taken in substantial part from *In re Enron,* 326 B.R. 497, 504 (S.D.N.Y. 2005).

> None of the Debtors, the Reorganized Debtors, the Creditors' Committee, and any of their respective directors, officers, employees, members, attorneys, consultants, advisors and agents (acting in such capacity), shall have or incur any liability to any holder of a Claim or Equity Interest for any act taken or omitted to be taken in connection with and subsequent to the commencement of the Chapter 11 Cases, the formulation, preparation, dissemination, implementation, confirmation or approval of the Plan or any compromises or settlements contained therein, *provided, however,* that the foregoing provisions of this Section shall not affect the liability of any Entity that otherwise would result from any such act or omission to the extent that such act or omission is determined in a Final Order to have constituted gross negligence or willful misconduct, including, without limitation, fraud and criminal misconduct.

The Bankruptcy Court in *Enron* found that the exculpation provision in the plan was appropriately limited to qualified immunity for acts of negligence and did not relieve any party of liability for gross negligence or willful misconduct, and further found that the provision was "reasonable and customary and in the best interests of the estates," and that "without such exculpation, negotiation of a Plan in these Chapter 11 Cases would not have been possible."[7]

Exculpation provisions of this nature have been approved when they are limited "to fiduciaries who have served a debtor through a chapter 11 proceeding."[8] There is significant authority, however, that, to the extent such exculpation provisions cover third parties such as the debtor's officers, directors, employees and professionals, or other major players in a chapter 11 case and their officers, etc., they will be subject to a third-party release analysis, where their

[7] *Id.* at 501. *See also In re PWS Holding Co.,* 228 F.3d 224, 246-47 (3d Cir. 2000) (approving a similar exculpatory provision because it did not affect the liability of these parties, but rather stated the standard of liability under the Code").

[8] *In re Health Diagnostic Laboratory, Inc.,* 551 B.R. 218, 232-33 (Bankr E.D. Va. 2016) (citing authorities). *But see In re Pacific Lumber Co.,* 584 F.3d 229, 252-53 (5th Cir. 2009) (disapproving exculpation provision for debtor's officers and directors, even though it was confined to negligence occurring during the chapter 11 proceedings, but approving it for creditors' committee and its members based on qualified immunity implied by 11 U.S.C. §1103(c)).

approval must be based on "consent" or under the standards for approving non-consensual third-party releases.[9] As a moderating mechanism, the bankruptcy courts have been willing to approve a plan provision which requires third-party claims to be brought first before the bankruptcy court for a threshold inquiry as to whether they actually belong to the third party or belong to the estate, and, if determined to be the former, for the litigation to be brought, at least initially, in the bankruptcy court.[10]

Similarly, where an exculpation provision may be considered other than customary and appropriate is when it purports to exculpate third parties from prepetition acts taken or omitted in connection with a contemplated restructuring.[11] In that case, the exculpatory provision will also be analyzed and approved or disapproved as a nonconsensual third-party release.[12]

III. THIRD-PARTY RELEASES

Overview of the Law

There is no question that "[t]hird-party releases are often problematic in chapter 11 cases – seemingly prohibited entirely in some Circuits but permitted under limited circumstances in other Circuits."[13] The Second Circuit has held that both consensual and nonconsensual third-

[9] *See e.g. In re Motors Liquidation Company,* 447 B.R. 198, 220-21 (Bankr. S.D.N.Y. 2011) (examining such an exculpation provision, which was limited to postpetition events and excepted out willful misconduct or gross negligence, as a third-party release under *Metromedia); In re Adelphia Communications Corp.,* 368 B.R. 140, 267 (Bankr. S.D.N.Y. 2007) (stating that "though without question it has long been the custom in the bankruptcy community to make distinctions between releases involving pre- and postpetition conduct, I think that after *Metromedia*, limitation to postpetition events, by itself, is insufficient to justify a third-party release"), *appeal dismissed* 367 B.R. 84 (S.D.N.Y. 2007).

[10] *Motors Liquidation Company,* 447 B.R. at 221; *Adelphia,* 368 B.R. at 269.

[11] *See In re Exide Technologies*, 303 B.R. 48, 75 (Bankr. D. Del. 2003).

[12] *Id.*

[13] *In re Avanti Communications Group PLC,* 582 B.R. 603, 606 (Bankr. S.D.N.Y. Apr. 9, 2018).

party releases are within the power of a bankruptcy court to approve.[14] The Fourth, Sixth, Seventh and Eleventh Circuits have also held that third-party releases may be given consensually and, subject to more rigorous criteria, may be approved without consent.[15] On the other hand, the Fifth, Ninth, and Tenth Circuits have held that third-party releases are impermissible by virtue of 11 U.S.C. §524(e),[16] which provides, in relevant part, that "discharge of a debt of the debtor does not affect the liability of any other entity on, or the property of any other entity for, such debt." The D.C. Circuit has not explicitly approved or disapproved third-party releases, but has dismissed as moot an appeal from the District Court's ruling that the plan's release provisions, which made available a pool of $3 million to unsecured creditors if they gave a release to certain third parties, "did not constitute an impermissible discharge of … third parties, contrary to Bankruptcy Code §524(e)."[17]

The countervailing view to the Fifth, Ninth and Tenth Circuit authority is that "section 524(e) provides only that a discharge does not affect the liability of third parties. This language does not purport to limit or restrain the power of the bankruptcy court to otherwise grant a release to a third party."[18] As elucidated by Judge Gerber in *Adelphia Communications:*

[14] *In re Metromedia Fiber Network, Inc.* 416 F.3d 136, 141-42 (2d Cir. 2005).

[15] *See In re Seaside Engineering & Surveying, Inc.,* 780 F.3d 1070, 1077-78 (11th Cir. 2015); *National Heritage Foundation, Inc. v. Highbourne Foundation,* 760 F.3d 344, 347-50 (4th Cir. 2014); *In re Airadigm Communications., Inc.*, 519 F.3d 640, 655–57 (7th Cir. 2008); *In re Dow Corning Corp.*, 280 F.3d 648, 657–58 (6th Cir. 2002).

[16] *In re Pacific Lumber Co.)*, 584 F.3d 229, 251–52 (5th Cir. 2009) (stating that Fifth Circuit cases "broadly foreclose non-consensual non-debtor releases and permanent injunctions"); *In re Lowenschuss,* 67 F.3d 1394, 1401-02 (9th Cir. 1995); *In re W. Real Estate Fund, Inc.*, 922 F.2d 592, 600–02 (10th Cir. 1990) (*per curiam*).

[17] *In re AOV Indus., Inc.*, 792 F.2d 1140, 1143, 1147 (D.C. Cir. 1986).

[18] *Matter of Specialty Equipment Companies,* 3 F.3d 1043, 1047 (7th Cir. 1993).

> Section 524(e) provides that the *discharge itself* does not grant such a release or injunction, and is silent on whether a bankruptcy court can expressly discharge or otherwise affect the liability of a non-debtor. That silence does not mean that third-party releases are always forbidden.[19]

IV. CONSENSUAL RELEASES

The Second Circuit has recognized creditor "consent" as a basis for approving third-party releases[20], and there is extensive case law within the Circuit and elsewhere, particularly from the Delaware bankruptcy courts, concerning what might be sufficient to constitute consent. In determining whether a creditor has consented to a third-party release, courts generally apply contract principles.[21] But the cases are not uniform as to how consent may be manifested in this context. The difference in opinion focuses principally on the form of the ballot and whether there is clear and conspicuous notice of how consent will be deemed to be given.

All courts seem to agree that a vote in favor of the plan will constitute consent for a third-party release as long as the plan and disclosure statement make it clear that such a vote will have that effect.[22] Within this camp are decisions which have found consent where, in addition to a

[19] *In re Adelphia Communications Corp.,* 368 B.R. 140, 266 (Bankr. S.D.N.Y. 2007), *appeal dismissed* 367 B.R. 84 (S.D.N.Y. 2007).

[20] *In re Metromedia Fiber Network, Inc.* 416 F.3d 136, 142 (2d Cir. 2005) (citing approvingly *Matter of Specialty Equipment Companies,* 3 F.3d 1043, 1047 (7th Cir. 1993)). In *Specialty Equipment*, the Seventh Circuit approved the third-party releases at issue on the independent basis that they were consensual. *Specialty Equipment Companies,* 3 F.3d at 1047 ("Although these releases in their various forms do pose a rather knotty problem, it is not one that we need to unravel completely inasmuch as the Releases granted in the Debtors' reorganization are consensual").

[21] *In re Relativity Fashion,, LLC,* 2018 WL 2938516, at *5 (Bankr. S.D.N.Y. June 7, 2018); *In re SunEdison, Inc.,* 576 B.R. 453, 458 (Bankr. S.D.N.Y. 2017); *In re Coram Healthcare Corp.,* 315 B.R. 321, 336 (Bankr. D. Del. 2004).

[22] *In re Relativity Fashion, LLC, 2018 WL 2938516,* at *4 (Bankr. S.D.N.Y. June 7, 2018); *In re SunEdison, Inc.,* 576 B.R. 453, 458 (Bankr. S.D.N.Y. 2017); *In re Abeinsa Holding, Inc.,* 562 B.R. 265, 285 (Bankr. D. Del. 2016); *In re Chassix Holdings, Inc.,* 533 B.R. 64, 80 (Bankr.

vote accepting the plan, the creditor was afforded the opportunity to "opt-out" of the third-party release by checking a box providing for the opt-out and did not do so. [23]

The decisions are divided, however, on two important issues: (1) whether impaired, non-voting creditors who were solicited with a ballot that had an opt-out provision and were given explicit instructions on the effect of not voting and not opting out ("abstaining creditors") will be deemed to have consented to a third-party release by virtue of their "silence;" and relatedly, (2) whether unimpaired creditors can be deemed to consent to a third-party release by virtue of their unimpaired status.

At the more liberal end of the spectrum, cases that have approved third-party releases on the theory of consent for non-voting creditors who were given an opt-out ballot and explicit instructions regarding the effect of not returning a ballot include the following[24]:

S.D.N.Y. 2015); *In re MPM Silicones, LLC,* 2014 WL 4436335, at *32 (Bankr. S.D.N.Y. Sept. 9, 2014), *aff'd* 531 B.R. 321 (S.D.N.Y. 2015), *aff'd in part on other grounds, rev'd in part on other grounds and remanded on other grounds,* 874 F.3d 767 (2d Cir. 2017); *In re Adelphia Communications Corp.,* 368 B.R. 140, 268 (Bankr. S.D.N.Y. 2007), *appeal dismissed* 367 B.R. 84 (S.D.N.Y. 2007); *In re Exide Technologies*, 303 B.R. 48, 74 (Bankr. D. Del. 2003); *In re Zenith Electronics Corp.,* 241 B.R. 92, 111 (Bankr. D. Del. 1999). *See also In re Lower Bucks Hospital,* 571 Fed. Appx. 139, 143-44 (3d Cir. July 3, 2014) (upholding bankruptcy court's ruling that third-party release in plan would not be given effect due to the failure of the disclosure statement or plan to conspicuously highlight the third-party release).

[23] *See In re Abeinsa,* 562 B.R. 265, 285 (Bankr. D. Del. 2016); *In re Genco Shipping & Trading Limited,* 513 B.R. 233, 271 (Bankr. S.D.N.Y. 2014); *In re Indianapolis Downs, LLC,* 486 B.R. 286, 304 (Bankr. D. Del. 2013); *In re Washington Mutual, Inc.,* 442 B.R. 314, 355 (Bankr. D. Del. 2011).

[24] Additionally, at least two decisions have approved a third-party release based on consent for creditors who voted to ***reject*** the plan and did not affirmatively opt-out when they were given explicit instructions on the effect of not affirmatively opting out on the ballot. *In re Genco Shipping & Trading Limited,* 513 B.R. 233, 271 (Bankr. S.D.N.Y. 2014)*; In re MPM Silicones, LLC,* 2014 WL 4436335, at *32 (Bankr. S.D.N.Y. Sept. 9, 2014), *aff'd* 531 B.R. 321 (S.D.N.Y. 2015), *aff'd in part on other grounds, rev'd in part on other grounds and remanded on other grounds,*874 F.3d 767 (2d Cir. 2017). It follows, *a fortiori,* that if these decisions approved a third-party release for creditors who voted to ***reject*** a plan but did not opt out of the release, they

- *In re Gulfmark Offshore*, 2017 WL 5461364, at *11 (Bankr. D. Del. Oct. 4, 2017)

- *In re Indianapolis Downs, LLC,* 486 B.R. 286, 304-05 (Bankr. D. Del. 2013)

- *In re DSDB North America, Inc.,* 419 B.R. 179, 218-19 (Bankr. S.D.N.Y. 2009), *aff'd* 2010 WL 1223109 (S.D.N.Y. Mar. 24, 2010), *aff'd in part, rev'd in part* 627 F.3d 496 (2d Cir. 2010)

- *In re Calpine Corp.,* 2007 WL 4565223, at *10 (Bankr. S.D.N.Y. Dec. 19, 2007), *appeal denied as moot* 390 B.R. 508 (S.D.N.Y. 2008), *aff'd* 354 Fed. Appx. 479 (2d Cir. Nov. 25, 2009)

Cases which have refused to find consent to a third-party release for these so-called "abstaining" creditors include the following:

- *In re SunEdison, Inc.,* 576 B.R. 453, 461 (Bankr. S.D.N.Y. 2017

- *In re Chassix Holdings, Inc.,* 533 B.R. 64, 80 (Bankr. S.D.N.Y. 2015)

- *In re Washington Mutual, Inc.,* 442 B.R. 314, 355 (Bankr. D. Del. 2011).

Of these cases, *Chassix Holdings* specifically rejected the idea that a creditor or equity security holder who was deemed to have rejected the plan, *see* 11 U.S.C. §1126(g), or returned a ballot rejecting the plan, but did not opt out of the third-party release on the ballot, could be

certainly would approve the release, on the basis of consent, for creditors who did not return a ballot and therefore did not vote one way or the other on the plan.

deemed to have consented to the third-party release.[25] Rather, in such circumstances, it required an "opt-in" provision on the ballot in order to find consent from such parties.[26]

The bankruptcy court in *Sun Edison* came to the same conclusion as did the bankruptcy court in *Chassix Holdings*, reasoning that under contract law, the impaired creditors who did not return a ballot were under no "duty to speak" against the third-party release by returning a ballot and affirmatively opting out.[27] However, this analysis raises the question whether the bankruptcy court can impose a duty to speak by virtue of an order approving voting procedures that would require creditors to affirmatively "opt-out" of a third-party release.

Courts are similarly divided on whether unimpaired creditors can be bound by a third-party release when they do not object to the plan. In *In re Spansion, Inc.*, the Delaware bankruptcy court held that unimpaired creditors were bound by the third-party release by their failure to object to the plan..[28] Further, the United States Trustee in the Third Circuit has suggested that a creditor may be deemed to grant releases to third parties "when it is considered unimpaired and does not vote."[29]

[25] *Chassix Holdings,* 533 B.R. at 81 ("[c]harging all inactive creditors with full knowledge of the scope and implications of the proposed third party releases, and implying 'consent' to the third party releases based on creditors' inaction, is simply not realistic or fair and would stretch the meaning of 'consent' beyond the breaking point.").

[26] *Id.*

[27] *SunEdison,* 576 B.R. at 458-59. Viewing the third-party release provision as an "offer" under contract law, the court cited contract law cases for the proposition that "absent a duty to speak, a party's silence cannot be translated into an acceptance of an offer to contract." *Id.* (internal quotations omitted).

[28] *In re Spansion, Inc.,* 426 B.R. 114, 144 (Bankr. D. Del. 2010).

[29] *In re Abeinsa Holding, Inc.,* 562 B.R. 265, 285 (Bankr. D. Del. 2016).

On the other hand, the bankruptcy court in *Chassix Holdings* has rejected the idea that "unimpaired" creditors should be presumed to have consented to a third-party release by virtue of their "unimpaired" status, reasoning that they could not remain "unimpaired" if they were deemed to be releasing third parties, which would constitute an alteration of their legal rights under 11 U.S.C. §1124.[30] It further made the common sense observation that if the releases only related to claims the debtor itself was satisfying, they would serve no purpose, whereas if they covered "claims that the creditors might be able to pursue notwithstanding the satisfaction of their claims against the Debtors," there was "no good basis on which to say that the Debtors' satisfaction" of their own liabilities should give rise to a "deemed consent" by "unimpaired creditors" to release their own claims against third parties.[31]

V. NON-CONSENSUAL RELEASES

Overview of the Law

The Second Circuit Court of Appeals has held that a bankruptcy court has the power to enjoin a creditor from suing a third party, which it has equated with a nondebtor release, *In re Metromedia Fiber Network, Inc.,* 416 F.3d 136, 141 (2d Cir. 2005), only upon a "finding that truly unusual circumstances render the release terms important to the success of the plan …." *Id.* Before considering the factors identified and applied by the Second Circuit and other courts for approving third-party or nondebtor releases, it is necessary to identify both the jurisdictional and statutory authority for such releases.

[30] *In re Chassix Holdings, Inc.,* 533 B.R. 64, 81 (Bankr. S.D.N.Y. 2015). *Accord In re Genco Shipping & Trading Limited,* 513 B.R. 233, 270 (Bankr. S.D.N.Y. 2014) ("[t]he Court agrees that simply classifying a party as unimpaired does not mean that they should be somehow automatically deemed to grant a release where the requirements of *Metromedia* have not been met").

[31] *Id.*

In the Second Circuit, a bankruptcy court's subject matter jurisdiction to approve a third party release included in a plan of reorganization turns on whether the claims subject to the release "might have any 'conceivable effect' on the bankruptcy estate."[32] Stated differently, "a bankruptcy court only has jurisdiction to enjoin third-party non-debtor claims that directly affect the *res* of the bankruptcy estate."[33] A common ground for finding a jurisdictional basis for a third-party release is when the third party in whose favor the release runs has a right of indemnification from the debtor if the released claims were allowed to proceed.[34]

The statutory grounds for third-party releases have been identified by the courts as some combination of 11 U.S.C. §§105(a), 1123(a)(5) (plan must include adequate means for implementation) and 1123(b)(6) (plan may include any other provision not inconsistent with the Bankruptcy Code). [35]

Turning to the standards that have been identified by the courts as relevant to determining whether to approve a third-party release, while the Second Circuit has stated that "this is not a

[32] *In re Quigley Co., Inc.,* 676 F.3d 45, 57 (2d Cir. 2012) (quoting *In re Cuyahoga Equip. Corp.*, 980 F.2d 110, 114 (2d Cir.1992)).

[33] *In re Johns-Manville,* 517 F.3d 52, 66 (2d Cir. 2008), *reaff'd* 600 F.3d 136, 153 (2d Cir. 2010).

[34] *In re SunEdison, Inc.,* 576 B.R. 453, 462-63 (Bankr. S.D.N.Y. 2017) (citing authorities); *In re Sabine Oil & Gas Corporation,* 555 B.R. 180, 290 (Bankr. S.D.N.Y. 2016); *In re Residential Capital, LLC,* 508 B.R. 838, 848-49 (Bankr. S.D.N.Y. 2014).

[35] *In re Ingersoll, Inc.,* 562 F.3d 856, 864 (7th Cir. 2009); *In re Airadigm Communications., Inc.*, 519 F.3d 640, 657 (7th Cir. 2008); *In re Dow Corning Corp.,* 280 F.3d 648, 656-57 (6th Cir. 2002); *In re Motors Liquidation Co.,* 447 B.R. 198, 220 (Bankr. S.D.N.Y. 2011); *In re Master Mortgage Inv. Funding, Inc.,* 168 B.R. 930, 934 (Bankr. W.D. Mo. 1994).

matter of factors and prongs,"[36] in the same opinion it directed bankruptcy courts to focus on certain considerations in making the determination.[37] They are:

- Whether the estate has received substantial consideration;
- Whether the enjoined claims are "channeled" to a settlement fund rather extinguished;
- Whether the enjoined claims would indirectly impact the debtor's reorganization by "way of indemnity or contribution"; and
- Whether the plan otherwise provides for the full payment of the enjoined claims.[38]

The Sixth Circuit Court of Appeals has identified the following seven factors as ones that must be present before a "bankruptcy court may enjoin a non-consenting creditor's claims against a non-debtor":[39]

> 1) There is an identity of interests between the debtor and the third party, usually an indemnity relationship, such that a suit against the non-debtor is, in essence, a suit against the debtor or will deplete the assets of the estate;
>
> (2) The non-debtor has contributed substantial assets to the reorganization;
>
> (3) The injunction is essential to reorganization, namely, the reorganization hinges on the debtor being free from indirect suits against parties who would have indemnity or contribution claims against the debtor;

[36] *Metromedia,* 416 F.3d at 142.

[37] *Id.* at 143.

[38] *Id.* at 142.

[39] *In re Dow Corning Corp.,* 280 F.3d 648, 658 (6th Cir. 2002). The Fourth and Eleventh Circuits, while adopting the *Dow* factors for determining whether a third-party release may be approved, have both said that bankruptcy courts should have discretion to determine which of the factors will be relevant in each case. *In re Seaside Engineering & Surveying, Inc.,* 780 F.3d 1070, 1079 (11th Cir. 2015). *National Heritage Foundation, Inc. v. Highbourne Foundation,* 760 F.3d 344, 348 (4th Cir. 2014).

> (4) The impacted class, or classes, has overwhelmingly voted to accept the plan;
>
> (5) The plan provides a mechanism to pay for all, or substantially all, of the class or classes affected by the injunction;
>
> (6) The plan provides an opportunity for those claimants who choose not to settle to recover in full and;
>
> (7) The bankruptcy court made a record of specific factual findings that support its conclusions.

The Seventh and Third Circuits have weighed in with their own factors, which are a variation of the factors identified in *Metromedia* and *Dow.* The Seventh Circuit has approved a third-party release when it was "necessary for the reorganization and appropriately tailored." [40] In *Airadigm,* the third-party release was much narrower than what we typically see in the Second Circuit, applying only to release claims against the debtor's most significant secured creditor that arose "out of or in connection with the reorganization itself" and did not include claims for "willful misconduct."[41] In the Third Circuit, "the 'hallmarks' of a permissible non-consensual third-party release [are] 'fairness, necessity to the reorganization, and specific factual findings to support these conclusions'."[42] In terms of fairness, the release must be exchanged for "adequate consideration" or "reasonable compensation."[43]

[40] *In re Airadigm Communications, Inc.,* 519 F.3d 640, 657 (7th Cir. 2008).

[41] *Id.* at 657.

[42] *In re Lower Bucks Hospital,* 571 Fed. Appx. 139, 144 (3d Cir. 2014) (quoting *In re Continental Airlines,* 203 F.3d 203, 214 (3d Cir. 2000)). *See also In re Global Industrial Technologies, Inc.,* 645 F.3d 201, 206 (3d Cir. 2011) (reaffirming standards for third-party releases that were set forth in *Continental*).

[43] *Id.* at 144 (citing *Continental,* 203 F.3d at 215; *In re Spansion, Inc.,* 426 B.R. 114, 144 (Bankr. D. Del. 2010)).

Lower courts in the Third Circuit have developed their own factors to determine the permissibility of third-party releases, apparently to address the Third Circuit's general requirements of "fairness" and "necessity." They are capsulized as follows:

> (1) an identity of interest between the debtor and non-debtor such that a suit against the non-debtor will deplete the estate's resources;
>
> (2) a substantial contribution to the plan by the non-debtor;
>
> (3) the necessity of the release to the reorganization;
>
> (4) the overwhelming acceptance of the plan and release by creditors and interest holders; and
>
> (5) the payment of all or substantially all of the creditors and interest holders under the plan. [44]

Application

In *Metromedia,* the Second Circuit made clear that even a significant financial contribution from a creditor of the estate will not support approval of a third-party release running to that creditor and certain other third parties related to the creditor absent a finding of the importance of the release to the success of the plan.[45] Importantly, the creditor who was the proposed recipient of the release, the Kluge Trust, forgave $150 million in secured loans, converted $15.7 million in secured debt to equity and committed to purchase up to $12.5 million in common stock of the debtor.[46] The release provided that the Kluge Trust, as well as its insiders, would be released from any claims held by any creditor of Metromedia arising out of

[44] *In re One2One Communications, LLC,* 2016 WL 3398580, at *6 (D.N.J. June 14, 2016) (citing *In re Zenith Electronics Corp.,* 241 B.R. 92, 110 (Bankr. D. Del. 1999), *In re Washington Mutual,* 442 B.R. 314, 346 (Bankr. D. De.l. 2011), and *In re Indianapolis Downs, LLC,* 486 B.R. 286, 3030 (Bankr. D. Del. 2013)).

[45] *Metromedia*, 416 F.3d at 413.

[46] *Id.* at 141.

any matter related to Metromedia and which are based on any act or omission taking place prior to the Effective Date of the plan.[47] Another release that was challenged released former or current Metromedia personnel from the same type claims, except for gross negligence or willful misconduct.[48]

The Second Circuit held that since there was no evidence presented as to the importance to the plan of the broad Kluge Trust release, which released not only the Klug Trust but numerous other third parties, it could not be approved.[49] Instructively, however, the Circuit did state that it was not a prerequisite to the approval of a third-party release that the consideration paid by the third party receiving the release must be paid to the enjoined creditors. On the other hand, it also rejected the notion that because the enjoined creditors were allocated a plan distribution, they received consideration sufficient to support the release.[50]

Some important take aways from the *Metromedia* decision are the following:

- Creditor consent is not a mandatory element for approving a third-party release.
- Evidence must be presented to support the "importance" of the third-party release to the success of the plan.

[47] *Id.*

[48] *Id.* at 141 n. 5.

[49] *Id.* at 143. Notably, the Second Circuit observed that when the debtor's Chief Operating Officer was asked at the confirmation hearing if he knew what would happen with respect to the settlement with the Kluge Trust if the release was not approved, he replied, "No, not really." *Id.* at 143 n.7.

[50] *Id.* at 143.

- The consideration paid by the released party does not have to be paid to or otherwise received by the releasing party.[51]
- A significant consideration is whether the released party has a right of indemnity from the debtor such that an action against the third party is, in effect, a claim against the debtor.

Post-*Metromedia*, non-consensual releases have been approved by the courts when there is an unusually significant contribution by a third party, such as a substantial "give-up" by a dominant secured creditor of the estate, or where the third party has a right of indemnification from the debtor for the claim that would be covered by the third-party release. For example, in *In re Sabine Oil & Gas Corp*,.[52] the third-party release at issue was for the benefit of the RBL Lenders, the debtor's major secured creditor, and was approved on the basis that they: 1) converted their entire secured claim to equity, 2) waived the right to receive cash for their adequate protection claims, which were estimated at between $123 and $227 million, 3) committed to providing the debtors with a new $200 million exit revolver credit facility, and 4) held contingent indemnification claims against the debtors based on their loan documents for claims which the challenging creditor sought to assert against the RBL Lenders.[53] Importantly, the court upheld the release notwithstanding that the consideration for it was not received by the creditors who were challenging the release, and because an evidentiary record was made which established that without the release, "the Debtors would not have obtained the significant debt

[51] *But see In re Spansion, Inc.,* 426 B.R. 114, 144 (Bankr. D. Del. 2010) (describing an element of the Third Circuit's test in *Continental* as "whether the non-consenting creditors receive reasonable compensation in exchange for the release").

[52] *In re Sabine Oil & Gas Corp.,* 555 B.R. 180 (Bankr. S.D.N.Y. 2016).

[53] *Id.* at 194, 291-93.

and equity financing contemplated in connection with the Plan on the same terms or the significant concessions from the RBL Released Parties."[54]

Similarly, in *In re Genco Shipping & Trading Limited,*[55] third-party releases in favor of the Debtors' major secured creditor with claims in excess of $1 billion were approved based on "substantial consideration to the reorganization" and rights of indemnification to which they were contractually entitled.[56] The substantial consideration consisted of allowing a distribution of warrants to equity, converting a substantial amount of secured debt to equity, and backstopping a $100 million rights offering.[57] The third party claims released were also ones for which the lenders held rights of indemnity from the Debtors under their prepetition credit agreements.[58]

It is important to emphasize that where the third-party release is broader than the indemnification obligations that are claimed to support it, the release will not be upheld. Thus, where a provision for indemnification of the debtor's lender and DIP financing source related only to postpetition acts, a third-party release that applied to all claims arising before the Effective Date of the plan could not be sustained.[59] Similarly, unless evidence is presented that the specifically identified third parties are entitled to indemnification by the debtor, a third-party release, such as of the debtor's "current and former affiliates, subsidiaries, advisors, principals,

[54] *Id.* at 292-93.

[55] *In re Genco Shipping & Trading Limited*, 513 B.R. 233 (Bankr. S.D.N.Y. 2014).

[56] *Id.* at 271-72.

[57] *Id.* at 272.

[58] *Id.* at 271.

[59] *In re SunEdison, Inc.,* 576 B.R. 453, 463 (Bankr.S.D.N.Y. 2017).

partners, managers, members employees, officers, directors, representatives, financial advisors, attorneys, accountants…," will not be approved.[60]

The third-party releases that have been upheld by the Circuit Courts of Appeal in other jurisdictions have been substantially narrower than the releases at issue in *Metromedia, Sabine Oil, Genco Trading* and *SunEdision.* In *Seaside Engineering,* while the third-party release was a release of any liability to the holder of a claim and ran to the officers, directors of the debtor and to the debtor's "representatives," it was limited to acts or omissions relating to or arising out of the Chapter 11 case or pursuit of a plan, except for willful misconduct and gross negligence.[61] The Eleventh Circuit, in upholding the release, undertook an analysis of the *Dow* factors and in the process, found that the contribution of the Debtor's officers and personnel in the form of labor was the "very lifeblood of the reorganized debtor" and was a factor in favor of the release, as was the importance for them to be free of additional lawsuits in the "labor-intensive" surveying business.[62]

In *In re Airadigm Communications, Inc,.*[63] the Seventh Circuit considered the same type of release, only it applied just to the debtor's major secured lender.[64] Applying the *Dow* factors, it approved the release because it only was a release of postpetition acts or conduct relating to the

[60] *Id.*

[61] *In re Seaside Engineering & Surveying, Inc.,* 780 F.3d 1070, 1076 (11th Cir. 2015).

[62] *Id.* at 1080. Interestingly, the Fourth Circuit in *National Heritage Foundation, Inc. v. Highbourne Foundation,* 760 F.3d 344 (4th Cir. 2014), specifically rejected the idea that a third-party release of the debtor's officers and directors could be supported by their promise to continue serving the debtor. *Id.* at 348. Such a promise, it held, did not constitute "meaningful consideration" because they were already getting compensated for their services or, as to preconfirmation services, had a fiduciary duty to render them. *Id.*

[63] *In re Airadigm Communications, Inc.,* 519 F.3d 640 (7th Cir. 2008).

[64] *Id.* at 657.

reorganization, except for willful misconduct, and because the lender consented to the restructuring of $188 million in secured claims, without which the reorganization could not have been possible.[65]

VI. CONSTITUTIONAL AUTHORITY/SUBJECT MATTER JURISDICTION OF BANKRUPTCY COURTS TO APPROVE THIRD-PARTY RELEASES[66]

In *Millennium Lab Holdings II, LLC,* Bankruptcy Judge Laurie Silverstein of the Delaware bankruptcy court, in a bench ruling, confirmed the debtors' ("Millennium") chapter 11 plan which contained a release of all claims held by creditors against a group of Millennium's equity holders who were contributing $325 million to the reorganization (the "Non-Debtor Equity Holders"). The plan was confirmed over the objections of a group of secured lenders denominated as Voya,[67] which had objected to confirmation on the grounds that the bankruptcy court did not have subject matter jurisdiction to release the common law fraud claims and RICO claims Voya was asserting against the Non-Debtor Equity Holders, that third-party releases are impermissible, and that, in any event, the releases at issue did not meet the *Continental* standard.[68]

[65] *Id.*

[66] This section of the materials addresses the constitutional and subject matter jurisdiction issues as they were raised and resolved in *In re Millennium Lab Holdings II, LLC,* 575 B.R. 252 (Bankr. D. Del. 2017), which was recently affirmed by the Delaware District Court on September 21, 2018. *See In re Millennium Lab Holdings II, LLC,* No. 1:17-cv-01461-LPS, 2018 WL 45219141 (D. Del. Sept. 21, 2018). A discussion of the affirmance is at the end of the materials.

[67] The group of lenders is fully identified in *In re Millennium Lab Holdings II, LLC,* 575 B.R. 252, 255 n. 2 (Bankr. D. Del. 2017), *aff'd* 2018 WL 45219141 (D. Del. Sept. 21, 2018).

[68] *Id.* at 257.

Voya appealed the confirmation order on the ground that the bankruptcy court lacked subject matter jurisdiction to approve the release and raised a new argument that the bankruptcy court also lacked constitutional authority to permanently release the claims post-*Stern v. Marshall*.[69] Millennium moved to dismiss the appeal on the ground of equitable mootness, but the district court denied the motion without prejudice and remanded to the bankruptcy court with instructions to consider whether, or clarify its ruling that, "it had constitutional adjudicatory authority to approve the nonconsensual release of Appellants' direct non-bankruptcy common law fraud and RICO claims against the Non-Debtor Equity Holders."[70] Thus begat a closely watched and widely discussed battle testing the limits of the United States Supreme Court's decision in *Stern v. Marshall*[71] as applied to confirmation of plans that contain non-consensual third-party releases.

It will be recalled that *Stern* held that, notwithstanding statutory authority to adjudicate, as a core proceeding, state-law counterclaims by the estate against persons filing claims against the estate, 28 U.S.C. §157(b)(2)(C), Article III of the Constitution precluded an Article I bankruptcy court from finally adjudicating a state law counterclaim to a creditor's proof of claim that is not resolved in the process of ruling on the creditor's proof of claim.[72] It was Voya's argument on appeal that the bankruptcy court was, in effect, finally adjudicating its non-bankruptcy claims without its consent, in derogation of *Stern,* because the entry of the confirmation order extinguished them without an actual adjudication on the merits by an Article

[69] *Opt-Out Lenders v. Millennium Lab Holdings II, LLC (In re Millennium Lab Holdings II, LLC),* 242 F.Supp.3d 322, 325 (D. Del. 2017).

[70] *Id.* at 340.

[71] *Stern v. Marshall,* 564 U.S. 462, 131 S.Ct. 2594, 180 L.Ed.2d 475 (2011).

[72] *Stern,* 564 U.S. at 503.

III judge.[73] This argument is premised on what Judge Silverstein denominated as the "broad interpretation" of *Stern,* which is that "a bankruptcy judge cannot enter a final judgment on all state law claims, all common law causes of action or all causes of action under state law."[74] (the "Broad Interpretation"). The "narrow interpretation" of *Stern*, on the other hand, holds that a bankruptcy judge "lack[s] constitutional authority to enter a final judgment on a state law counterclaim that is not resolved in the process of ruling on a creditor's proof of claim."[75] (the "Narrow Interpretation").

In *Millennium,* the plan proposed that in exchange for their $325 million contribution, the Non-Debtor Equity Holders would receive a release of any claims held by creditors of the estate against them and certain related parties. The release included fraud and RICO claims asserted by Voya based on allegations that Voya was fraudulently induced into participating in a $1.825 billion secured credit facility granted to Millennium, $1.3 billion of which was paid out to the Non-Debtor Equity Holders as a special dividend, while Millennium was undergoing an investigation by the U.S. Dept. of Justice into fraudulent billing practices[76] – an investigation that was never disclosed to Voya until after it made its loan of $106.3 million.[77] After the loan was made, and after receiving a notification from DOJ that it was revoking Millennium's Medicare billing privileges on account of the submission of fraudulent claims, Millennium disclosed to its lenders that it had entered into an agreement in principle with DOJ to settle the

[73] *Millennium Lab Holdings,* 242 F.Supp.2d at 340.

[74] *Millennium Lab Holdings,* 575 B.R. at 268-69.

[75] *Id.* at 268.

[76] Millennium is a provider of laboratory-based diagnostic testing services that derives significant revenue from Medicare and Medicaid reimbursements.

[77] *Millennium Lab Holdings,* 242 F.Supp.3d at 328-29.

fraudulent billing claims for $250 million.[78] Millennium's inability to structure an out-of-court workout or prepackaged plan is what led to its chapter 11 filing.[79]

It was only on appeal of the confirmation order to the district court when Voya raised for the first time an objection to the constitutional authority of the bankruptcy court to approve a release of its non-bankruptcy common law fraud claims and RICO claims against the Non-Debtor Equity Holders.[80] In its decision remanding to the bankruptcy court, the district court, while not ruling on the issue, expressed its disagreement with Millennium's view "that the plan release did not run afoul of *Stern* because it was not a final adjudication of the claims," reasoning that "[i]f Article III prevents the Bankruptcy Court from entering a final order disposing of a non-bankruptcy claim against a nondebtor outside the proof of claim process, it follows that this prohibition should be applied regardless of the proceeding (*i.e.,* adversary proceeding, contested matter, plan confirmation)."[81] The stage was thus set for Judge Silverstein's remand decision.

On remand, while the focus of her decision was on the constitutional authority of the bankruptcy court to approve a non-consensual third-party release as part of confirmation of a plan, Judge Silverstein first held that the bankruptcy court had subject matter jurisdiction to approve a release in that context because "[c]onfirmation of plans is one of sixteen core proceedings listed in §157(b)(2)."[82] She then turned her focus to the constitutional question.

[78] *Id.* at 329.

[79] *Id.*

[80] *In re Millennium Lab Holdings, LLC,* 575 B.R. 252, 257 (Bankr. D. Del. 2017).

[81] *Millennium Lab Holdings,* 242 F.Supp.3d at 339.

[82] *Millennium Lab Holdings,* 575 B.R. at 261. *But see In re Midway Gold US, Inc.,* 575 B.R. 475, 519 (Bankr. D. Colo. 2017) (stating that "the Court cannot permit third-party non-debtors to bootstrap their disputes into a bankruptcy case in this fashion" and concluding that "[t]here must

After setting forth the Narrow Interpretation and Broad Interpretation of *Stern*, Judge Silverstein noted that under either interpretation, "*Stern* is limited to a state law claim or counterclaim brought by the debtor-in-possession or trustee."[83] This recognition, alone, would take the issue of the bankruptcy court's constitutional authority to approve a plan release such as the one before Judge Silverstein outside the realm of *Stern*, because the estate was not asserting any state law claims or counterclaims.

Nonetheless continuing her analysis, Judge Silverstein adopted the position that "the operative proceeding for purposes of a constitutional analysis is confirmation of a plan,"[84] as distinct from the actual claims that would be subject to the third-party release. Thus, she reasoned that since "confirmation of a plan is not a state law claim of any type," the third-party release at issue would be constitutionally permissible under either the Narrow Interpretation or the Broad Interpretation.[85] She found further support for this conclusion by noting that a third-party release in a plan must pass muster under federal standards, particularly *Continental*, which do not implicate the merits of "the many claims that may be released by virtue of the third party releases.[86] Thus, she was not ruling on the merits of those claims but rather, whether the plan and third party releases comported with the *Continental* standard.

Judge Silverstein further found that adopting Voya's interpretation – that under *Stern*, its RICO and fraud claims "neither stem from the bankruptcy itself nor are resolvable in the claims

be some independent statutory basis for the Court to exercise jurisdiction over the third-parties' disputes before the Court may adjudicate them").

[83] *Id.* at 268-69.

[84] *Id.* at 271.

[85] *Id.*

[86] *Id.* at 272.

allowance process"[87] – would dramatically change the division of labor between the bankruptcy and district courts because various matters that are considered routine for the bankruptcy court affect in some way purely state law claims and thus, under Voya's interpretation, would have to resolved by the district court. The examples the Judge gave were: 1) a §363 asset sale in which the purchaser seeks to be relieved of successor liability; 2) requests to compel annual shareholder meetings; 3) substantive consolidation of debtors, and/or debtors and non-debtors; 4) recharacterization or subordination; 5) requests to establish notice procedures to preserve a debtor's NOLs by prohibiting trading in the stock without certain advance notice and 6) a sale of property co-owned by the debtor and a non-debtor.[88]

As an additional or alternative ground for her ruling, Judge Silverstein held that Voya both forfeited and waived any objection to her constitutional authority to enter a final order confirming the plan by failing to expressly make the constitutional objection before the hearing on confirmation, as a result of which Voya "implicitly consented" to her authority and thereby waived any right to contest it.[89]

After Judge Silverstein's remand decision, the case returned to Judge Stark of the Delaware District Court for resolution of Voya's appeal of the confirmation order. The merits of the appeal, as well as another motion to dismiss the appeal filed by Millennium based on mootness, were fully briefed and then argued on July 12, 2018.[90] On September 21, 2018, by which time these materials had been fully prepared, Judge Stark issued his decision affirming

[87] *Id.* at 273-74.

[88] *Id.* at 286.

[89] *Id.* at 288.

[90] *See Opt Out Lenders v. Millennium Lab Holdings II, LLC,* United States District Court for the District of Delaware, Civ. No. 1:17-cv-01461-LPS (ECF No. 45).

Judge Silverstein's decision on remand.[91] Accordingly, the materials have been supplemented to include a discussion of the affirmance.

Addressing first the constitutional issue, Judge Stark recapped that in the Third Circuit "the hallmarks of permissible non-consensual releases are fairness, necessity to the reorganization, and specific factual findings to support these conclusions," added to which is the requirement that "the releases were given in exchange for fair consideration."[92] Although thereafter acknowledging his preliminary view that extinguishing Voya's RICO and fraud claims was tantamount to an adjudication on the merits of the claims and that *Stern* applied as much to plan confirmation proceedings as it did to any other bankruptcy-related proceeding,[93] he reversed course and adopted Judge Silverstein's view that *Stern* did not apply in the context of plan confirmation.

Specifically, Judge Stark "agree[d] with Judge Silverstein's conclusion that '*Stern* did not address, either expressly or by implication, any context other than counterclaims,' nor did it 'announce a broad holding addressing every facet of the bankruptcy process'."[94] Judge Stark further agreed with the Judge Silverstein's alternative reasoning that even if *Stern*'s disjunctive test - whether the action at issue stems from the bankruptcy itself or would necessarily be resolved in the claims allowance process – were imported into the plan confirmation context, he

[91] *In re Millennium Lab Holdings II, LLC,* No. 1:17-cv-01461-LPS, 2018 WL 45219141 (D. Del. Sept. 21, 2018) (hereinafter the "Millennium Affirmance").

[92] Millennium Affirmance, at *10 (quoting *In re United Artists Theater Co. v. Walton (In re United Artists Theater Co.*), 315 F.3d 217, 227 (3d Cir. 2003) and *In re Global Industrial Technologies, Inc.*, 645 F.3d 201, 206 (3d Cir. 2011)) (internal quotations omitted).

[93] This was articulated in the decision remanding to Judge Silverstein. *Millennium Lab Holdings,* 242 F.Supp.3d at 339.

[94] Millennium Affirmance, at *11.

would consider the test to have been satisfied on the basis that the RICO and fraud claims were resolved in the claims allowance process and the plan and its releases "stemmed from the bankruptcy itself."

Ultimately, however, Judge Stark did not consider it necessary to rule on whether the disjunctive test was satisfied because he found that Judge Silverstein was "correct in holding that plan confirmation is the operative proceeding, and in holding that *Stern* did not require application of the Disjunctive Test in the context of plan confirmation."[95] In that regard, he found persuasive the idea "that determining whether a bankruptcy court has constitutional authority to issue a final order on a proceeding requires looking **at the proceeding** – here, the confirmation plan proceeding – not on its incidental effects – which, here, would be its impact on Voya's RJCO/fraud claims."[96] As for Voya's argument that confirmation of the plan with the releases was tantamount to an adjudication of its claims on the merits, which the bankruptcy court lacked constitutional authority to do, Judge Stark adopted Judge Silverstein's view that "'taking the position that third party releases in a plan are equivalent to an impermissible adjudication of the litigation being released is, at best, a substantive argument against third party releases, not an argument that confirmation orders containing releases must be entered by a district court'."[97]

After holding that the bankruptcy court had constitutional authority to confirm the plan with the third-party releases, Judge Stark held that all other issues on appeal would be dismissed

[95] Millennium Affirmance at * 12.

[96] Millennium Affirmance at * 12 (emphasis original).

[97] Millennium Affirmance at *14 (quoting *Millennium*, 575 B.R. at 283).

as equitably moot.[98] But as a precaution and alternative holding, he went on to address the remaining merits of the appeal, *i.e.* subject matter jurisdiction and statutory authority to approve the releases.

Judge Stark held that subject matter jurisdiction was established under the Third Circuit's decision in *Pacor*, which asks whether, for "related to " jurisdiction over third-party claims, the outcome of the proceeding could conceivably have any effect on the estate being administered in bankruptcy."[99] *Pacor* was satisfied, concluded Judge Stark, because of Millennium's obligation to indemnify the non-debtor releasees against Voya's claims under the Debtors' operational agreements, or at least based on Millennium's obligation to advance defense costs even if the indemnity did not apply for RICO and fraud claims.[100]

As for the statutory authority to approve the releases, Judge Stark went through an application of the *Master Mortgage* factors,[101] which Judge Silverstein had applied, and found that three of the factors Voya had argued were not satisfied (factors 1, 2 and 5) were satisfied. The factors are:

> 1) an identity of interest between the debtor and the third party, such that a suit against the non-debtor is, in essence, a suit against the debtor or will deplete assets of the estate; (2) substantial contribution by the non-debtor of assets to the reorganization; (3) the essential nature of the injunction to the reorganization to the extent that, without the injunction, there is little likelihood of success; (4) an agreement by a substantial majority of creditors to support the injunction, specifically if the impacted class or classes "overwhelmingly" votes to accept the plan; and (5) provision in the

[98] Millennium Affirmance at *19.

[99] Millennium Affirmance at *20.

[100] Millennium Affirmance at *20.

[101] The factors are taken from *In re Master Mortgage Inv. Fund, Inc.,* 168 B.R. 930, 935 (Bankr. W.D. Mo. 1994).

> plan for payment of all or substantially all of the claims of the class or classes affected by the injunction.[102]

In summary, Judge Stark found as follows: (1) the "identity of interest" factor was satisfied based on Millennium's indemnification, advancement and defense obligations; (2) Voya' argument on the "substantial contribution" factor was waived; and (3) the factor which considers whether there is payment of all or substantially all of the claims of the class or classes affected by the injunction requires only that the plan provide "for payments to all classes of claims in excess of the liquidation value of the claims," which Millennium's plan had done.[103]

It remains to be seen whether Voya will appeal to the Third Circuit. The time for appeal would be 30 days from entry of the judgement or order absent the timely filing of a motion for rehearing or a motion to extend the 30-day period.[104]

[102] Millennium Affirmance at *20 (quoting *In re Master Mortgage Inv. Fund, Inc.,* 168 B.R. 930, 935 (Bankr. W.D. Mo. 1994)).

[103] Millennium Affirmance at *21-22.

[104] *See* Fed. R. App. P. 6(b), 4(a)(1)(A), 4(a)(5).

CONNECTICUT BANKRUPTCY CONFERENCE
OCTOBER 4, 2018

Issues in Individual Chapter 11 Cases

Key Issues Facing Individual Debtors (And Their Counsel) When Filing For Chapter 11 Relief

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Summary of Major Differences Between Chapter 13 and Chapter 11 for Individuals

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OVERVIEW

While it has long been the case that individual debtors can seek protection under Chapter 11 of the United States Bankruptcy Code,[1] the Bankruptcy Abuse Prevention And Consumer Protection Act of 2005 (BAPCPA) changed the landscape for individual debtors considering filing for such protection. The following provisions in the Bankruptcy Code[*] brought about through BAPCPA specifically affect Chapter 11 individual debtors:

- Section 1115 – property of the estate includes earnings and property acquired after the commencement of the case.
- Section 1123(a) – a plan must "provide for the payment to creditors under the plan of all or such portion of earnings from personal services performed by the debtor after the commencement of the case or other future income of the debtor as is necessary for the execution of the plan."
- Section 1127(e) – a confirmed plan can be modified upon request of the debtor, the trustee, the United States Trustee, or an unsecured creditor; the amount or duration of payments to certain creditors can be altered even after substantial consummation of the plan
- Section 1129(a)(15) – a plan cannot be confirmed over the objection of an unsecured creditor unless the plan either: (i) provides for payment of the allowed amount of the objecting creditor's claim or (ii) devotes all "projected disposable income" for the longer of five years or the term of the plan
- Section 1129(b)(2)(B) – debtor may retain his/her property only if the debtor complies with the disposable income requirement; a debtor may retain property included in his/her bankruptcy estate under section 1115
- Section 1141(d) – discharge for an individual Chapter 11 debtor is delayed (subject to the court's discretion) until the payments under his/her plan have been completed

Among the critical issues that arise from the Bankruptcy Code provisions affecting individuals in Chapter 11 cases and that have been addressed by courts across the nation are: (1) the definition of what constitutes property of an individual Chapter 11 debtor's bankruptcy estate and the application of the absolute priority rule as a requisite for confirmation of an individual's chapter 11 plan in a cram-down situation; (2) whether involuntary bankruptcy cases filed against individuals and the resulting control over a debtor's post-petition earnings triggers the individual debtor's constitutional right to be free from involuntary servitude; and (3) the ethical dilemma facing the attorney who advises the individual debtor before and after filing for Chapter 11 protection and whether the debtor, the estate or the trustee holds the attorney-client privilege.

[*] Hereinafter, any reference to "the Bankruptcy Code" or a "Section" shall be a reference to the United States Bankruptcy Code as codified in Title 11 of the United States Code, 11 U.S.C. § 101 *et seq.*, and the relevant section therein.

ABSOLUTE PRIORITY RULE ISSUES
11 U.S.C. § 1129(b)(2)(B)

Key concern: **Does the interplay between Sections 1115, 541, 1129(b)(2)(B)(II), 1123(a)(8), and 1129(a)(15) of the Bankruptcy Code repeal the absolute priority rule (APR) with respect to individual Chapter 11 debtors?**

The APR, codified in Section 1129(b)(2)(B) of the Bankruptcy Code, is a component of the "fair and equitable" requirement that must be met in order to confirm a plan over the objection of creditors. 11 U.S.C. § 1129(b) (2) (B) (i)-(ii). To meet this requirement, a plan must pay an impaired, dissenting class of unsecured claims in full, or disallow "holders of any junior claims or interests to receive or retain any property under the plan on account of such claims or interests." In re Henderson, 41 B.R. 783, 789 (M.D. Fla. 2006) (citations omitted); See also Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 202 (1988) ("no Chapter 11 reorganization plan can be confirmed over the creditors' legitimate objections. . . if it fails to comply with the [APR].").

Courts applying and interpreting the APR in individual Chapter 11 cases prior to BAPCPA held that a plan which provided for less than full payment to the unsecured creditors' class generally was not confirmable if the individual Chapter 11 debtor was retaining his/her interest in his/her property, unless the unsecured creditors' class accepted the plan or was not impaired. See e.g., In re Gosman, 282 B.R. 45, 53 (Bankr. S.D. Fla. 2002) (sustaining unsecured creditors' objection to the approval of the Debtor's plan by means of cram-down where individual debtor failed to contribute all of his exempt property under such plan to and for the benefit of unsecured creditors.).[2]

However, the amended Section 1115 (expanding definition of property of the estate) and the amendments to Sections 1123 and 1129 (establishing the contents of the plan as well as the conditions to confirm individual Chapter 11 plans), have raised the question of whether BAPCPA's modifications abrogate the APR for property in individual Chapter 11 cases or whether APR remains applicable to individual Chapter 11 debtor plans. See e.g., In re Eagan, 2013 Bankr. LEXIS 260 (Bankr. W.D.N.C. Jan. 22, 2013) ("Courts have disagreed whether this amendment was intended by Congress to abolish the absolute priority rule in individual Chapter 11 cases altogether, effectively allowing the debtor to retain the entire bankruptcy estate, including property acquired post-petition, over the objection of a dissenting class.").

This debate continues although in recent years more courts are holding that the APR continues to apply. Jessica R. Ellis, *The Absolute Priority Rule for Individuals after Maharaj, Lively, and Stephens: Negotiations or Game Over*, 55 Ariz. L. Rev. 1141, 1151-52 (2013) ("[m]ore than a dozen courts have come to the conclusion that the absolute priority rule applies to individuals.").

Caselaw: BAPCPA abrogates the APR

Several bankruptcy courts have held that the BAPCPA amendments eliminated the APR as applied to an individual's entire estate. See e.g., In re Bullard, 358 B.R. 541, 554 (Bankr. D. Conn. 2007) ("Section 1129(b)(2)(B)(ii) permits a debtor to retain his exempt property and still

confirm a plan under Section 1129(b)'s 'cram-down' provisions."); In re Shat, 424 B.R. 854, 868 (Bankr. D. Nev. 2010) ("Although the Plan was rejected by a class of unsecured creditors, and does not pay such creditors in full, it may still be confirmed. Changes in 2005 to 11 U.S.C. § 1129(b)(2)(B)(ii) modified the [APR. . . to allow these Debtors to keep their business.").[3]

These cases find that the "broad interpretation" of Section 1115 includes post-petition property and earnings in addition to all property delineated in Section 541. One commentary on the conflicting application of the APR summarized the foundation of this interpretation, stating, "it would be 'illogical' to require individual debtors to devote five years of disposable income to their plans, but remove the debtors' means of providing that income, which would be the result if the application of the [APR] were to prevent debtors from retaining valuable prepetition business assets." Andrew G. Balbus, *Continued Disagreements Over the Application of the Absolute Priority Rule to Individuals in Chapter 11: Friedman and Maharaj*, 21 Norton Bankr. L. & Prac. 755, 761 (2012).

In re O'Neal	The Debtors' plan ultimately was not confirmed on grounds other than APR, including, that the plan (1) failed to specify certain creditors and the class to which they were assigned pursuant to Section 1123; (2) failed to properly classify claims under Section 1122; (3) was impossible to perform; and (4) was not proposed in good faith. In re O'Neal 2013 Bankr. LEXIS 1531, 21-23 (Bankr. W.D. Ark. Apr. 12, 2013). However, in reaching this outcome, the court also analyzed the application of the APR and found that Section 1115 defined all property of an individual Chapter 11 case. Id. at 34-36. Thus, with respect to individual debtors, the court found that amended Section 1129(b)(2)(B)(ii) eliminated the application of the APR from property described in Section 1115. Id. More specifically, the court found that "[t]o read Section 1115 and Section 1129(b)(2)(B)(ii) as exempting only future income from the APR renders ineffective any practical application of Section 1115, especially in light of the additional requirements of Section 1129(a)(15)(B)." Id. at 36. The court also reasoned "that since there does not appear to be any other logical reason for all of the changes made exclusively to Chapter 11 for individuals except to make it work like Chapter 13, this Court concludes that Congress did intend for Section 1115 to define all property of an individual Chapter 11 case (just as § 1322 does). Therefore, by the express terms of amended § 1129(b)(2)(B)(ii) the [APR] does not apply to any property of the estate of individual Chapter 11 debtors." Id. at 36-37.
In re Bullard	Where all requirements for plan confirmation had been satisfied pursuant to Section 1129(a), except for Section 1129(a)(8) because there were two non-accepting impaired classes, the court had to determine whether the Debtor could "cram down" said classes under Section 1129(b)(2)(B). In re Bullard, 358 B.R. 541 (Bankr. D. Conn. 2007). Under the Debtor's plan, he would retain income from his post-petition business activities, an automobile acquired post-petition, and assets claimed as exempt. Id. In subsequently confirming the plan, the court held that the post-petition

income and the automobile acquired post-petition were within the purview of Section 1115, the debtor's retention of the assets was not an impediment to plan confirmation, and Section 1129(b)(2)(B)(ii) permitted the Debtor to retain his exempt property and still confirm the plan. Id. at 544-545.

In re Shat

The only issue facing the bankruptcy court at the Debtors' confirmation hearing was whether the APR applied. In re Shat, 424 B.R. 854, 862 (Bankr. D. Nev. 2010). The court found that the estate property in an individual Chapter 11 case is comprised of all the property encompassed by Section 541, in addition to post-petition income and other property acquired post-petition. Id. at 866. The court concluded that Section 1115 "absorbs and then supersedes Section 541 for individual chapter 11 cases," meaning that Section 1129(b)(2)(B)(ii)'s exception to the APR applies to all estate property, which was consistent with Chapter 11's rehabilitative goals. Id. at 865. Moreover, Shat found that in implementing the BAPCPA amendments, Congress intended to make individual Chapter 11 cases more like Chapter 13 cases and noted that Chapter 13 debtors are not subject to the APR. Id. at 868. The court ultimately confirmed the plan, despite being rejected by a class of unsecured creditors and failing to pay such creditors in full, finding that the BAPCPA amendments allowed the debtors to retain their property (i.e., a dry-cleaning business). Id. at 868.

Caselaw: APR Continues to Apply in Individual Cases

On the other side of this issue, the Fourth, Fifth, Sixth, Ninth, and Tenth Circuits, and several bankruptcy courts have held that the APR continues to apply in individual Chapter 11 cases. See e.g., In re Lindsey, 453 B.R. 886, 905 (Bankr. E.D. Tenn. 2011) ("In summary, the court agrees with those cases adopting the narrow interpretation, finding that §1115 supplements rather than supplants §541 with respect to individual Chapter 11 debtors. The absolute priority rule set forth in 11 U.S.C. §1129(b)(2)(B)(ii), therefore, continues to apply to individual Chapter 11 debtors.").[4]

Ice House Am., LLC v. Cardin

The Debtor's chapter 11 plan, which had been approved by the bankruptcy court, would have allowed him to retain all of his assets after paying off the loans they secure, while making a single payment of $124,000 towards Ice House's unsecured claim of $1.545 million. Ice House Am., LLC v. Cardin, 751 F.3d 734, 737 (6th Cir. 2014). The court found that "the absolute-priority rule continues to apply to pre-petition property of individual debtors in Chapter 11 cases. The plan confirmed here did not comply with the rule, and thus the plan's confirmation was error." Id. at 740. The court reasoned that "[t]he critical language in § 1129(b)(2)(B)(ii) is that 'the debtor may retain property included in the estate under section 1115.' And the key word within that language is 'included'. . . . The action described in 'included' is either 'to take in as a part, an element, or a member'. . . . Thus—employing this definition and converted into the active voice—§ 1129(b)(2)(B)(ii) provides that 'the debtor may retain

property that § 1115 takes into the estate." Id. at 738-39. "Section 1115 cannot take into the estate property that was already there. . . .Thus, it is only *that* property—property acquired after the commencement of the case, rather than property acquired before then—that 'the debtor may retain' when his unsecured creditors are not fully paid." Id. at 739.

Zachary v. Cal. Bank & Trust

In this Ninth Circuit decision, the court overturned the holding of In re Friedman, 466 B.R. 471 (B.A.P. 9th Cir. 2012), and found that the APR continues to apply in individual Chapter 11 reorganizations. Zachary v. Cal Bank & Trust, 811 F.3d 1191, 1193 (9th Cir. 2016). Under the Debtors plan, their largest unsecured creditor, California Bank & Trust, was placed into its own class, and they proposed to pay it $5,000 on a claim of almost $2,000,000. Id. at 1193. California Bank & Trust objected, arguing that the plan violated the APR, and the bankruptcy judge agreed, disagreeing with the court in In re Friedman, 466 B.R. 471 (B.A.P. 9th Cir. 2012) which had held that the absolute priority rule did not apply in individual debtor Chapter 11 cases. Id. at 1193 and 473. The Ninth Circuit court agreed with the reasoning of the Ice House Am., LLC v. Cardin court stated above. Id. at 1197.

In re Lively

The Debtor proposed a reorganization plan that would allow him to retain all of his pre-petition property, while paying his unsecured creditors a small dividend that exceeded the liquidation value of his assets. In re Lively, 717 F.3d 406, 407 (5th Cir. 2013). The unsecured class voted overwhelmingly to approve the plan, but the majority class voted to reject it, thus requiring the court to determine whether the APR applies. Id. at 407. The court held that the APR applied to individual cases and failed to confirm the plan. Id. at 408. The Circuit Court agreed with the lower court that the "'narrow' interpretation is unambiguous and correct, and the exception to the absolute priority rule plainly covers only the individual debtor's post-petition earnings and post-petition acquired property. But even if the statutory language is ambiguous, then the 'narrow view' must prevail, because the opposite interpretation leads to a repeal by implication of the absolute priority rule for individual debtors." Id. at 409.

In re Woodward

The court held "that the absolute priority rule still applies in individual Chapter 11 cases to prevent debtors from retaining prepetition property. Our holding is supported by: (1) the language and context of § 1129(b)(2)(B)(ii) and 1115; (2) the absence of a clear indication by Congress of an intent to abrogate; and (3) the weight of existing authority." In re Woodward, 537 B.R. 894, 899 (B.A.P. 8th Cir. 2013). The court also noted that "[t]he majority of courts to address the issue. . .follow the 'narrow view'. . . . They have held, as we do today, that § 1115 merely augments existing estate property as set out in § 541 by drawing in

postpetition property and income. In fact, no circuit court has ruled otherwise." Id. at 901.

In re Maharaj

Since the Debtors' plan proposed to allow the Debtors to retain ownership of their business, as well as certain other assets, while paying unsecured creditors an estimated 1.7 cents on the dollar, the requirements for "cram-down" were not satisfied, and the plan could not be confirmed over its rejection by the class of unsecured creditors. In re Maharaj, 449 B.R. 484, 493 (Bankr. E.D. Va. 2011). After reviewing the "broad view" cases, the court reasoned that their interpretation that the BAPCPA amendments intended to "harmonize" Chapter 11 and Chapter 13 would have been "more straight-forwardly expressed by simply stating 'except that in a case in which the debtor is an individual, this provision shall not apply,' rather than by awkwardly referring to § 1115.'" Id. at 493(citation omitted). Moreover, the court noted that, "if Congress intended for Chapter 11 to operate the same as Chapter 13 in the case of an individual debtor, 'Congress would have simply amended the statutory debt ceilings for Chapter 13 cases set out in 11 U.S.C. § 109(e), and either eliminate them altogether or make them much higher.'" Id. With this framework, the lower court adopted the reasoning of the "narrow view" line of cases and denied plan confirmation. On appeal, the Fourth Circuit decided, "notwithstanding the ambiguity of the plain language of the relevant BAPCPA provisions, when the 2005 BAPCPA amendments are viewed in light of the specific context in which they were enacted and the broader context of the BAPCPA and the field of bankruptcy law, we arrive at the conclusion that Congress did not intend to alter longstanding bankruptcy practice by effecting an implied repeal of the [APR] for individual debtors proceeding under Chapter 11." In re Maharaj, 681 F.3d 558, 568 (4th Cir. Va. 2012). The court "conclude[d] that the [APR] as it applies to individual debtors in Chapter 11 has not been abrogated by BAPCPA, and … affirm[ed] the bankruptcy court's order denying plan confirmation." Id. at 575.

In re Lee Min Ho Chen

In this First Circuit decision by Judge Tester, the Debtor had claimed that the APR rule did not apply to individual Chapter 11 cases, and that even if it did, she was exempted from the rule's application because she would be providing new value to the bankruptcy estate under her plan. In re Lee Min Ho Chen, 482 B.R. 473, 476-477 (Bankr. D.P.R. 2012). Specifically, the Debtor contended that the court should adopt a broad interpretation of the APR where Section 1115 includes pre-petition property specified in Section 541, as well as post-petition earnings. Id. The Debtor also claimed that "even if the court adopts the narrow view, the new value exception applies because she is voluntarily contributing all her valuable exempt assets such as her vehicles and post-petition wages to fund her Plan. Thus, the Debtor is providing new value to the estate in order to contribute to the

Plan." Id. "Courts have construed the new value exception. . . to find that an interest holder in a chapter 11 debtor whose plan violates the [APR] may nonetheless in some instances retain such pre-petition property interest because that interest holder provides 'new value' to the debtor in the form of new capital or other similar fresh contributions". Id. at 484. The court recognized that this exception may not apply but, if it did, the Debtor would have to demonstrate that the contributed capital is "new, substantial [and] necessary for success of the plan, reasonably equivalent to the value retained, and in the form of money or money's worth." Id. Here, Judge Tester found that the Debtor failed to meet the requirements of the APR (adopting the narrow view) and failed to contribute new value to the plan that is derived from a source other than herself. Id. at 484-85. As a result, plan confirmation was denied. Id. at 485.

In re Stephens

At the confirmation hearing of the Debtor's proposed plan, the court analyzed whether the plan met the standards of Section 1129(a)(8). In re Stephens, 704 F.3d 1279, 1287 (10th Cir. Okla. 2013). The proposed plan provided for the individual Chapter 11 Debtor to retain non-exempt property of an aggregate value of almost $400,000 while paying less than 100% to a non-accepting class of unsecured creditors resulting in the largest unsecured creditor receiving 1% of its unsecured claim. Id. at 1282. The Tenth Circuit ultimately reversed the bankruptcy court's order confirming the plan, holding that the BAPCPA exempted individual Chapter 11 debtors from the APR and, thus, the plan violated Section 1129(b)(2)(B)(ii). Id. at 1287. Citing conflicting caselaw on the legislative history of Section 1115, and because both the statutory language and Congressional intent was ambiguous, the court heeded the presumption against implied repeal of the APR. Id. The court found that the statutory language and legislative history lacked any clear indication that Congress intended to erode a "pillar of creditor bankruptcy protection." Id.

In re Draiman

The bankruptcy court adopted the narrow view, holding that Section 1129(b)(2)(B)(ii) limits the application of the APR by allowing an individual to retain only the property that is added to the estate by Section 1115. In re Draiman, 450 B.R. 777, 2011 Bankr. LEXIS 1471, at *37 (Bankr. N.D. Ill. Apr. 19, 2011). "Congress did not explicitly eliminate the [APR] for individual Chapter 11 debtors. The cases that have held that the absolute priority rule has been eliminated have done so because they found § 1115 absorbs § 541, representing the entire definition of the bankruptcy estate. Section 1115 explains that certain post-petition property and earnings are 'include[d]' in the bankruptcy estate in addition to the property set forth in § 541. This Court's reading of § 1115 is that it adds property to the debtor's estate which has already been established by § 541. Thus, § 1115 consists only of the property set forth in subsections (1) and (2) of § 1115(a)." Id. at *37.

In re Walsh

In this Chapter 11 proceeding, a trust that held both secured and unsecured claims filed a limited objection to the Debtor's plan. In re Walsh, 447 B.R. 45, 47 (Bankr. D. Mass. 2011). The court held that "Section 1115 deals with something more than post-petition income from services [as focused on in Shat]—it also brings in property described in section 541 but which is acquired post-petition. . . . [B]ecause it deals with post-petition section 541(a) property (a most awkward construction), Section 1115 does not include section 541(a) property as such." Id. at 45. The court rejected the Debtor's claim that the APR did not apply to the plan and found that, "assuming the existence of a dissenting class, Debtor will be required to confirm her plan by satisfying Section 1129(b)" Id. at 49. Whether the Debtor met this requirement turned on an application of Massachusetts law regarding "dragnet clauses." Since the court was unable to determine the "valuation of the various items of collateral" without a resolution of the state law issue, the court scheduled a final evidentiary hearing. Id. at 50-51.

CONSTITUTIONAL ISSUES
11 U.S.C. § 303(a)

<u>Key concern:</u> **Is Section 303(a) of the Bankruptcy Code unconstitutional as applied to individual *involuntary* Chapter 11 debtors?**

Generally, Section 303(a) of the Bankruptcy Code provides that an involuntary case may be commenced under Chapter 11. In <u>Toibb v. Radloff</u>, 501 U.S. 157 (1991), the U.S. Supreme Court discussed constitutional concerns about involuntary "reorganization"

> …Congress' primary concern about a debtor's being forced into bankruptcy under Chapter 13: that such a debtor, whose future wages are not exempt from the bankruptcy estate, § 1322(a)(1), would be compelled to toil for the benefit of creditors in violation of the Thirteenth Amendment's involuntary servitude prohibition. See H. R. Rep. No. 95-595, at 120. Because there is no comparable provision in Chapter 11 requiring a debtor to pay future wages to a creditor, Congress' concern about imposing involuntary servitude on a Chapter 13 debtor is not relevant to a Chapter 11 reorganization. <u>Toibb</u>, 501 U.S. at 165-66.
>
> The legislative history referenced by the Court states:
> …Chapter 13 is completely voluntary. This committee firmly rejected the idea of mandatory or involuntary Chapter XIII in the 90th Congress. The Thirteenth Amendment prohibits involuntary servitude. Though it has never been tested in the wage earner plan context, it has been suggested that a mandatory Chapter 13 by forcing an individual to work for creditors would violate this prohibition.

H.R. Rep. No. 95-595, 95th Cong. 1st Sess. 322 (1977), at 120; S. Rep. No. 95-989, 95th Cong. 2d Sess. 94 (1978) at 32.

Using this framework, some debtors have claimed that certain provisions of Chapter 11 may threaten an individual debtor's Constitutional rights. The list of potential provisions under Chapter 11 that, when invoked in an involuntary filing, may violate an individual debtor's Constitutional rights include:

(i) Section 1115(a)(2), which expands the definition of property of the estate to include "earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 12, or 13, whichever occurs first"; Section 1115 in conjunction with Section 1123(a)(8) require that debtor utilize his post-petition earnings (i.e., future income) for execution of a confirmed plan.

(ii) Section 1129(a)(15)(B) requires that if the holder of an unsecured claim objects to confirmation of the plan, "the value of the property to be distributed under the plan is not less than the projected disposable income of the debtor" that the debtor receives for a least five years following confirmation.

(iii) The debtor has no absolute right to dismiss or convert his case pursuant to Section 1112(a)(1-3) since the Chapter 11 case was not voluntarily selected by the debtor.
(iv) A creditor can propose a plan under Section 1121(c).
(v) The APR may require the debtor to surrender his house and other personal possessions.
(vi) Section 1141(d)(5) precludes entry of a discharge until all payments due under the plan have been completed.
(vii) The court may find the debtor in contempt for failure to comply with any confirmed plan and such contempt may be punishable by fine or jail.

Caselaw:

While Section 303(a), as applied to involuntary Chapter 11 individual debtors may raise consititutional issues, no case has yet found involuntary Chapter 11 individual cases to be unconstitutional.

In re Gordon: While opposing a conversion from Chapter 7 to Chapter 11, the Debtor challenged the application of Section 706(b) as being in violation of the Thirteenth Amendment's prohibition on involuntary servitude. In re Gordon, 465 B.R. 683, 696-697 (Bankr. N.D. Ga. 2012). In examining the scope of involuntary servitude under the Thirteenth Amendment, the Court cited the Second Circuit in reasoning: "courts have consistently found the involuntary servitude standard is not so rigorous as to prohibit all forms of labor that one person is compelled to perform for the benefit of another. The Thirteenth Amendment does not bar labor that an individual may, at least in some sense, choose not to perform, even when the consequences of that choice are 'exceedingly bad.'" Id. at 698 (citing Immediato v. Rye Neck School Dist., 73 F.3d 454 (2nd Cir. 1996)). The Debtor argued that converting his case from Chapter 7 to Chapter 11 constituted involuntary servitude in that "there is the potential for a number of provisions in Chapter 11 to be invoked." Id. However, the Court ultimately decided the case on standing grounds, finding that while "11 U.S.C. § 706(b) permits the Court to convert an individual non-consumer debtor's case from Chapter 7 to Chapter 11 and the act of conversion alone does not violate the Thirteenth Amendment. . . . Many of the. . . potential constitutional violations have not yet occurred, may not occur, and would only occur on subsequent order of the Court." Id. at 703. Therefore, the Debtor's claims were not ripe for decision, and he lacked standing to raise them. Id. at 703-04. Nonetheless, the court did note the "[t]he only effect of converting the case under Section 706(b) is that the Debtor's post-petition earnings become property of the estate, which means that, if he wishes to use those post-petition earnings for non-typical purposes, a request for approval to spend the money must be filed with the bankruptcy court and the use must be approved." Id. at 697; 11 U.S.C. § 363; See also Id. (The Debtor also must file certain operating reports with the U.S. Trustee and pay a U.S. Trustee's fee.).

In re Marciano: An involuntary Chapter 11 petition was filed against the Debtor by a group of creditors that had obtained state court judgments against him. The judgments were entered as sanctions for the Debtor's discovery abuse. In re Marciano, 446 B.R. 407 (Bankr. C.D. Cal. 2010). One of the Debtor's objections to the involuntary petition was that the Bankruptcy Code provisions "which authorize the filing of an involuntary Chapter 11 petition against an individual debtor violate the Thirteenth Amendment prohibition against involuntary servitude." In re Marciano, 459 B.R. 27, 38-39 (B.A.P. 9th Cir. 2011). More specifically, the Debtor argued that the application of Section 1115(a)(2) in an involuntary individual Chapter 11 case would violate the Thirteenth Amendment. Id. at 39. This challenge, however, was weakened by the Debtor's declaration that he did not have any earnings from post-petition income. Id. Regardless, both the bankruptcy court and the Bankruptcy Appellate Panel failed to reach the constitutional issue, determining that the issue was not ripe. Both courts ruled that until the entry of an order of relief against the Debtor, the constitutionality of Section 1115 could not be challenged. "[T]he time to determine whether [debtor] had "earnings from personal services" that might constitute property of the estate was after an order for relief was entered. . . unless and until an order for relief was entered in the case, the constitutional issue raised by [Debtor] was not ripe." Id. at 40.

Although caselaw on this issue has been limited, legal commentary has been more active. In a law review article, Margaret Howard discusses how the BAPCPA Amendments created Thirteenth Amendment concerns by creating a statutory system where a debtor can be involuntary involved in an individual Chapter 11 proceeding. Margaret Howard, *Bankruptcy Bondage*, 2009 U. Ill. L. Rev. 191, 234, (2009). She notes that this is same statutory configuration that was rejected in 1978 Bankruptcy Code discussions, partly on constitutional grounds. Id. at 192.

In another article, Anne Lawton presents findings from 370 individual Chapter 11 debtor cases in an effort to analysis the impact of the BAPCPA. Anne Lawton, *Musings on BAPCPA and the Individual Chapter 11 Debtor*, 90 Am. Bankr. L.J. 307 (2016). The data shows that post-BAPCPA individual involuntary Chapter 11 cases are exceedingly rare, with involuntary Chapter 11 filings comprising less than 1% of all Chapter 11 cases for fiscal years 2009 through 2013. Id. at 309-310. The data also shows that individual Chapter 11 debtors generally do not fare well, with fewer than 3 in 10 reaching plan confirmation. Id. at 326.

ATTORNEY CLIENT PRIVILEGE ISSUES

Key concern: An individual debtor's fiduciary duty to creditors to act in the best interests of the bankruptcy estate is often at odds with their own interests.

Chapter 11 debtors owe a fiduciary duty to their creditors to act in the best interests of their bankruptcy estate.[5] The Bankruptcy Code permits Chapter 11 debtors to remain in possession of their assets and business operations[6] as, in short, a debtor-in-possession (DIP) to ensure that the creditors are paid.[7] Courts interpreting the DIP provisions of the Bankruptcy Code have universally held that *individual* Chapter 11 debtors owe the same fiduciary duties as corporate DIPs.[8] In other words, the individual Chapter 11 debtor must put the interests of his creditors ahead of his or her own interests, and must actively work to benefit the bankruptcy estate even when that would disadvantage him/her.

This generally means that, "[w]ith respect to an individual Chapter 11 debtor, the interests of the estate and of the debtor may not always coincide. For example, if the estate is insolvent, then each dollar paid for administrative expenses reduces the distribution to other creditors. If the estate is solvent, then each dollar paid to creditors reduces the amount to be retained by the individual debtor at the conclusion of the case." In re Graves, 2008 Bankr. LEXIS 3244 (Bankr. S.D. Tex. Sept. 4, 2008).

Caselaw:

Several cases demonstrate the issues that may arise when *individual* Chapter 11 debtors are held to the same fiduciary standard as corporate DIPs.

In re Johnson — The Debtor, a professional hockey player with the Columbus Blue Jackets, filed a voluntary petition for relief under Chapter 11. In re Johnson, 546 B.R. 83, 88 (Bankr. S.D. Ohio 2016). During his Chapter 11 proceedings, the court reminded the Debtor of the fiduciary duties he owed to his creditors. Id. at 88. Those fiduciary duties include the duty to preserve his earnings by controlling his expenses, and supporting his parents and brother is a clear violation of that duty. Id. at 143 and 146. The court noted that the Debtor's "sense of responsibility for his brother—while certainly understandable—does not trump his fiduciary duty to creditors. . . . While his willingness to support his brother may have been laudable, the Debtor has no responsibility to ensure that his brother lived in a half-million dollar home or that he continued to attend an expensive private high school." Id. at 146.

In re Bownan: — A Chapter 7 Debtor objected to the trustee's settlement of a lawsuit for an amount that would pay the Debtor's creditors in full but not produce any distribution to the Debtor. In re Bownan, 181 B.R. 836, 841 (Bankr. D. Md. 1995). The Debtor exercised her right to convert her case to a Chapter 11 proceeding. Id. The court granted the Debtors' motion but immediately reconverted the case to a Chapter 7 proceeding, finding the Debtor's insistence on further litigation of her claim was a violation of her fiduciary

duty as a Chapter 11 DIP. Id. at 845-46. The court reasoned that "in this case when debtor must weigh whether to accept a prompt settlement that would substantially pay her creditors or to wait and gamble on a potential to receive a greater recovery, *her creditors' interests have a higher priority than the debtor's own; and they must take precedence*. Debtor's own statement that she 'intends to proceed with litigation, through trial,' indicates her unwillingness to examine other interests above hers. But there is more to the conflict than mere unwillingness, it is an inherent conflict of interest between her duty as a fiduciary to the estate and her desire to maximize the amount of money she may recover for herself." (emphasis added.) Id. at 845; See also, In re Tel-Net Hawaii Inc., 105 B.R. 594, 595 (Bankr. D. Haw. 1989) (the court removed the DIP who was the corporation's controlling shareholder due to its failure to pursue preference actions that would have increased its exposure on guaranteed debts and appointed an independent trustee.)

Key concern: Who holds the attorney client privilege in an individual Chapter 11 case?

While highly litigated, the lower courts generally follow three distinct lines of reasoning regarding who holds the attorney client privilege prior to and during a Chapter 11 bankruptcy case.

The first line holds that an individual Chapter 11 debtor holds the attorney/client privilege, for both pre- and post-bankruptcy periods, without passing the privilege to the bankruptcy estate or a later appointed trustee. See In re Hunt, 153 B.R. 445 (Bankr. N.D. Tx 1992) (trustee under confirmed plan was not entitled to waive privilege.); In re SIDCO, Inc., 173 B.R. 194 (E.D. Cal 1994) (attorney's independent duty to estate exists only in unusual circumstances; basic tenet is that attorney has fiduciary duty only to client, the DIP.).

The second line of reasoning finds that the privilege passes from the individual to his bankruptcy estate. By focusing on the individual DIP's duty to his creditors to benefit the estate, these courts find that either the transfer or the waiver of the privilege furthers that duty. See e.g., Ramette v. Bame (In re Bame), 251 B.R. 367 (Bankr. D. Minn. 2000) (holding that the trustee succeeded to privilege regarding all communications that were relating to estate administration and that took place while the debtor was a debtor in possession.); See also In re Miller, 2000 Bankr. LEXIS 355, 357 (N.D. Ohio Feb 1, 2000) (reasoning that bankruptcy trustee, as a matter of law, superceeded the attorney-client privilege of an individual debtor (citing In Re Smith, 24 B.R. 3, 4 (Bankr. S.D. Fla 1982.). At least one court reasoned that "[t]he unique circumstances which surround insolvency and the filing of a Chapter 11 case place the attorney for the debtor in possession in the unusual position of sometimes owing a higher duty to the estate and the bankruptcy court than to his client. . . . The attorney for a debtor in possession is not merely a mouthpiece for his client." In re Sky Valley, Inc., 135 B.R. 925, 938-39 (Bankr. N.D. Ga. 1992).

The third, and most widespread, reasoning is that the determination of who holds the privilege must be done on a case by case basis—the court must balance both the policies underlying the privilege, the harm of disclosure and the trustee's duty to maximize the value of the estate. In re Benum, 339 B.R. 115, 135 (Bankr. D.N.J. 2006).

SUMMARY OF MAJOR DIFFERENCES BETWEEN CHAPTER 13 AND CHAPTER 11 FOR INDIVIDUALS

	Chapter 13	**Chapter 11**
ELIGIBILITY LIMITS	§109(e) – secured debt $1,184,200, unsecured debt $394,725	No eligibility limits
DEBTOR'S DISMISSAL/ CONVERSION AS OF RIGHT	§1307 – conversion and dismissal as of right except for bad faith or abuse of process	§1112 – conversion as of right with limited exceptions, dismissal only upon motion and court order
CODEBTOR STAY	§1302 - yes	None by statute, possible upon motion and court order
DISCHARGE GENERALLY	§1328 – 523(a)(1)(A) tax debts (although all priority claims must be paid within plan term), §523(a)(10) – (19) (although adversary proceeding required). Includes §523(a)(15) non-domestic support obligations	§1141(d)(2) – no discharge of any debt listed under §523
PLAN DURATION	§1322(d) – 3 to 5 years depending on Statement of Income	No minimum or maximum duration of plan
PLAN CONFIRMATION	§1325 – must meet requirements and address objections but no balloting	§1129 – must have one impaired accepting class and either 1) all creditor classes affirmatively vote in favor of plan, or 2) must comply with §1129(b). Must also address any objections
APPLICABILITY OF MEANS TEST	§1325(b) – if party in interest objects	§1129(b)(15) – if unsecured creditor objects, and then only for first five years of plan
PRACTICAL CONCERNS	• Much less expensive • Less debtor involvement • Creditors do not vote on plan	• Much more expensive • Demands much higher debtor involvement , especially in first stages of case • Need for affirmative votes in favor of plan can be problematic

[*] Section references are to 11 U.S.C. § 101 et seq.

Endnotes

[1] See Toibb v. Radloff, 501 U.S. 157, 160-61, 166 (1991) ("While Chapter 11 of the Bankruptcy Code is primarily intended for debtors with ongoing businesses, an individual debtor not engaged in business may seek "reorganization" relief under Chapter 11.").

[2] Notably, even before BAPCPA, courts did not agree whether an individual debtor could cram down a plan over the dissent of a class of unsecured creditors. See Bruce A. Markell, *Symposium: Consumer Bankruptcy And Credit In The Wake Of The 2005 Act: The Sub Rosa Subchapter: Individual Debtors In Chapter 11 After BAPCPA*, 2007 U. Ill. L. Rev. 67, 88-89 (2007); 11 U.S.C.A. § 1129(a)(15), (b)(2)(B). Moreover, courts were split as to whether individual debtors could retain any property without paying their unsecured creditors in full—Compare In re Gosman, 282 B.R. at 53 with In re Henderson, 321 B.R. 550, 561 (Bankr. M.D. Fla. 2005); aff'd, VanBuren Indus. Investors v. Henderson (In re Henderson), 341 B.R. 783 (M.D. Fla. 2006) (individual debtor can retain exempt property without violating the APR; See also, In re Shin, 306 B.R. 397, 404 & n.17 (Bankr. D.D.C. 2004) ("to apply the absolute priority rule to an individual debtor's wholly exempt property stands the [APR] on its head--affording to unsecured creditors an artificial 'priority' in exempt property that unsecured creditors simply do not possess." (citing West's Bankruptcy Law Letter (October 2002))).

[3] See also, SPCP Grp., LLC v. Biggins, 465 B.R. 316 (M.D. Fla. 2011) (affirming unpublished decision of bankruptcy court.); In re Johnson, 402 B.R. 851 (Bankr. N.D. Ind. 2009); In re Roedemeier, 374 B.R. 264 (Bankr. D. Kan. 2007); In re Tegeder, 369 B.R. 477 (Bankr. D. Neb. 2007).

[4] See In re Maharaj, 681 F.3d 558 (4th Cir. 2012) (affirming the bankruptcy court's decision in 449 B.R. 484 (Bankr. E.D. Va. 2011.); In re Lee Min Ho Chen, 482 B.R. 473, 2012 WL 5463256 (Bankr. D. P.R. 2012); In re Tucker, 479 B.R. 873 (Bankr. D. Or. 2012); In re Arnold, 471 B.R. 578 (Bankr. C.D. Cal. 2012); In re Lively, 467 B.R. 884 (Bankr. S.D. Tex. 2012); In re Borton, No. 09-00196-TLM, 2011 Bankr. LEXIS 4310, 2011 WL 5439285 (Bankr. D. Idaho Nov. 9, 2011); In re Lindsey, 453 B.R. 886 (Bankr. E.D. Tenn. 2011); In re Kamell, 451 B.R. 505 (Bankr. C.D. Cal. 2011); In re Draiman, 450 B.R. 777 (Bankr. N.D. Ill. 2011); In re Walsh, 447 B.R. 45 (Bankr. D. Mass. 2011); In re Stephens, 445 B.R. 816 (Bankr. S.D. Tex. 2011); In re Karlovich, 456 B.R. 677 (Bankr. S.D. Cal. 2010); In re Gelin, 437 B.R. 435 (Bankr. M.D. Fla. 2010); In re Steedley, 2010 Bankr. LEXIS 3113 (Bankr. S.D. Ga. Aug. 27, 2010); In re Mullins, 435 B.R. 352 (Bankr. W.D. Va. 2010); In re Gbadebo, 431 B.R. 222 (Bankr. N.D. Cal. 2010).

[5] See gen. In re Cenargo Int'l, PLC, 294 B.R. 571, 599 & n.32 (Bankr. S.D.N.Y. 2003) ("There is no question that a debtor in possession is a fiduciary, like a chapter 11 trustee, for the estate, creditors and shareholders."); Commodity Futures Trading Comm'n v. Weintraub, 471 U.S. 343, 355 (1985) (directors of a corporate debtor in possession "bear essentially the same fiduciary obligation to creditors and shareholders as would the trustee for a debtor out of possession."). In re Waters, 2008 Bankr. LEXIS 374 at *5 & n.6 (Bankr. D. Conn. Feb. 8, 2008) ("A chapter 11 debtor in possession is the equivalent of a trustee…and is a fiduciary for the estate and its creditors.") (citations omitted).

[6] See In re Eurospark Indus., 424 B.R. 621, 627 (Bankr. E.D.N.Y. 2010); In re Adelphia Commc'ns. Corp., 336 B.R. 610, 655 (Bankr. S.D.N.Y. 2006).

[7] See In re Bowman, 181 B.R. 836, 843 (Bankr. D. Md. 1995) (citing Grayson-Robinson Stores, Inc. v. Securities Exchange Comm'n, 320 F.2d 940 (2d Cir. 1963)); In re Tricycle Enters., 2006 Bankr. LEXIS 4261 (Bankr. N.D.N.Y. Mar. 29, 2006) ("the creditors' interests take precedence over those of the Debtor."); Guttman v. Assocs. Commer. Corp. (In re Furley's Transp., Inc.), 272 B.R. 161, 176 (Bankr. D. Md. 2001) ("A debtor-in-possession's authority is constrained by its fiduciary responsibility to act in the best interest of the creditors of the estate, and not in its own interest.") (citations omitted).

[8] A DIP owes fiduciary duties to the bankruptcy estate, "includ[ing] a duty of care to protect the assets, a duty of loyalty and a duty of impartiality." In re Bownan, 181 B.R. 836, 843 (Bankr. D. Md. 1995) (citations omitted); Smart World Techs., LLC v. Juno Online Servs., Inc. (In re Smart World Techs., LLC), 423 F.3d 166, 175 (2d Cir. 2005) (stating that a debtor-in-possession's "duty to wisely manage the estate's legal claims is implicit in the debtor's role as the estate's only fiduciary"); see also, In re Hardy, 319 B.R. 5 (Bankr. N.D. Fla. 2004) (full disclosure of assets and of business transactions required.); In re Robino, 243 B.R. 472 (Bankr. N.D. Ala. 1999) (compliance with court orders.); In re Tornheim, 181 B.R. 161 (Bankr. S.D.N.Y. 1995) (duty to pay fees and file required reports.); In re Bownan, 181 B.R. 836 (Bankr. D. Md. 1995) (duty to put creditor interests first in settlement of a lawsuit.); In re Harp, 166 B.R. 740 (Bankr. N.D. Ala. 1993) (duty to properly account for estate property and to properly use estate funds.).

CONNECTICUT BANKRUPTCY CONFERENCE

OCTOBER 4, 2018

WESTBROOK, CONNECTICUT

ISSUES IN INDIVIDUAL CHAPTER 11 CASES

Honorable Ann M. Nevins

United States Bankruptcy Judge, District of Connecticut

Douglas S. Skalka

Neubert, Pepe & Monteith, P.C., New Haven, Connecticut

Scott Charmoy

Charmoy & Charmoy, Fairfield, Connecticut

Additional Materials

- Individual Chapter 11 Debtors – Key Issues Facing Individual Debtors (and Their Counsel) When Filing for Chapter 11 Relief
  - Prepared by Douglas S. Skalka, Esq.

- Summary of Major Differences Between Chapter 13 and Chapter 11 for Individuals
  - Prepared by Scott Charmoy, Esq.

Early Business Success

- Clark Kent was an entrepreneurial businessman who founded a popular newspaper, The Connecticut Daily aka “The Daily” in 1988.
- The Daily was owned and operated by Kent, LLC, a Connecticut limited liability company owned solely by Clark Kent.
- The Daily grew rapidly through the 1990s and early 2000s.

Expanding Operations and Lifestyle

- In 1999, as the business grew, Clark purchased a 50,000 square foot commercial office building in New Haven to house The Daily's operations.

- Because The Daily occupied the entire parcel of real estate Clark was able to get a favorable mortgage from his local lender, Gotham National Bank ("Gotham Bank"). Clark owned the commercial real estate in his own name.

- Clark purchased a 5,000 square foot house in Westbrook and gave Gotham a $2 million blanket mortgage on his house and commercial real estate. Kent, LLC guaranteed the Gotham Loan. As part of the Gotham loan, Clark provided Gotham with a conditional assignment of all rents and leases.

- Clark Kent and The Daily became well known throughout Connecticut. Clark was philanthropic. By day, he spent a great deal of time giving back to the community, while by night he was thwarting all criminal activity in the State.

The Internet, Social Media and Business Losses

- As a result of his busy schedule, Clark missed the major media shift to digital platforms.
- By 2015, The Daily had suffered significant reductions in print subscriptions and advertising revenue.
- Clark and The Daily were slow to invest in new technology and digital media opportunities.
- By 2018, The Daily had significant liquidity issues and Clark had reduced his compensation from The Daily by 50%.

Problems Pile Up

- To keep suppliers shipping to Kent, LLC, Clark personally guaranteed certain supplier agreements.
- In 2015, Clark loaned $250,000 to Kent, LLC; however, the parties never prepared formal loan documents.
- After nearly thirty years of wedded bliss, Clark's wife, Lois, left him in 2018 and commenced a divorce proceeding seeking alimony and a property division.
- Kent, LLC fell behind on employee withholding payment obligations. Clark was the only signatory on Kent, LLC's bank accounts.
- Clark stopped paying his credit card bills and accumulated over $500,000 in unsecured debts, including guarantee obligations.
- Ultimately, in 2018 Clark violated loan covenants with Gotham Bank and Gotham Bank sent a notice of default.

Meeting With Counsel

- Clark met with his long time attorney, Jimmy Olsen.
- Jimmy had represented both Clark and Kent, LLC for many years.
- During the meeting, Jimmy realized the severity of the situation and discussed the possibility of an individual chapter 11 bankruptcy filing for Clark.

QUESTIONS:

Attorney/Client Issues:

a. What issues will Jimmy and Clark have to deal with regarding Jimmy's prior legal services?

b. What issues will Jimmy, Clark, and Kent, LLC have to deal with in connection with the scope of the attorney-client privilege if Clark seeks to retain Jimmy as his counsel in an individual chapter 11 bankruptcy proceeding?

Bankruptcy Planning – Other Professional Services Necessary

- Jimmy suggests a meeting with Clark's accountant to prepare for the possibility of a Chapter 11 filing.
- At that meeting, Jimmy realizes that the accountant is under-qualified and is owed money for services provided to Kent, LLC.
- The accountant is also Clark's brother-in-law (or, soon to be ex-brother-in-law).
- At Jimmy's urging, Clark meets with a new accountant with experience in Chapter 11 proceedings.

QUESTIONS :

a. Before filing, has the client been advised about the issues regarding prior professional (legal/accounting) representation the United States Trustee's office may review during the Chapter 11 case?

b. Before filing, has the client been advised about the breadth of disclosure required and the ongoing administrative burdens inherent in an individual Chapter 11 case?
    1) Monthly Operating Reports
    2) Accountant's Fees
    3) United States Trustee's Office Fees

Filing – First Day Issues

- Approaching Gotham Bank for use of cash collateral and support for the Debtor
- The Cash Collateral Budget: Adequate Protection Issues
- Addressing and Resolving the "insider issues"
  - Is Kent, LLC paying a market-based rent?
  - Is Clark's compensation from Kent, LLC reasonable?
  - Are Clark's living expenses reasonable and necessary?
- What is Lois' role in the case? Lois is not cooperating and is reluctant to produce information regarding her income or expenses.

Operations During Chapter 11

- Gotham Bank agrees to a monthly budget including Clark's living expenses and cash collateral issues are resolved.
- The U.S. Trustee appoints a Committee.
- The Committee consists of:
  - Kent, LLC's largest vendor - "Mega Paper"
  - Kent, LLC's primary trucking company – "Luthor's Shipping" (owned by Clark's nemesis, Lex Luthor)
  - Larry the Landscaper, the gardener who maintains Clark's Westbrook home

Clark's Actions in the Chapter 11 Case

- Clark takes the lead on looking for investors to fund a Chapter 11 Plan.
- Jimmy learns that Clark has told potential investors in Kent, LLC that he will require certain benefits to consider offers, including an employment contract with severance benefits
- Clark talks with his long time friend Perry White to serve as his real estate broker and market both the commercial real estate and his Westbrook home. Perry is 85 years old and has not sold a piece of Connecticut real estate as a broker since 1993.

QUESTIONS:

What should Jimmy do about Clark's discussions and how can he deal with Clark?

- When does Jimmy have an affirmative obligation to inform the Court or the U.S. Trustee about strategic decisions being made during Clark's case, including the relative qualifications of the proposed real estate agent?

Lackluster Chapter 11 Operations

- Post-petition operations for Kent, LLC are deteriorating, and Jimmy believes a sale of all assets is needed to avoid conversion of Clark's case.
- Committee member, Mega Paper, expresses interest in purchasing Kent, LLC and acting as a stalking horse bidder.
- Mega Paper provides Clark with a term sheet with aggressive bidding procedures and says "take-it-or-leave-it".

Post-petition financial challenges

- Vendors are reluctant to provide/extend credit terms to Kent, LLC, cash is tight, making it difficult to produce The Daily.
- Key employees at Kent, LLC are starting to leave for new opportunities.
- Clark is earning a reasonable salary and requires it to meet his personal financial obligations, but Kent, LLC is having difficulty paying his salary.
- Clark's new accountant advises him that the tax basis in his real estate is roughly 25% of the current fair market value of the real estate exposing him to significant capital gains tax liabilities.

QUESTION:

How can Debtor's Professionals get a sale on track in light of Clark's actions, Clark's capital gains tax issues, and Mega Paper's hard line on sale terms?

Transition to a Sale of Kent and Clark's Real Estate

- Dealing with Clark
  - Reminder of obligations to creditors
  - Risk of losing control absent a credible process
- Dealing with Mega Paper
  - Sale terms and procedures need to be credible
- Dealing with Creditors – Gotham Bank and Committee
- Setting up the sale to succeed
  - Transparency of process
  - Reasonable speed; access to information for competitive bidders

A White Knight Emerges

- At the last moment, technology billionaire Bruce Wayne of Wayne Enterprises decides to diversify and enter the local newspaper marketplace to "disrupt" the industry.
- His goal is to develop a huge social media marketplace in Connecticut for The Daily.
- Bruce recognizes, however, that he needs Clark to succeed and is prepared to give him an employment contract.
- Rather than a sale, Bruce proposes to fund Kent, LLC's operations for the purpose of confirming a plan.

Plan – Issues

- As part of Plan negotiations with the Committee, the Committee wants Clark to resolve his divorce proceedings with Lois as quickly as possible. Clark is still hoping for reconciliation with Lois.
- Clark wants his discharge as soon as possible.
- The Plan proposed will provide only a speculative recovery for unsecured creditors based upon Kent, LLC's performance, but will fully pay Gotham Bank and priority tax claims (benefitting Clark).
- The Committee sees no equity available to unsecured creditors from Clark's real estate and threatens a conversion to chapter 7.

What are some practical ways to satisfy the Committee and obtain support for the Plan?

Reconciling with the Committee

- Use of expedited discovery to facilitate resolution
- Negotiations with a goal to resolve the issues:
  - A settlement as part of the plan
  - Bruce to enhance the dividend to unsecured creditors?
  - Clark contribution through voluntary reduction of his salary?
- Absolute priority rule issues
  - Can the Plan satisfy 11 U.S.C. 1129 (a)(15)?

THANK YOU FOR ATTENDING
THIS PRESENTATION ON INDIVIDUAL
CHAPTER 11 BANKRUPTCY ISSUES

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The First Annual
Connecticut Bankruptcy Conference

October 4, 2018
Water's Edge Resort and Spa

Non-Profits in Bankruptcy

Panel:
Honorable James J. Tancredi
Craig Lifland, Esq., Halloran & Sage, LLP
Robert A. White, Esq., Murtha Cullina, LLP

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OVERVIEW

The non-profit sector is a major contributor to the economy at an estimated $906 billion annually. Over the past ten years the number of public charities has grown nearly 20% to a total of one million non-profits. The sector employs 13.7 million people. Just like for-profit corporations, non-profits can face financial distress and may need to file bankruptcy. These materials address some of the unique issues presented in a bankruptcy or workout of a non-profit.

HALLORAN SAGE

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CBA's First Annual Bankruptcy Conference
October 4, 2018

Non-Profits in Bankruptcy

Asset Sales

The unique nature of non-profits and the public interest being served by them permits the board of a non-profit debtor more latitude in choosing a purchaser that is more in keeping with the mission and goals of the non-profit. In entertaining any offer from a prospective buyer, a non-profit debtor is charged with the fiduciary duties to act in furtherance of the organization's charitable mission while also acting in the best interests of creditors. *See In re United Healthcare Sys., Inc.*, No. 97-1159, 1997 WL 176574 (D. N.J. Mar. 26, 1997). Federal bankruptcy law typically trumps contrary state law and often allows certain transactions to occur in bankruptcy that would not be able to occur outside of bankruptcy. Certain amendments to the Bankruptcy Code in 2005, however, made transfers of assets of a non-profit debtor in bankruptcy expressly subject to compliance with applicable non-bankruptcy law, including the laws of the relevant state(s) with jurisdiction over the debtor and its assets.

Courts have looked to state law even before the 2005 amendments were adopted. For example, under Pennsylvania law, the board of an non-profit, in discharging its duties, may consider, among other things, (i) the effects of the action on various constituencies and the communities where the non-profit is located, (ii) the short-term and long-term interests of the non-profit, and (iii) the resources, intent and conduct (past, stated and potential) of the potential purchaser. *See* 15 Pa. Cons. Stat. § 5715(a). Therefore, in analyzing offers for the sale of its assets in bankruptcy, the debtor should appropriately consider how its charitable mission and the public interest will be furthered by each proposed purchaser. *In re United Healthcare Sys., Inc.*, 1997 WL 176574, at *5; *In re Brethren Care of South Bend, Inc.*, 98 B.R. 927, 935 (N.D. Ind. 1989) (holding that ongoing beneficial treatment of the residents of the retirement and nursing facility was a good business consideration in the sale decision).

It may be the case that the bidder submitting an offer for the most consideration (in terms of purchase price) will not be the "highest and best" offer if that purchaser cannot appropriately demonstrate that the debtor's charitable mission and the public interest will be furthered by the sale transaction. In the case of *In re United Healthcare System, Inc.*, a non-profit entity conducted a sale process with respect to the Children's Hospital of New Jersey. In deciding which bidder to select, the non-profit's board of trustees was advised by its financial advisor to consider four factors, with price ranking last in importance. The non-profit selected the winning bid based on, among other things, the purchaser's: (i) ability to further the hospital's charitable mission, (ii) assurance that it would keep the hospital in one location, which was a concern for the Commissioner of Health and Senior Services of New Jersey, and (iii) commitment to provide $5 million in future investments. The bankruptcy court, however, declined to approve the sale transaction, finding that the debtor's board of trustees did not exercise sound business judgment in selecting a bidder that the court believed was offering lower consideration than another offeror. *In re United Healthcare Sys., Inc.*, 1997 WL 176574, at *3.

On appeal, the district court noted that "[w]hen analyzing an articulated business reason for the sale, the bankruptcy court must also take into consideration the fact that a debtor is a charitable entity . . . . The officers and directors of a nonprofit organization are charged with the fiduciary obligation to act in furtherance of the organization's charitable mission." The district court noted that purchase price alone should not be used to determine the best offer for a non-profit's assets, and the bankruptcy court was too focused on the monetary aspects of the competing bids. Instead, the "overriding consideration of public health" must be considered. In addition, the purchaser's ability to further the debtor's charitable mission must be analyzed, as the district court found that the bankruptcy court failed to acknowledge that the non-profit's board of trustees "had a fiduciary obligation to maintain the legacy of the Children's Hospital." The district court ultimately determined that the non-profit's board of trustees exercised sound business judgment in approving the original sale, notwithstanding the lower purchase price, and reversed the bankruptcy court's order.

OTHER CASES

Second Circuit

- *In re HHH Choices Health Plan, LLC*, 554 B.R. 697 (Bankr. S.D.N.Y. 2016) (approval of sale of substantially all of assets of debtor not-for-profit corporation that provided senior housing to first bidder, rather than to competing bidder, given that different effects of the different proposals on general unsecured creditors were negligible, at most, first bidder's proposal was more consistent with the mission of the company, first bidder's proposal was consistent with board of directors' decision, which was entitled to some deference, and while the competing bidder's proposal may have been better for some current residents, on the whole, the current residents' interests were better served by the first bidder's proposal)

Other Courts

- *In re Valley Health System*, 429 B.R. 692 (Bankr. C.D. Cal. 2010) (debtor's board of directors did not have fiduciary duty precluding it from approving asset sale agreement

that contained unconditional “no shop” provision barring solicitation or consideration of new or alternative bids for assets absent breach or default by purchaser)

- *In re Fam. Christian, LLC*, 533 B.R. 600 (Bankr. W.D. Mich. 2015) (court could not approve proposed sale, to corporate insider, of substantially all of debtors' assets, even though sale had overwhelming support of all of debtors' major stakeholders, and though, in absence of prompt sale, it was unlikely that debtors would be able to continue as going concerns)

Role of the Attorney General

States have empowered their attorney generals, either through statute or the common law, as representative of the public, to protect the interests of the public in the operations of the charitable entity and the disposition of assets of the charitable entity. As mentioned above, federal bankruptcy law typically trumps contrary state law and often allows certain transactions to occur in bankruptcy that would not be able to occur outside of bankruptcy. Certain amendments to the Bankruptcy Code in 2005, however, made transfers of assets of a non-profit debtor in bankruptcy expressly subject to compliance with applicable non-bankruptcy law, including the laws of the relevant state(s) with jurisdiction over the debtor and its assets. Under Section 363(d), the trustee may sell, use or lease property of a nonprofit debtor outside of the ordinary course of business. Any such sale, however, is expressly conditioned upon compliance with "applicable non-bankruptcy law that governs the transfer of property by a corporation or trust that is not a moneyed, business, or commercial corporation or trust". 11 U.S.C. § 363(d). This provision of the Code may require the trustee to obtain the permission of a state attorney general, or a regulatory arm of the state, such as the department of health, before selling assets. Section 1129(a)(16) of the Bankruptcy Code contains a similar requirement that transfers of assets of an non-profit entity pursuant to a Chapter 11 plan comply with all applicable non-bankruptcy law.

Conn. Gen. Stat. Sec. 3-125 provides the attorney general statutory authority to represent the public interest in the protection of any gift, legacies or devises intended for public or charitable purposes. *See Lieberman v. Rogers*, 481 A. 2d 1295 (1984) (powers are broad enough to include actions to enforce, terminate, administer or invalidate terms of charitable trust).

Additionally, pursuant to Conn. Gen. Stat. Sec. 19a-486 et seq., the Office of the Attorney General is responsible for reviewing proposed transfers of assets or operations of nonprofit hospitals to for-profit entities within the State of Connecticut. The Attorney General's review and approval is required whenever a nonprofit hospital enters into an agreement to transfer a material amount of its assets or operations to a for-profit entity. These reviews are conducted jointly with the Department of Public Health and Office of Health Care Access.

OTHER CASES

Second Circuit

- *In re Albert Lindley Lee Meml. Hosp.,* 428 B.R. 283 (Bankr. N.D.N.Y. 2010) (the New York Attorney General argued that state law that creates obligation may be examined to ascertain whether its incidents are such as to constitute a "tax," within meaning of applicable bankruptcy provision. Court sided with AG finding the Debtor's reimbursement liability was an "excise" tax)
- *Winstead Memorial Hospital, 249 B.R. 588 (Bankr. D. Conn. 2000)* (the Attorney General sought to obtain income from trust. Court held that non-profit could continue to receive funds from charitable trust even if the funds will only be used to repay debts that incurred when the charity was operational)

Other Courts

- *In re: Gardens Hospital and Medical Center, Inc.,* 567 B.R. 820 (Bankr. C.D. Cal. 2017) (debtor was required to obtain the California Attorney General's consent prior to selling a material amount of its assets of prior acute care facility because a closed hospital does not qualify as a "health facility" under California law)
- *In re Parkview Hosp.,* 211 B.R. 619 (Bankr. N.D. Ohio 1997)
(Ohio Attorney General sufficiently traced trust property, in seeking to establish that debtor-hospital's development fund was express charitable trust under Ohio law, excluded from bankruptcy estate, even though periodic bank reconciliations were not undertaken or were lost, since documents detailing contributions to fund sufficiently showed that fund received donations which could roughly correspond to balance in account, and fund was kept in distinct account separate from hospital's other accounts)
- *In re Genesys Research Inst., Inc.*, 15-12794-JNF, 2016 WL 3583229 (Bankr. D. Mass. June 24, 2016) (the Attorney General requested the court to disapprove the debtor's intent to abandon until a hearing could be held at which all potentially interested researchers and agencies could be identified and all available options for transfer of the biological materials could be explored.)

Confirmation Issues

a. Absolute Priority Rule

Section 1129(b)'s "fair and equitable" requirement prohibits distributions to any junior class of claims or interests over the objection of a senior class that has not been paid the allowed amount of its bankruptcy claim in full. Specifically, as it relates to unsecured creditors, this provision provides that "the holder of any... interest in a debtor may not receive or retain property on account of such an interest unless creditors have been paid in full." Therefore, the ability to distinguish non-profit membership (or sponsorship) from equity or other interest is vital for non-profits hoping to allow their existing members to retain control following approval of a plan or reorganization under which all creditors, particularly unsecured creditors, are not paid in full.

Courts that have confirmed a nonprofit's reorganization plan which leaves the prepetition members in control of the non-profit even with the dissent of an impaired class of creditors, have highlighted the lack of distributable tangible economic value

possessed prepetition and retained post-confirmation by those parties in control of the nonprofit. For example, in *In re Whittaker Memorial Hospital Association*, the U.S. Bankruptcy Court for the Eastern District of Virginia permitted the members of the debtor, a "Virginia nonstock, membership corporation," to retain control of the debtor hospital following approval of a reorganization plan even though certain unsecured creditors were not paid in full. In reaching this conclusion, the court emphasized that nothing "beyond control" was retained by the members and that the debtor's structure "places it in a unique status apart from private enterprise." *In re Whittaker Memorial Hosp. Ass'n, Inc.*, 149 B.R. 812 (Bankr. E.D. Va. 1993). In a similar decision, also involving a healthcare facility, the court in *In re Independence Village Inc.* allowed members of a nonprofit "life- care" facility for the elderly to retain control of the nonprofit despite the objection of an indenture trustee, noting that the debtor has "no shareholders, hence... no interests inferior to the unsecured creditors" and, accordingly, that "there should be little difficulty [in confirming a plan that leaves pre-petition members in place, notwithstanding]... the absolute priority rule." *In re Independence Village, Inc.,* 52 B.R. 715, 726, (Bankr. E.D. Mich. 1985).

In re General Teamsters, Warehousemen and Helpers Union Local 890 is also frequently cited in support of the proposition that the absolute priority rule does not bar members of a nonprofit from retaining control following confirmation of a reorganization plan under which unsecured creditors are not paid in full. *In re General Teamsters, Warehousemen and Helpers Union Local* 890, 225 B.R. 719, (Bankr. N.D. Cal. 1998). In *General Teamsters*, the debtor, a labor union organized as an unincorporated nonprofit association, proposed a plan under which it would borrow and distribute to creditors a sum of money totaling the equity in substantially all of its assets. Under this proposal, the debtor estimated that unsecured creditors would receive a 31% return on their claims.

<u>OTHER CASES</u>

- *Matter of Wabash Valley Power Ass'n, Inc.*, 72 F.3d 1305 (7th Cir. 1995) (court held that event though a rural electric cooperative's members received lower utility rates as a result of their membership status and other benefits, they could retain their membership interest without paying a dissenting class of creditors in full)
- *In re Eastern Maine Elec. Co-op., Inc.,* 125 B.R. 329 (Bankr. D. Me. 1991) (court held that the rights of members of an agricultural cooperative to recover from patronage capital accounts were more accurately described as equity interests and not as claims for the repayment of debt)
- *In re S.A.B.A.T.C. Townhouse Association, Inc.*, 152 B.R. 1005 (Bankr. M.D. Fla. 1993) (court found that non-profit homeowners association that held title to certain common areas and maintained reserves and proposed to give unsecured creditors pro rata distributions from an account containing approximately $30,000 which represented two years of membership dues collected violated the absolute priority rule)

b. Feasibility of a Plan

Section 1129(a)(11) provides that a Chapter 11 plan may be confirmed only if "[c]onfirmation of the plan is not likely to be followed by the debtor's liquidation, or the need for further financial reorganization of the debtor or any successor to the debtor under the plan." 11 U.S.C. § 1129(a)(11). This is known as the "feasibility" requirement.

For example, in *In re Save Our Springs* (S.O.S.) Alliance Inc., the Fifth Circuit found that the plan proposed by the debtor, Save Our Springs Alliance (SOS), which was to be funded solely by donations to a creditor settlement fund, was not feasible. *In re Save Our Springs (S.O.S) Alliance Inc.,* 632 F.3d 168 (5th Circ. 2011). SOS had limited assets and relied almost exclusively on a handful of donors to fund its ongoing operations. After it commenced its bankruptcy case, SOS proposed a plan that provided that distributions would be paid from a $60,000 creditor settlement fund, which would be generated solely by charitable contributions from SOS's donors within 60 days of the plan's effective date. At the confirmation hearing, SOS asserted that it had already obtained $20,000 in pledges and expressed confidence that it could raise the balance of the creditor settlement fund through donations within the requisite 60-day period. The bankruptcy court disagreed, ruling that the plan was not feasible because, among other things, the evidence established that SOS had secured only $12,500 in donations and that SOS's established donors had expressly declined to contribute to the plan, despite its repeated requests. The Fifth Circuit affirmed the bankruptcy court's decision, finding that SOS had failed to meet its burden of proving feasibility.

In contrast, the court in *In re Indian National Finals Rodeo Inc.* came to a different conclusion on feasibility where the debtor had operational income to fund a plan despite declining donations (in the form of sponsorship agreements). *In re Indian National Finals Rodeo Inc.,* 453 B.R. 387 (Bankr. D. Mont. 2011). In this case, the nonprofit debtor, Indian National Finals Rodeo Inc. (INFR) commenced a Chapter 11 case to reorganize its debts, including a judgment debt owed to a creditor. It proposed a reorganization plan that was funded by regional fees paid by its 11 regional members, membership fees and entry fees paid by contestants who participated in INFR's rodeos, sponsorship agreements and ticket sales. At confirmation, the judgment creditor argued that INFR's plan was not feasible because sponsorships had declined. The bankruptcy court disagreed and confirmed the plan, finding that the plan was feasible because the evidence established that INFR had a positive cash flow for 2010, its ticket sales had consistently increased since 2005 and INFR could likely reduce its expenses as projected in its plan. The court further found that the decline in sponsorships was the result of the judgment creditor's own aggressive collection attempts and that sponsorships would in all likelihood increase once those efforts were barred by the confirmed plan.

OTHER CASES

- *In re Archdiocese of St. Paul and Minneapolis*, 579 B.R. 188 (Bankr. D. Minn. 2017) (plan proposed by unsecured creditors committee in Chapter 11 case of bankrupt archdiocese did not satisfy the feasibility requirement for confirmation;

under committee's plan, further reorganization of debtor would be necessary, as plan required debtor to obtain financing from unknown third-party sources using unidentified property as collateral, plan did not make adequate showing that such funding would likely occur, plan relied on funding from uncertain and speculative future litigation to pay one class of claimants, plan relied on debtor to do fundraising without evidence of sufficiently firm commitment from its donors to contribute, and plan proposed to transfer most if not all of debtor's property to litigation trust, but left reorganized debtor with the same obligation as it had prepetition)

- *In re Machne Menachem, Inc.*, 371 B.R. 63 (Bankr. M.D. Pa. 2006) (debtor objected to Chapter 11 plan proposed by non-profit corporation's former director, under which newly formed entity to which corporation's real property and certain other assets were to be transferred would acquire all of debtor's liabilities and only a portion of its assets and be in danger of sinking into liquidation because it was starting out its not-for-profit life in debt. Debtor raised concerns as to plan's feasibility, however, court found that former director could meet these concerns, and modified plan could be confirmed as feasible, if this new entity or debtor's former director was willing to escrow sufficient sum with court)

c. Best-Interest Test

Section 1129(a)(7) of the Bankruptcy Code requires a plan proponent to establish that each creditor will receive at least as much under the proposed plan as it would receive, if the debtor's assets were liquidated. 11 U.S.C. § 1129(a)(7). Under this requirement, known as the "best-interest test," a bankruptcy court must determine the probable distribution that the holders in each impaired class of claims and interests would receive if the debtor's assets were liquidated under Chapter 7. The court first determines the liquidation value that a forced sale of the debtor's assets would generate and then applies the projected proceeds of such a sale to the distribution scheme set forth in § 1129(b). Unlike other bankruptcy actions, the Bankruptcy Code and state law may preclude or restrict the forced sale of a non-profit's assets. For example, under § 1112(c) of the Code, a non-profit's creditors cannot force a nonprofit to convert its Chapter 11 case to a Chapter 7, nor can they file an involuntary petition against a non-profit. As discussed above, some state statutes impose stringent requirements on the transfer or sale of the non-profit's assets. Accordingly, a non-profit could argue that the best-interest test does not apply where the non-profit is seeking to reorganize because of the above prohibitions on forcing a non-profit to liquidate its assets.

In a non-profit's Chapter 11 case, certain factors may work to substantially lower the barrier to confirmation set by the best-interest test. If a non-profit debtor has to comply with applicable state law before selling or transferring its assets under § 1129(a)(16), it could mean notifying and obtaining consent from the state's attorney general. As discussed above, the sale of hospitals in certain states requires the approval of the state's attorney general. The costs associated with this additional compliance burden, coupled with the delay and uncertainty associated with that compliance process, could depress the forced liquidation value of the nonprofit's assets to a potential buyer. The

lower liquidation value, in turn, could result in a lower minimum level of distribution to creditors for purposes of the best-interest test.

OTHER CASES

- *In re Ft. Wayne Telsat, Inc.*, 489 B.R. 773 (Bankr. N.D. Ind. 2010), *subsequently aff'd*, 665 F.3d 816 (7th Cir. 2011) (proposed compromise, whereby Chapter 7 debtor's alleged rights in Federal Communications Commission (FCC) license for educational broadband service station were relinquished in exchange for $100,000 payment by non-profit entity allegedly identified as licensee in the FCC's records, would be approved as fair and equitable and in best interests of estate; trustee acted reasonably in totally discounting possibility that debtor could succeed in establishing that it had rights in license, as successor to alleged assignee that itself discredited validity of assignment, and in instead adopting as high-end valuation of debtor's recovery, on estoppel theory, the roughly $116,000 that it incurred in constructing facilities to use license, such that settlement provided estate with something close to its estimated maximum recovery, without expense of complex and hotly disputed litigation)
- *In re Forum Health*, 444 B.R. 848 (Bankr. N.D. Ohio 2011)(in determining whether unusual circumstances existed such that it was not in creditors' best interests to dismiss not-for-profit charitable organizations' Chapter 11 cases upon showing of requisite “cause,” court could consider the best interests only of creditors of these charitable organizations and not of related debtors, a hospital and medical organization to which these charitable organizations had ability to make grants from their unrestricted funds, but which had no ability to take charitable organizations' unrestricted funds to pay their own creditors)

MURTHACULLINA

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NON-PROFITS IN BANKRUPTCY

Property of the Estate

Often non-profits are the beneficiaries of charitable trusts where the donors have restricted the use of the income and principal to certain uses such as the operation of a hospital. Under state law the charity must use the gift or bequest in a manner consistent with the donor's intent. These state law restrictions have raised thorny questions of what constitutes property of a non-profit's estate.

Statute

541 (a) Property of the estate includes all legal and equitable interests of the debtor in property as of the commencement of the case and includes gifts or bequests acquired 180 days after the filing;

(c)(2) trust restrictions enforceable under non-bankruptcy law are also enforceable in bankruptcy;

(d) excludes property in which the debtor holds only legal title but not an equitable interest.

Connecticut General Statutes Section 47-2 – Charitable Uses. All estates granted for the maintenance of the ministry of the gospel, or of schools of learning, or for the relief of the poor, or for the preservation, case and maintenance of any cemetery, cemetery lot or monuments thereon, or for any other public and charitable use, **shall forever remain to the uses to which they were granted, according to the true intent and meaning of the grantor, and to no other use whatever.** (emphasis added)

The legal or equitable interest of a debtor in a particular asset is generally determined under state law. *Butner v. United States*, 440 U.S. 48, 54 (1979).

Income From a Trust

In 2000 Judge Krechevsky addressed this issue in the Chapter 7 bankruptcy of Winsted Memorial Hospital. At the time of the filing the Hospital had closed. The asset in question was the income of a bequest that was restricted by the donor to the hospital's general expenses and other charitable purposes. The Attorney General, who has supervisory powers over charitable funds, filed a motion to compel the trustee to abandon the income. The AG argued that since the Hospital was closed the trustee's use of the funds did not satisfy the donor's intent. The AG's planned to commence a *cy pres* proceeding to redirect the funds to a similar charitable use. Although the trustee made no claim to the corpus of the trust, she did object to the motion as to the income. The trustee sought to use the income to pay for claims of employees and vendors who had provided goods and services to the Hospital while it was operating. She did not seek to use any funds to pay for administrative expenses.

The court ruled in favor of the trustee. Under Connecticut law, the bequest had vested with the Hospital at the time of the donor's death when the Hospital was operating. The proposed use of the funds to pay pre-petition operating expense was consistent with the restriction. The court rejected the AG's argument that the Hospital had to be operating at the time of payment to satisfy the charitable restriction.

The court also permitted the trustee to use the income from three of nine individual gifts based on the circumstances of each bequest and granted the AG's motion as to the other six gifts.

In re Winsted Memorial Hospital, 249 B.R. 588 (Bankr. D. Ct 2000), aff'd 3cv1299 (D. Ct. 2000) (AWT)

In re Boston Regional Medical Center, 410 F.3d 100 (1st Cir. 2005) Massachusetts would adopt the vesting rule and find that as long as the Hospital was operating at the time the testator died, the subsequent closing of the Hospital did not divest the Hospital of the use of the funds. See also: *Freme v. Maher,*480 A.2d 783 (Sup. Ct. Me. 1984).

But see: *Salisbury v. Ameritrust Texas,N.A. (In re Bishop College)* 151 BR 394,401 (Bankr. N.D. Tex. 1993). Cessation of the college before payment of operational expenses divested the trustee of any interest in the income.

Corpus

The corpus of a donor-restricted trust generally does not constitute property of the estate. The trustee sought to use both the income and the corpus of a trust. The court

did not allow the trustee to use either. *In re Parkview Hospital (Hunter v. St. Vincent Medical Center,* 211 BR 619,641 (Bankr. N.D. Ohio, 1997).

City of Detroit

The most widely-publicized case in which charitable gifts played a substantial role is the City of Detroit Chapter 9 proceeding. At issue was art held at the Detroit Institute of Art (DIA) valued between $450 and $800 million. The Emergency Manager, a bankruptcy lawyer who was directing the City's case, claimed that the art belonged to the City and should be sold to pay pension and other obligations of the City. The Attorney General issued an opinion which concluded that the City held the art pursuant to a charitable trust which precluded its use to pay creditors. While the art had been owned by the DIA which received support from the City, in 1919 the DIA transferred the art to the City. In 1997 the City and the DIA entered into an operating agreement whereby the City retained legal ownership but the museum maintained day-to-day operations.

The dispute was never resolved by the court. The Emergency Manager skillfully played on this issue to negotiate the "Grand Bargain" whereby the private philanthropists, foundations, and the state contributed $800 million to the debtor for payment to creditors on the condition that the art not be sold and remain open to the public.

Obi and Simmons, *Detroit's Art: Priceless Public Treasure or the City's Disposable Assets?* 32 ABI Journal Nov. 2013 p.20.

Property of Catholic Archdioceses

Sixteen Catholic archdioceses have filed Chapter 11 to address liabilities arising from the clergy sex abuse scandal. At issue in these cases has been whether property and assets of local parishes are property of the archdiocese, the overarching entity that governs the affairs of churches and clergy in the archdiocese. To resolve this issue courts have had to delve into the operative law to determine whether they had jurisdiction to resolve these issues in the face of the First Amendment and the Religious Freedom Restoration Act (RFRA).

In the Archdiocese of Portland, Oregon case a Tort Committee sought to avoid certain transfers involving local parish property. The debtor defended on, among other grounds, the claims that the transfer of parish property did not involve property of the estate and that RFRA barred the Committee's action. The court held that the Archdiocese was a

corporation sole and that whether parish property belonged to the Archdiocese was an issue to be determined by Oregon law, not canon law. Under state law parishes could not own property so the property in question was part of the debtor. However, the court found that there were questions of fact on whether RFRA precluded the court from hearing the merits of the avoidance action.

In re Archdiocese of Portland, Oregon, 335 BR 842 (Bankr. D. Or. 2005)

In an action arising from the Archdiocese of Milwaukee case, the claimants' committee sought to avoid the debtor's transfer of $55 million to a trust for the perpetual care of cemeteries. The Archdiocese brought a declaratory judgment action that sought to bar application of the Code to the transfer on First Amendment and RFRA grounds. The committee moved for partial summary judgment on those issues. The bankruptcy court granted the motion but the District court reversed. On appeal, the Seventh Circuit found that 1) the Code constituted a set of principles of general and neutral applicability that did not burden the Free Exercise of religion; and 2) RFRA applied only to government action and the committee was neither the government nor was it acting under color of law. Disagreeing with the Eighth Circuit, the court found that the application of the avoidance provisions to the transfers was narrowly tailored to advance a compelling government interest. Accordingly the committee was permitted to continue the avoidance action on the merits.

Listecki v. Official Committee of Unsecured Creditors 780 F.3d 731 (7th Cir. 2015)

Ellis and Hyams, *RFRA Circuit Split on Compelling Government Interest,* 34 Am. Bankr. Inst. L. J. 36 (No. 2015)

FIDUCIARY DUTIES OF DIRECTORS AND OFFICERS OF A NON-PROFIT

Like directors of for-profit entities, directors of non-profits have duties of care and loyalty to the organization. However, in some jurisdictions directors of non-profits also have a duty of "obedience" whereby their actions must be consistent with the mission of the organization as defined in the organizational documents. We could find no Connecticut case on the issue. Most states provide for some type of immunity for uncompensated directors and officers of non-profits.

Connecticut statutes

Connecticut General Statutes Section 33-1104 – Nonstock Corporations – General Standards for Directors.

(a) A director shall discharge his duties as a director, including his duties as a member of a committee: (1) in good faith; (2) with the care on ordinary prudent person in a like position would exercise under similar circumstances; and (3) in a manner he reasonably believes to be in the best interests of the corporation.

(b) In discharging his duties a director is entitled to rely on information, opinions, reports or statements, including financial statements and other financial data, if prepared or presented by: (1) one or more officers or employees of the corporation whom the director reasonably believes to be reliable and competent in the matters presented; (2) legal counsel, public accountants or other persons as to matters the director reasonably believes are within the person's professional or expert competence; or (3) a committee of the board of directors of which he is not a member if the director reasonably believes the committee merits confidence.

(c) A director is not acting in good faith if he has knowledge concerning the matter in question that makes reliance otherwise permitted by subsection (b) of this section unwarranted.

(d) A director is not liable for any action taken as a director, or any failure to take any action, if he performed the duties of his office in compliance with this section.

Connecticut General Statutes Section 52-557m – Immunity From Liability of Directors, Officers and Trustees of Nonprofit Tax-Exempt Organizations.

Any person who serves as a director, officer or trustee of a nonprofit organization qualified as a tax-exempt organization under Section 501(c) of the Internal Revenue Code of 1986, or any subsequent corresponding internal revenue code of the United States, as from time to time amended, and who is not compensated for such services on a salary or prorated equivalent basis, shall be immune from civil liability for damage or injury occurring on or after October 1, 1987, resulting from any act, error or omission made in the exercise of such person's policy or decision-making responsibilities if such person was acting in good faith and within the scope of such person's official functions and duties, unless such damage or injury was caused by the reckless, willful or wanton misconduct of such person.

Sale of Assets and the Conflicting Duties of Obedience and Value Maximization

What should a non-profit director do when confronted with two offers – a lower offer which continues the organization's mission and a higher offer that provides a greater return to creditors. Two cases provide an example of this tension. However, recent amendments to the Code may provide some comfort to directors.

In the Boston Regional Medical Center case the directors had determined that they had to sell the hospital and concentrate on operating diagnostic centers. The hospital was likely insolvent. The entity was affiliated with the Seventh Day Adventist Church whose affiliate was the member of the organization and had several members of the Board. The directors were confronted with an offer from Tenet that would provide a higher return to creditors and a lower offer from another non-profit that promised to continue the affiliation with the Seventh Day Adventists. The directors chose the lower offer. When the non-profit buyer was unable to close and Tenet was no longer interested, the Medical Center was forced to close. It filed a Chapter 11 liquidating plan. Thereafter the Creditors" Committee sued the directors and officers for breach of fiduciary duty in district court. The court found that the Committee had standing to bring claims on behalf of the entity despite the simultaneous ability of the Attorney General to take action. The AG had not sued the directors and, in fact, had approved the proposed sale. Based on the Massachusetts immunity statute, the court dismissed the action against the uncompensated directors. However, the court did permit the action to continue against the CEO who was a paid employee.

In re Boston Regional Medical Center, 328 F.Supp. 2d 130 (D. Mass. 2004)

In the United Healthcare case the non-profit debtor proposed a sale to a buyer that would continue the mission of the organization that offered less money than a bidder with a higher offer that would not continue the mission. The bankruptcy court did not approve the sale to the lower bidder. On appeal the district court reversed and held that the directors were entitled to consider the continuation of the mission in making its decision.

In re United Healthcare, 1997 US Dist Lexis 5090 (D. N.J. March 20, 1997)

Allegheny Health, Education and Research Foundation (AHERF)

Executives ignore restrictions on charitable gifts at their peril. In AHERF the Attorney General indicted several officers of AHERF for misuse of charitable fiunds. The essence of the claim was that the officers used the charitable funds for the operations of the hospitals and for various acquisitions. There were no allegations of self-dealing. The chief executive officer pled guilty and served jail time. The directors and officers paid $94 million to settle claims brought by the AG. Insurance covered most of the claim.

HYPOTHETICAL #1

Susan is a bankruptcy lawyer whose client is Hartford Sings, Inc., a non-profit that has been around for 30 years. The organization trains inner-city kids in choral music and puts on concerts in its auditorium. The organization has run a significant deficit for the last four years and has lost grant funding. The founder, who serves as president, has been drawing down the endowment to keep things afloat. The local newspaper has published allegations that the founder placed a lot of personal expenses on the organization's credit card over the last few years. A few years ago, the Board heard similar allegations and asked the founder about them. She said all the expenses were proper and the Board took no further action. The founder announced she will retire in the next two months. The CFO has resigned to take another job. The board has just learned that the 2017 audit was not done because of lack of funds. The founder says there will be enough funds from operations and the endowment to stay open for six months. However, she has never been good with math! The organization owns the building. The Board consists of seven members but three have resigned recently.

Several ideas have surfaced:

1) Hold a fund-raising campaign and stay open;

2) close the program, sell the real estate to a neighboring non-profit that provides sports activities for inner-city kids. Use the proceeds to pay vendors, including many small local businesses, and place the remainder in a fund to provide music scholarships to inner-city kids.

3) file Chapter 7 bankruptcy.

What are the pros and cons of each option? What should Susan recommend to the Board? Are there other steps the Board should take?

If Susan was a member of the Board, what other issues would be raised?

HYPOTHETICAL #2

Podunk Community Hospital (hereafter "Podunk") serves a rural area providing critical healthcare to the local community. For a variety of reasons, including mismanagement services Medicare reimbursement rates insufficient to cover basic operating costs, and pension obligations, the hospital is losing money and runs the risk of having to shut down. The Board of Directors determines the hospital should file for Chapter 11 and put itself up for sale and conduct a competitive bidding process. Podunk's lender, Big Bad Bank (BBB) which is underwater, wholeheartedly agrees and supports a filing and a cash collateral order that provides a time table for funding operations for 120 days in order to effectuate a sale of the hospital. The cash collateral order includes benchmarks for sale approval of 120 days and closing within 30 days thereafter. BBB agrees to this notwithstanding its collateral position erodes every day.

The sale process produces three bids. Bid #1 is from a catholic hospital and continue its operations fulfilling Podunk's original mission statement except with limitations on women's reproductive health. Bid #2 is for a higher amount by another hospital, but they will convert Podunk into an emergency care center only and refer all other patients to its hospital in the big city. Neither Bid #1 or #2 come close to paying BBB in full or leaving money for the bankruptcy estate. Bid #3 is from Trumpy and is by far the largest cash offer (BBB will be paid in full with proceeds to priority and unsecured creditors), however if they are the successful bidder they will shut Podunk down and build a casino that will create over 1,000 new jobs in this rural community. The State of Connecticut has an agreement with Trumpy to get a percentage of the slots revenue for the first twenty years of its operations.

The Board selects Bid #1 because the hospital will continue to serve the community and is generally consistent with Podunk's mission statement. The purchase agreement correctly provides that the sale is subject to approval by the State of Connecticut with an outside deadline of 30 days post sale approval by the Court consistent with the cash collateral order. Over the objections of BBB and the Creditor's Committee, the Court enters the Sale Order (to Bid #1) on the 120th day following the filing of the Chapter 11. BBB and the Creditor's Committee objected to the selection of Bid #1 as not representing the highest and best offer and filed a notice of appeal. Sixty days after sale approval by the bankruptcy court, Podunk is still losing money. The state has not yet approved the sale and the bank files a motion for relief from the automatic stay based on (i) lack of adequate protection because its assets continue to erode and (ii) the sale has not closed within the 150-day deadline in the cash collateral order. BBB further terminates its consensual use of cash collateral. BBB wants stay relief granted so it can foreclose on its collateral and sell to Trumpy and agrees any excess proceeds will go back to Podunk's estate for priority and unsecured creditors. The Debtor seeks an order requesting continued use of cash collateral until the State of Connecticut approves the sale to Bidder #1. What happens?

SOME NON-PROFIT CASES IN THE DISTRICT OF CONNECTICUT

Hospital

Old JMMC/ fdba Johnson Memorial Hospital, Inc. (and related cases) 15-20056 (Ch. 11)

Johnson Memorial Hospital, Inc. (and related case) 08-22188 (Ch. 11)

Winsted Memorial Hospital 96-23984 (Ch. 7)

Nursing Home and Assisted Living

Hebrew Home and Hospital, Incorporated (and related cases) 16-21311 (Ch. 11)

Old JMMC/ The Johnson Evergreen Corporation 15-20056 (Ch. 11)

The Jewish Home for the Aged 11-30312 (Ch. 11)

East Hill Woods, Inc. 97-31158 (Ch. 11)

Church

Greater Evangel Temple Church of God in Christ, Inc. 16-31239 (Ch. 11)

The Trinity Temple Church of God in Christ 16-30714 (Ch. 11)

The Trinity Church of God in Christ 14-31520 (dismissed)

Arts, Cultural and Social Organizations

Wall Street Theater Company, Inc. (and related case) 18-50132 (Ch. 11)

Urban Oaks Organic Farm, Inc. 16-20573 (Ch. 7)

Greater Hartford Architectural Conservancy 00-21425 (Ch. 7)

Stamford Center for the Arts 08-50773 (Ch. 11)

ETHICS ISSUES IN BANKRUPTCY CASES

First Annual Connecticut Bankruptcy Court Conference
October 4, 2018

JUDY JONES
CHAPTER 11 HYPOTHETICAL

1) What statutes and rules (both Professional Conduct, as well as federal local rules of bankruptcy procedure) are implicated by Ethan’s request?

- 2) What are Judy’s ethical responsibilities?

- 3) What are Ethan’s ethical responsibilities?

4) Can Judy serve as special counsel even though Judy still represents the principals of the Debtor in the insurance litigation?

5) What are Ethan’s duties to collect the loan from Ted?

6) Does Ethan need to sue to recover from Mary for the Escalade?

7) Does Ethan need to sue the private school to recover the gift?

8) Does it matter if there is a creditor's committee to pursue the claims against insiders?

9) Is having conflicts counsel a practical solution?

10) Should the Court consider appointing a Chapter 11 trustee?

11) What are the privilege issues for Judy in the event of a conversion?

12) The trustee owns the privilege, but what about communications that concern both the non-estate litigation and estate litigation?

13) If the case converts to Chapter 7, can Judy represent Ted and Mary in litigation brought by the trustee against them?

THE CHAPTER 7 CASE OF JOHN SMITH

- **The Debtor, John Smith**, filed a voluntary petition for relief under Chapter 7 of the Bankruptcy Code. Prior to the filing, the Debtor retained **Attorney Christopher Jackson** as his counsel and paid Mr. Jackson a fee of $800.00. The Debtor never met Mr. Jackson in his office, but instead communicated with him online and over the phone.
- On September 5, 2018, the Debtor's 341 Meeting was held. The Debtor appeared at the 341 meeting, but Attorney Jackson did not appear to represent the Debtor. Instead, **Attorney Christina Hughes** made an appearance on behalf of the Debtor. While the Debtor knew that an attorney would represent him at the 341 meeting, he did not know that it would be Attorney Hughes.
- Attorney Hughes was not hired by the Debtor or employed by Attorney Jackson's law firm. Attorney Hughes had never met the Debtor prior to the 341 meeting and was not familiar with the Debtor's schedules. The Chapter 7 Trustee concluded that she could not examine the Debtor without correct schedules, so the Trustee adjourned the examination to a later date so that the Debtor could file corrected schedules.

THE CHAPTER 7 CASE OF JOHN SMITH

- The continued 341 Meeting was held on September 19, 2018. **Attorney Jones** (not Attorney Jackson or Attorney Hughes), appeared to represent the Debtor at the continued 341 meeting. Because the Debtor's schedules were still incorrect, the Chapter 7 Trustee again continued the 341 meeting to a later date.
-
- Following the continued 341 Meeting, the Debtor submitted a letter to the Court stating that Attorney Jackson failed to advise the Debtor that he would not appear at any of the 341 meetings or that he would send another attorney on his behalf. The letter also noted that Attorney Jackson failed to obtain the Debtor’s consent to file the amended schedules.

QUESTION 1

Has Attorney Jackson violated the Rules of Professional Conduct?

If so, which Rules have been violated?

QUESTION 2

Have Attorney Hughes and Attorney Jones violated the Rules of Professional Conduct?

If so, which rules have been violated?

QUESTION 3

Should Attorney Jackson have to disgorge the compensation he received from the Debtor?

QUESTION 4

Have any of the attorneys violated any of the Local Rules of Bankruptcy Procedure?

If so, which Rules have been violated?

THOUGHTS?

QUESTIONS?

CT RULES OF PROFESSIONAL CONDUCT

Rule 1.1. Competence

A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.

Rule 1.2. Scope of Representation and Allocation of Authority between Client and Lawyer

(a) Subject to subsections (c) and (d), a lawyer shall abide by a client's decisions concerning the objectives of representation and, as required by Rule 1.4, shall consult with the client as to the means by which they are to be pursued. A lawyer may take such action on behalf of the client as is impliedly authorized to carry out the representation. A lawyer shall abide by a client's decision whether to settle a matter. In a criminal case, the lawyer shall abide by the client's decision, after consultation with the lawyer, as to a plea to be entered, whether to waive jury trial and whether the client will testify. Subject to revocation by the client and to the terms of the contract, a client's decision to settle a matter shall be implied where the lawyer is retained to represent the client by a third party obligated under the terms of a contract to provide the client with a defense and indemnity for the loss, and the third party elects to settle a matter without contribution by the client.

(b) A lawyer's representation of a client, including representation by appointment, does not constitute an endorsement of the client's political, economic, social or moral views or activities.

(c) A lawyer may limit the scope of the representation if the limitation is reasonable under the circumstances and the client gives informed consent. Such informed consent shall not be required when a client cannot be located despite reasonable efforts where the lawyer is retained to represent a client by a third party that is obligated by contract to provide the client with a defense.

(d) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may (1) discuss the legal consequences of any proposed course of conduct with a client; (2) counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law; or (3) counsel or assist a client regarding conduct expressly permitted by Connecticut law, provided that the lawyer counsels the client about the legal consequences, under other applicable law, of the client's proposed course of conduct.

Rule 1.3. Diligence

A lawyer shall act with reasonable diligence and promptness in representing a client.

Rule 1.4. Communication

(a) A lawyer shall:
(1) promptly inform the client of any decision or circumstance with respect to which the client's informed consent, as defined in Rule 1.0 (f), is required by these Rules;
(2) reasonably consult with the client about the means by which the client's objectives are to be accomplished;
(3) keep the client reasonably informed about the status of the matter;
(4) promptly comply with reasonable requests for information; and
(5) consult with the client about any relevant limitation on the lawyer's conduct when the lawyer knows that the client expects assistance not permitted by the Rules of Professional Conduct or other law.
(b) A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.

Rule 1.5. Fees

(a) A lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses. The factors to be considered in determining the reasonableness of a fee include the following:

(1) The time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;
(2) The likelihood, if made known to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;
(3) The fee customarily charged in the locality for similar legal services;
(4) The amount involved and the results obtained;
(5) The time limitations imposed by the client or by the circumstances;
(6) The nature and length of the professional relationship with the client;
(7) The experience, reputation, and ability of the lawyer or lawyers performing the services; and
(8) Whether the fee is fixed or contingent.

(b) The scope of the representation, the basis or rate of the fee and expenses for which the client will be responsible, shall be communicated to the client, in writing, before or within a reasonable time after commencing the representation, except when the lawyer will charge a regularly represented client on the same basis or rate. Any changes in the basis or rate of the fee or expenses shall also be communicated to the client in writing before the fees or expenses to be billed at higher rates are actually incurred. In any representation in which the lawyer and the client agree that the lawyer will file a limited appearance, the limited appearance engagement agreement shall also include the following: identification of the proceeding in which the lawyer will file the limited appearance; identification of the court events for which the lawyer will appear on behalf of the client; and notification to the client that after the limited appearance services have been completed, the lawyer will file a certificate of completion of limited appearance with the court, which will serve to terminate the lawyer's obligation to the client in

the matter, and as to which the client will have no right to object. Any change in the scope of the representation requires the client's informed consent, shall be confirmed to the client in writing, and shall require the lawyer to file a new limited appearance with the court reflecting the change(s) in the scope of representation. This subsection shall not apply to public defenders or in situations where the lawyer will be paid by the court or a state agency.

(c) A fee may be contingent on the outcome of the matter for which the service is rendered, except in a matter in which a contingent fee is prohibited by subsection (d) or other law. A contingent fee agreement shall be in a writing signed by the client and shall state the method by which the fee is to be determined, including the percentage or percentages of the recovery that shall accrue to the lawyer as a fee in the event of settlement, trial or appeal, whether and to what extent the client will be responsible for any court costs and expenses of litigation, and whether such expenses are to be deducted before or after the contingent fee is calculated. The agreement must clearly notify the client of any expenses for which the client will be liable whether or not the client is the prevailing party. Upon conclusion of a contingent fee matter, the lawyer shall provide the client with a written statement stating the outcome of the matter and, if there is a recovery, showing the remittance to the client and the method of its determination.

(d) A lawyer shall not enter into an arrangement for, charge, or collect:

(1) Any fee in a domestic relations matter, the payment or amount of which is contingent upon the securing of a dissolution of marriage or civil union or upon the amount of alimony or support, or property settlement in lieu thereof; or

(2) A contingent fee for representing a defendant in a criminal case.

(e) A division of fee between lawyers who are not in the same firm may be made only if:

(1) The client is advised in writing of the compensation sharing agreement and of the participation of all the lawyers involved, and does not object; and

(2) The total fee is reasonable.

Rule 1.6. Confidentiality of Information

(a) A lawyer shall not reveal information relating to representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation, or the disclosure is permitted by subsection (b), (c), or (d).

(b) A lawyer shall reveal such information to the extent the lawyer reasonably believes necessary to prevent the client from committing a criminal or fraudulent act that the lawyer believes is likely to result in death or substantial bodily harm.

(c) A lawyer may reveal such information to the extent the lawyer reasonably believes necessary to:

(1) Prevent the client from committing a criminal or fraudulent act that the lawyer believes is likely to result in substantial injury to the financial interest or property of another;

(2) Prevent, mitigate or rectify the consequence of a client's criminal or fraudulent act in the commission of which the lawyer's services had been used;

(3) Secure legal advice about the lawyer's compliance with these Rules;

(4) Comply with other law or a court order.

(5) Detect and resolve conflicts of interest arising from the lawyer's change of employment or from changes in the composition or ownership of a firm, but only if the revealed information would not compromise the attorney-client privilege or otherwise prejudice the client.

(d) A lawyer may reveal such information to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client.

(e) A lawyer shall make reasonable efforts to prevent the inadvertent or unauthorized disclosure of, or unauthorized access to, information relating to the representation of a client.

Rule 1.7. Conflict of Interest: Current Clients

(a) Except as provided in subsection (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:
(1) the representation of one client will be directly adverse to another client; or
(2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.
(b) Notwithstanding the existence of a concurrent conflict of interest under subsection (a), a lawyer may represent a client if:
(1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;
(2) the representation is not prohibited by law;
(3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or the same proceeding before any tribunal;
and
(4) each affected client gives informed consent, confirmed in writing.

Rule 1.10. Imputation of Conflicts of Interest:

General Rule
(a) While lawyers are associated in a firm, none of them shall knowingly represent a client when any one of them practicing alone would be prohibited from doing so by Rules 1.7 or 1.9, unless:

(1) the prohibition is based on a personal interest of the disqualified lawyer and does not present a significant risk of materially limiting the representation of the client by the remaining lawyers in the firm; or
(2) the prohibition is based upon Rule 1.9 (a) or 1.9 (b) and arises out of the disqualified lawyer's association with a prior firm, and
(A) the disqualified lawyer is timely screened from any participation in the matter and is apportioned no part of the fee therefrom;
(B) written notice is promptly given to any affected former client to enable the former client to ascertain compliance with the provisions of this Rule, which shall include a description of the screening procedures employed; a statement of the firm's and of the screened lawyer's compliance with these Rules; a statement that review may be available before a tribunal; and an agreement by the firm to respond promptly to any written inquiries or objections by the former client about the screening procedures; and
(C) certifications of compliance with these Rules and with the screening procedures are provided to the former client by the screened lawyer and by a partner of the firm, at reasonable intervals upon the former client's written request and upon termination of the screening procedures.
(b) When a lawyer has terminated an association with a firm, the firm is not prohibited from thereafter representing a person with interests materially adverse to those of a client represented by the formerly associated lawyer and not currently represented by the firm, unless:
(1) The matter is the same or substantially related to that in which the formerly associated lawyer represented the client; and
(2) Any lawyer remaining in the firm has information protected by Rules 1.6 and 1.9 (c) that is material to the matter.
(c) A disqualification prescribed by this Rule may be waived by the affected client under the conditions stated in Rule 1.7.
(d) The disqualification of lawyers associated in a firm with former or current government lawyers is governed by Rule 1.11.

Rule 3.3. Candor toward the Tribunal

(a) A lawyer shall not knowingly:
(1) Make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by the lawyer;
(2) Fail to disclose to the tribunal legal authority in the controlling jurisdiction known to the lawyer to be directly adverse to the position of the client and not disclosed by opposing counsel; or
(3) Offer evidence that the lawyer knows to be false. If a lawyer, the lawyer's client, or a witness called by the lawyer, has offered material evidence and the lawyer comes to know of its falsity, the lawyer shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal.
(b) A lawyer who represents a client in an adjudicative proceeding and who knows that a person intends to engage, is engaging or has engaged in criminal or fraudulent conduct related to the proceeding shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal.
(c) The duties stated in subsections (a) and (b) continue at least to the conclusion of the proceeding, and apply even if compliance requires disclosure of information otherwise protected by Rule 1.6.
(d) In an ex parte proceeding, a lawyer shall inform the tribunal of all material facts known to the lawyer that will enable the tribunal to make an informed decision, whether or not the facts are adverse.
(e) When, prior to judgment, a lawyer becomes aware of discussion or conduct by a juror which violates the trial court's instructions to the jury, the lawyer shall promptly report that discussion or conduct to the trial judge.

Rule 5.1. Responsibilities of Partners, Managers, and Supervisory Lawyers

(a) A partner in a law firm, and a lawyer who individually or together with other lawyers possesses comparable managerial authority in a law firm, shall make reasonable efforts to ensure that the firm has in effect measures giving reasonable assurance that all lawyers in the firm conform to the Rules of Professional Conduct.
(b) A lawyer having direct supervisory authority over another lawyer shall make reasonable efforts to ensure that the other lawyer conforms to the Rules of Professional Conduct.
(c) A lawyer shall be responsible for another lawyer's violation of the Rules of Professional Conduct if:
(1) The lawyer orders or, with knowledge of the specific conduct, ratifies the conduct involved; or
(2) The lawyer is a partner or has comparable managerial authority in the law firm in which the other lawyer practices, or has direct supervisory authority over the other lawyer, and knows of the conduct at a time when its consequences can be avoided or mitigated but fails to take reasonable remedial action.

Rule 5.2. Responsibilities of a Subordinate Lawyer
A lawyer is bound by the Rules of Professional Conduct notwithstanding that that lawyer acted at the direction of another person.

Rule 8.4. Misconduct

It is professional misconduct for a lawyer to:

(1) Violate or attempt to violate the Rules of Professional Conduct, knowingly assist or induce another to do so, or do so through the acts of another;
(2) Commit a criminal act that reflects adversely on the lawyer's honesty, trustworthiness or fitness as a lawyer in other respects;
(3) Engage in conduct involving dishonesty, fraud, deceit or misrepresentation;
(4) Engage in conduct that is prejudicial to the administration of justice;
(5) State or imply an ability to influence improperly a government agency or official or to achieve results by means that violate the Rules of Professional Conduct or other law; or
(6) Knowingly assist a judge or judicial officer in conduct that is a violation of applicable rules of judicial conduct or other law.

The Bankruptcy Code

- **11 U.S.C. Section 327 (employment of professional persons)**

▫ "(a) Except as otherwise provided in this section, the trustee, with the court's approval, may employ one or more attorneys ... that do not hold or represent an interest adverse to the estate, and that are disinterested persons, to represent or assist the trustee in carrying out the trustee's duties under this title."

▫ "(c) In a case under chapter 7, 12, or 11 of this title, a person is not disqualified for employment under this section solely because of such person's employment by or representation of a creditor, unless there is objection by another creditor or the United States trustee, in which case the court shall disapprove such employment if there is an actual conflict of interest."

▫ "(e) The trustee, with the court's approval, may employ, for a specified special purpose, other than to represent the trustee in conducting the case, an attorney that has represented the debtor, if in the best interest of the estate, and if such attorney does not represent or hold any interest adverse to the debtor or to the estate with respect to the matter on which such attorney is to be employed."

- **Section 329(b)**

Authorizes the denial of compensation to debtor's counsel, the cancellation of his or her employment agreement with the Debtor, or the return of compensation paid, if the Court finds that the compensation paid exceeds the reasonable value of the legal services provide.

o In evaluating the value of legal services under 329(b), the question is whether the sum an attorney was paid was excessive for what he accomplished for a debtor in that case.

The Federal Rules of Bankruptcy Procedure

Rule 2014(a)

▫ " An order approving the employment of attorneys ... shall be made only on application of the trustee or committee ... The application shall state ... all of the person's connections with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee. The application shall be accompanied by a verified statement of the person to be employed setting forth the person's connections with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee or any person employed in the office of the United States trustee"

The Local Rules of Bankruptcy Procedure for the District of Connecticut

LBR 2014-1(a) (employment of professional persons)

- As counsel for the DR, you need to file an application for employment of an appearance attorney with full disclosure of services rendered by the appearance attorney.
- "In addition to the requirements set forth in Fed.R.Bank.P. 2014, all applications for th employment of professional persons shall state whether the person has an interest adverse to the estate and the nature of that interest and whether or not the person is o LBR 2014-1

LBR 2016-1

- As counsel for the DR, you need to file an application for compensation to an appearance attorney with full disclosure of services rendered by the appearance attorney. disinterested ..."