2015 Bankruptcy Institute Case Law Update

A review of the opinions of the Supreme Court of the United States, the United States Court of Appeals for the Eighth Circuit, the United States Bankruptcy Appellate Panel for the Eighth Circuit, the United States District Courts for the District of Minnesota, and the United States Bankruptcy Courts for the District of Minnesota issued after those cases presented at the 2014 Bankruptcy Institute through generally, with some exceptions, August 2015, that affect the general practice of bankruptcy or closely related debt issues.

These materials should not be relied upon or cited.

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JURISDICTION/APPEALS

1. Wellness Intern. Network, Ltd. v. Sharif, 135 S. Ct. 1932 (2015) (Sotomayor, J).

PARTIES MAY CONSENT TO A BANKRUPTCY COURT'S FINAL ADJUDICATION OF *STERN* CLAIMS

The Court held that Article III permits bankruptcy judges to adjudicate *Stern* claims with the parties' knowing and voluntary consent, even if such consent is not express. Note: This material is excerpted from the July 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

2. Bullard v. Blue Hills Bank, 135 S. Ct. 1686 (2015) (Roberts, C.J.).

A BANKRUPTCY COURT'S ORDER DENYING CONFIRMATION OF A DEBTOR'S PROPOSED REPAYMENT PLAN IS NOT A FINAL ORDER THAT THE DEBTOR CAN IMMEDIATELY APPEAL

The dispute in this case was about how to define the immediately appealable "proceeding" in the context of the Chapter 13 confirmation process. Debtor argued for a plan-by-plan approach, reasoning that each time a proposed plan comes before the bankruptcy court, the court conducts a separate proceeding. In debtor's view, an order denying confirmation and an order granting confirmation both terminate that proceeding—both are final and appealable. The bank argued that the relevant "proceeding" is the entire process of considering plans, which terminates only when a plan is confirmed or—if the debtor fails to offer any confirmable plan—when the case is dismissed. Thus, an order denying confirmation is not final, if it leaves the debtor free to propose another plan. The Court agreed with the bank: "The relevant proceeding is the process of attempting to arrive at an approved plan that would allow the bankruptcy to move forward. This is so, first and foremost, because only plan confirmation—or case dismissal—alters the status quo and fixes the rights and obligations of the parties. When the bankruptcy court confirms a plan, its terms become binding on debtor and creditor alike . . . Confirmation has preclusive effect, foreclosing relitigation of" issues covered by the confirmed plan. The Court reasoned that when "confirmation is denied and the case is dismissed as a result, the consequences are similarly significant. Dismissal of course dooms the possibility of a discharge and the other benefits available to a debtor under Chapter 13. Dismissal lifts the automatic stay entered at the start of bankruptcy, exposing the debtor to creditors' legal actions and collection efforts . . . And it can limit the availability of an automatic stay in a subsequent bankruptcy case . . . Denial of confirmation with leave to amend, by contrast, changes little. The automatic stay persists. The parties' rights and obligations remain unsettled. The trustee continues to collect funds from the debtor in anticipation of a different plan's eventual confirmation. The possibility of discharge lives on. 'Final' does not describe this state of affairs. An order denying confirmation does rule out the specific arrangement of relief embodied in a particular plan. But that alone does not make the denial final any more than, say, a car buyer's declining to pay the sticker price is viewed as a 'final' purchasing decision by either the buyer or seller. 'It ain't over till it's over.'" The Court

added that several other considerations bolstered its conclusion that the relevant "proceeding" is the entire process that ultimately culminates in confirmation or dismissal. The Court stated that the first consideration was a "textual clue" found in 28 U.S.C.A. § 157(b)(2)(L), which lists "confirmations of plans"among "core proceedings" statutorily entrusted to bankruptcy courts. "Although this item hardly clinches the matter for the Bank—the provision's purpose is not to explain appealability—it does cut in the Bank's favor. The presence of the phrase 'confirmations of plans,' combined with the absence of any reference to denials, suggests that Congress viewed the larger confirmation process as the 'proceeding,' not the ruling on each specific plan," the Court said. Note: This material is excerpted from the April 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

3. In re Civic Partners Sioux City, LLC, 779 F.3d 572 (8th Cir. 2015) (Gruender, J.).

AN ORDER DENYING CONFIRMATION OF A PLAN, WHICH DOES NOT DISMISS THE CASE, IS NOT A FINAL ORDER AND CANNOT BE APPEALED

The Eighth Circuit stated that it lacked jurisdiction to review the order denying confirmation of debtor's second plan of reorganization, noting that in *Lewis v. U.S. Farmers Home Admin*., 992 F.2d 767, 772 (8th Cir. 1993), it had held that "bankruptcy orders denying confirmation of a proposed plan but not dismissing the underlying petition are nonfinal decisions not subject to appeal." The court added that, fifteen years later, it repeated that "[u]nder Eighth Circuit law, which is consistent with the views of other circuits, an order denying confirmation of a plan, which does not dismiss the case, is not a final order and cannot be appealed." *In re Zahn*, 526 F.3d 1140, 1143 (8th Cir. 2008). In this case, the court observed that the bankruptcy court had not dismissed the debtor's case. Because of this fact, it was clear to the Eighth Circuit that it could not review the denial of confirmation of the debtor's second plan of reorganization. Note: This material is excerpted from the April 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

4. In re Roussel, 769 F.3d 574 (8th Cir. 2014) (Benton, J.).

DISTRICT COURT'S REMAND ORDER WAS NOT FINAL WHERE THE BANKRUPTCY COURT WAS REQUIRED TO DECIDE ON REMAND WHETHER ATTORNEY'S FEES AWARDED BY A STATE COURT WERE NONDISCHARGEABLE

Finality of a bankruptcy court order depends on the extent to which: (1) "the order leaves the bankruptcy court nothing to do but execute the order;" (2) "delay in obtaining review would prevent the aggrieved party from obtaining effective relief;" and (3) "a later reversal on the [contested issue] would require recommencement of the entire proceeding." The Eighth Circuit added that an order of remand is not final unless it "leaves only ministerial duties for the bankruptcy court;" an order is ministerial and final if it effectively resolves the merits, and the task on remand is "unlikely to generate a new appeal or to affect the issue that the disappointed

party wants to raise on appeal. In this case, the circuit court found that the state court judge did not specify whether the award for attorney's fees was for a breach of fiduciary duty or a breach of contract (or some apportionment); the bankruptcy court determined that the attorney's fees were dischargeable because they were based on a contract (the operating agreement), or breach of contract. Here, the district court's remand order required the bankruptcy court to determine whether the operating agreement connected the attorney's fees to the nondischargeable fiduciary debt. This, the Eighth Circuit concluded, was something more than a ministerial act, observing that the fees at issue here were not "for the litigation in question" or "attributable to the case," but for a prior case in the state court. In this case, the debtor was liable for the fees before the bankruptcy filing; "the dispute is whether they are dischargeable. The district court's order is not final," the court concluded. Note: This material is excerpted from the November 2014 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2014 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

5. In re Carlson, 519 B.R. 756 (B.A.P. 8th Cir. 2014) (Federman, J.), *aff'd*, 600 F. App'x 501 (8th Cir. Apr. 27, 2015) (NO. 14-3563) (per curiam), *as corrected* (Apr. 27, 2015).

BECAUSE THE DEBTORS FAILED TO PROVIDE AN ADEQUATE RECORD OF THE BANKRUPTCY COURT'S DECISIONS, THE BAP COULD NOT HOLD THAT THE FACTUAL BASIS OF THE BANKRUPTCY COURT'S ORDERS WAS CLEARLY ERRONEOUS

All three orders being appealed were one-page orders that referred to findings and conclusions made on the record at the respective hearings. The debtors, however, did not provide the BAP with transcripts of any of the hearings, as required by Fed. R. Bankr. P. 8006 and Fed. R. Bankr. P. 8009(b). The BAP found that even if it was able to ascertain from the debtors' briefs on appeal what factual errors, if any, they asserted that the court committed, the BAP was unable to review the bankruptcy court's orders because the debtors failed to provide an adequate record of the bankruptcy court's decisions. "Since we do not know the factual basis for the dismissal and bar to refiling, we cannot hold that such factual basis was clearly erroneous," the BAP ruled. Note: This material is excerpted from the December 2014 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2014 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

6. In re Seifert, 533 B.R. 265 (B.A.P. 8th Cir. 2015) (Shodeen, J.).

REQUESTS FOR DECLARATORY RELIEF ARE SUBJECT TO MOOTNESS DOCTRINE; LIVE CONTROVERSY EXISTS IF PARTIES HAVE AN INTEREST IN THE OUTCOME

In this chapter 12 case, the debtor resolved objections by proposing a plan in which his net equity in his property was stipulated, subject to the outcome of a pending, disputed claim of exemption in crop proceeds payable jointly to the debtor and a creditor. After the debtor turned over the checks to the creditor, the bankruptcy court determined that the exemption issue was moot. The BAP reversed, noting that the plan undoubtedly reserved the disputed claim of exemption, and held that the payment of the checks did not determine what amount would be paid to unsecured creditors, so the question of whether the debtor was entitled to the exemption was not moot.

7. In re Tri-State Financial, LLC, 519 B.R. 759 (B.A.P. 8th Cir. 2014) (Nail, J.).

ON REMAND, THE TRIAL COURT IS FREE TO PASS UPON ANY ISSUE THAT WAS NOT EXPRESSLY OR IMPLIEDLY DISPOSED OF ON APPEAL AND THE TRIAL COURT IS NOT BOUND BY ITS EARLIER RULINGS IF THE APPELLATE COURT DOES NOT ADOPT THOSE RULINGS

This case involved an ownership dispute over $1,190,000.00 between the chapter 7 trustee of the estate of Tri-State Ethanol and Thomas Stalnaker, as chapter 11 trustee of the estate of Tri-State Financial. On February 13, 2013, the bankruptcy court in the chapter 11 case entered an order determining that the $1,190,000.00 was not part of the bankruptcy estate, that the bankruptcy estate was entitled to be reimbursed for legal fees and expenses in litigating the ownership of the funds, and outlining the procedure for Stalnaker to request reimbursement for those fees, costs, and expenses.

On May 21, 2013, the bankruptcy court entered another order in the chapter 11 case allowing fees and expenses to be reimbursed by surcharging the $1,900,000.00. Stalnaker was awarded fees and expenses in the amount of $35,944.45, to which no party objected. The chapter 7 trustee was awarded $61,886.90 over the objections of several parties in interest, including "Jandrain, et al.," a creditor group. The same date, the bankruptcy court entered a judgment incorporating both the February and May orders.

Stalnaker and Centris (a creditor of Tri-State Financial) appealed; Jandrain filed a cross-appeal. Two issues were presented: (1) whether the bankruptcy court erred in concluding the $1,190,000.00 was not property of the estate; and (2) whether the bankruptcy court erred in surcharging Stalnaker's attorney fees, costs, and expenses against the $1,190,000.00. Stalnaker and Centris argued that Tri-State Financial was judicially estopped from having any position imputed upon it, other than the $1,190,000.00 belonged to Tri-State Financial and that Tri-State Financial was released from turning over those funds pursuant to a prepetition release. Stalnaker also argued that Tri-State's investors should be estopped from asserting ownership to those funds. The BAP held that these issues were premature since the bankruptcy court order was silent on them. The BAP reversed and remanded for further proceedings. (*Stalnaker I*)

On remand, the bankruptcy court changed its earlier ruling by entering an order determining that the $1,190,000.00 was property of the chapter 11 estate and was subject to the security interest of Centris. The bankruptcy court did not change the award of legal fees and expenses or its surcharge decision. Jandrain, REI, Hoiches, and American Interstate appealed.
On appeal, the BAP identified five issues: (1) whether the bankruptcy court exceeded its mandate on remand; (2) whether the bankruptcy court disregarded the law of the case; (3) whether the bankruptcy court failed to comply with Fed. R. Civ. P. 63 and Fed. R. Bankr. P. 9028; (4) whether the bankruptcy court erred in concluding the $1,190,000.00 was property of the chapter 11 bankruptcy estate; and (5) whether the bankruptcy court erred in surcharging Stalnaker's attorney fees, costs, and expenses against the $1,190,000.00.

Regarding the first issue, Jandrain argued that when the bankruptcy court changed its ruling and determined that the $1,190,000.00 was not part of the estate, the bankruptcy court failed to follow the appellate court's mandate on remand. The BAP disagreed, stating that "on remand the trial court is free to pass upon any issue that was not expressly or impliedly disposed of on appeal." In the first appeal, the BAP explicitly declared that deciding the issue would be premature. Therefore, the bankruptcy court was free to consider the issue.

The BAP came to a similar conclusion on the second issue. Under the law-of-the-case doctrine, "when a court decides upon a rule of law, that decision should continue to govern the same issues in subsequent stages in the same case." Moreover, the doctrine "applies to both appellate decisions and [trial] court decisions that have not been appealed." The BAP stated that because the bankruptcy court's order was appealed and the BAP did not adopt any of the bankruptcy court's rulings, the bankruptcy court was not bound by its earlier rulings.

Regarding the third issue, while *Stalnaker I* was still pending, the bankruptcy judge retired and the case was then assigned to a different judge. Fed. R. Civ. P. 63 and Fed. R. Bankr. P. 9028 state: "[i]f a judge conducting a hearing or trial is unable to proceed, any other judge may proceed upon certifying familiarity with the record and determining that the case may be completed without prejudice to the parties . . . ." Because the bankruptcy court did not certify familiarity with the record and make a determination that the case could be completed without prejudice to the parties before entering judgment, the case was remanded to allow the bankruptcy court to comply with the above rules.

The BAP also stated that the bankruptcy court was free to consider the remaining undecided issues.

8. Premier On Landscapes, LLC v. Hrkal, 2014 WL 4954696 (D. Minn. 2014 (Montgomery, J.).

MISAPPLICATION OF CLEAR AND UNAMBIGUOUS PROCEDURAL RULES CANNOT EXCUSE FAILURE TO FILE A TIMELY NOTICE OF APPEAL

The bankruptcy court dismissed a creditor's adversary complaint with prejudice. Creditor appealed the dismissal 28 days later, mistakenly believing the appeal period to be 30 days, not the 14 imposed by Fed.R. Bankr. P. 8002(a). Appellant counsel realized the error and filed a motion before the bankruptcy court to extend the appeal deadline, arguing that counsel's erroneous research, and the erroneous date entered by counsel's inaccurate pleading software, constituted excusable neglect. The bankruptcy court denied the motion. The district court denied the appeal for lack of jurisdiction due to the untimeliness of the appeal. Appellant argued that the bankruptcy court was wrong when it found no excusable neglect for the late appeal, but the district court noted that, first, the order finding no excusable neglect and denying the motion to extend the time to appeal was not appealed, and second, even if the issue of excusable neglect was properly before the district court on appeal, the bankruptcy court was correct in ruling that that "inadvertence, ignorance of the rules, or mistakes construing the rules do not usually constitute 'excusable neglect.'" And it must be so, the court noted, or every appellant lawyer could plead inability to understand the law when he misses a deadline.

9. Ritchie Capital Management, LLC v. JPMorgan Chase & Co., Civil No. 14-4786 (DWF/FLN) (D. Minn. July 2, 2015) (Frank, J.).

ALL *PETTERS* RELATED CASES SHOULD BE BEFORE THE BANKRUPTCY TRIBUNAL PRESIDING OVER THE *PETTERS* BANKRUPTCY CASES, AT LEAST FOR PURPOSES OF ALL PRE-JURY TRIAL PROCEEDINGS

In this case the plaintiffs, affiliated investment companies, brought numerous fraud claims against the defendants, numerous banks, arising out of Petters and Polaroid transactions in which the banks were involved. On motion by defendant banks to refer the case to bankruptcy court, the district court determined that jurisdiction was proper under 28 U.S.C. § 1334(b) as a case related to bankruptcy proceedings ongoing in this district. The court then held that 28 U.S.C. § 157(a) and (c), and Local Bankruptcy Rule 1070-1, applied to render a transfer to the bankruptcy court proper. The district court concluded that Local Rule 5011-3 (transfer from bankruptcy court to district court of a proceeding in which there is a right to a jury trial) does not affect the bankruptcy court's jurisdiction because it does not impair the ultimate right to a jury trial in the district court, following the conclusion of all pre-trial stages in the bankruptcy court. Similarly, the district court also noted that referral at this stage does not run afoul of Stern v. Marshall. Finally, the court observed that there is an interest in uniform administration of all matters that implicate the Petters related bankruptcies because of similar administrative, factual and legal issues involved in hundreds of adversary cases related to each other and the overall bankruptcy.

On the motion to intervene brought by the bankruptcy trustees of the Polaroid and Petters cases, the district court analyzed the test for intervention by right under Fed. R. Civ. P. 24(a)(2), including timeliness (requiring consideration of surrounding circumstances, reason for delay,

prior knowledge of the pending action, progression of the litigation and likelihood of prejudice), and the party's interest in the subject matter of the litigation (whether the interests of the proposed intervenors are potentially impaired by the disposition of the litigation and not adequately protected by the existing parties), under liberal construction with all doubts resolved in favor of the proposed intervenors. The court granted the motion, concluding that the trustees' motion was timely and that the trustees shared a direct, substantial, and legally protectable interest in the claims being asserted and litigated by the plaintiffs; that the parties at least partially seek recovery of the same funds, which funds could be recovered by one party at the expense of the other as proceedings move forward; and that the interests of the parties cannot fully align and thus the trustees' interests could not be adequately protected.

STANDING

10. Cutcliff v. Reuter, 791 F.3d 875 (8th Cir. 2015) (Gruender, J.).

STANDING TO APPEAL REQUIRES AN AGGRIEVED PARTY; SATISFACTION OF THE CONCEIVABLE EFFECTS TEST ALLOWS REFERRAL TO BANKRUPTCY COURT; DAMAGE DETERMINATION DOES NOT ALWAYS REQUIRE AN EVIDENTIARY HEARING

Nathan and Kathleen Reuter appealed a district court order for default judgment and damages against Vertical Group, LLC. Nine plaintiffs had brought a lawsuit against Nathan Reuter (Nathan) and Vertical Group, LLC based on their alleged roles in a scheme where victims were "'lure[d]' into making a 'high-yield, zero-risk investment' from which their money was 'appropriated.'" Vertical Group, LLC failed to defend against the action and default judgment was entered against it. Nathan filed bankruptcy, at which point the district court closed the case until the bankruptcy was resolved.

In Nathan's bankruptcy, Nathan proposed a Chapter 11 plan that sought to settle the plaintiffs' claims against him. The plaintiffs objected to the plan and brought an adversary proceeding seeking to have their claims against Nathan found nondischargeable. The bankruptcy court ruled in favor of the plaintiffs and awarded actual and punitive damages to the plaintiffs for their claims against Nathan. The bankruptcy court also determined that Nathan's bankruptcy estate had succeeded to Nathan's rights as co-trustee of the Kathleen Trust, a trust created by Nathan and Kathleen into which they transferred assets prior to Nathan's bankruptcy. The estate's rights, however, were limited as subject to Kathleen Reuter's consent as co-trustee.

In the district court case, the plaintiffs sought to reach the assets of the Kathleen Trust and they reopened the case to determine their damages. On request of the plaintiffs and over the objection of the defendants, the district court referred the matter to the bankruptcy court. After receiving affidavits and documents, but without an evidentiary hearing, the bankruptcy court made proposed findings of fact and conclusions of law in which it recommended awarding actual damages, punitive damages, and attorneys' fees to the plaintiffs. The district court adopted these findings and conclusions and entered a default judgment against Vertical Group, LLC. Nathan and Kathleen appealed.

The first issue discussed by the Eighth Circuit Court of Appeals was the standing of Nathan and Kathleen to appeal the district court's order. "Ordinarily, only a party aggrieved by a judgment or order of a district court may exercise the statutory right to appeal therefrom." "[A] litigant that is a party to the overall case may lack standing to appeal from a judgment [concerning] a claim to which it was not a party [where] the appellants were not personally aggrieved by the judgment under appeal." The appellate court found that Kathleen had standing to appeal because of her interest in the Kathleen Trust. The plaintiffs emphasized their intention to reach the assets of the trust, so Kathleen had standing. However, the appellate court found that Nathan did not have standing to appeal because Nathan's rights regarding the trust were an asset of his bankruptcy estate.

The next issue addressed by the appellate court was Kathleen's contention that the district court erred by referring the matter to the bankruptcy court. The appellate court stated, "Congress has provided that a district court may refer certain proceedings over which it has jurisdiction to a bankruptcy court, including those that are 'related to a case under title 11' of the United States Code. 28 U.S.C. §157(a)." "A proceedings is 'related to' a bankruptcy case if 'the outcome of that proceeding could conceivably have any effect on the estate being administered in the bankruptcy.'" This is a broad test, sometimes referred to as the conceivable effects test, that is met if the proceeding "could alter the debtor's rights, liabilities, options, or freedom of action . . . and which in any way impacts upon the handling and administration of the bankruptcy estate." Because the plaintiffs' action sought to gain access to the Kathleen Trust, in which Nathan's bankruptcy estate has rights, the district court did not err in referring the case to the bankruptcy court.

Finally, the appellate court addressed Kathleen's objections to the award of actual and punitive damages. Kathleen asserted that the district court erred in awarding damages because the misconduct alleged was not performed by Vertical Group, LLC, but rather was performed by another entity. The appellate court rejected this argument, stating "[a] defaulted claim . . . precludes a party from contesting the facts in the complaint that establish liability . . . Kathleen is impermissibly contesting Vertical Group's liability, the court did not clearly err . . . ." Next, the appellate court rejected the argument that an evidentiary hearing was necessary to determine the amount of the plaintiffs' actual damages. Regarding punitive damages, however, the court acknowledged the rule that an evidentiary hearing is required but noted at least one exception, which it applied here. That is, an evidentiary hearing will not be required where the district court has "longstanding familiarity with the matter."

11. In re Heyl, 770 F.3d 729 (8th Cir. 2014) (per curiam).

AN LLC's PRINCIPAL LACKED STANDING TO APPEAL BANKRUPTCY COURT'S ORDER REGARDING THE LLC's CLAIM

The Eighth Circuit concluded that an LLC's principal did not have standing to appeal the bankruptcy court's order regarding the LLC's claim. The Eighth Circuit noted that the proof of claim filed in the debtor's bankruptcy case demonstrated that the LLC had a claim against the debtor's bankruptcy estate; the principal was simply trying to enforce it. The circuit court also noted that the principal, who did not claim to be a licensed attorney, could not litigate on the LLC's behalf. Note: This material is excerpted from the December 2014 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2014 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com

12. In re Living Hope Southwest Medical Services, LLC, 598 F. App'x 467 (8th Cir. 2015) (per curiam).

ONE WHO IS NOT A PARTY OR HAS NOT BEEN TREATED AS A PARTY TO A JUDGMENT HAS NO RIGHT TO APPEAL THEREFROM

Affirming district court's order affirming bankruptcy court's orders denying motions to intervene, for reconsideration and for a new trial, the Eighth Circuit concluded summarily that the bankruptcy court had correctly denied the motion to intervene as untimely. Therefore, the appellant lacked standing to appeal.

13. In re Broos, 534 B.R. 358 (B.A.P. 8th Cir. 2015) (Schermer, J.).

CLAIMS AGAINST IRS EMPLOYEES ARE BARRED BY SOVEREIGN IMMUNITY AND THE BANKRUPTCY COURT PROPERLY SUBSTITUTED THE UNITED STATES AS THE PROPER DEFENDANT; DEBTOR HAS NO STANDING FOR VIOLATION OF DISCHARGE INJUNCTION UNTIL ADMINISTRATIVE REMEDIES ARE EXHAUSTED

Debtors filed an adversary proceeding against IRS employees for levies and tax liens filed post-discharge. The United States filed a motion to dismiss, and the debtors sought default judgment. The bankruptcy court substituted the United States as the sole defendant, denied the default judgment and dismissed the complaint. Affirming, the BAP explained that substitution was proper because the United States was the proper party defendant. "In general, a private litigant may not sue the United States or any of its officers or employees without a waiver of sovereign immunity." The Internal Revenue Code provides such a waiver with respect to suit against the United States in connection with any collection of Federal tax, but sovereign immunity applies with respect to federal employees in tax debt collection cases. Entry of default judgment was not appropriate because the IRS employees were not parties to the action and because the United States had timely entered its appearance and had not failed to plead or otherwise defend against the complaint. Dismissal was proper because under the applicable Internal Revenue Code

provisions the debtors lacked standing for failing to first exhaust available administrative remedies by filing an administrative claim for damages with the IRS.

14. O&S Trucking, Inc. v. Mercedes Benz Fin. Servs. USA (In re O&S Trucking, Inc.), 529 B.R. 711 (B.A.P. 8th Cir. 2015) (Kressel, J.).

APPEAL DISMISSED FOR LACK OF JURISDISCTION DUE TO LACK OF STANDING AND MOOTNESS

The Eighth Circuit BAP dismissed the chapter 11 debtor's entire appeal for lack of jurisdiction. The debtor appealed three orders of the bankruptcy court: 1) an order sustaining, in part, the debtor's objection to claim, 2) an order denying the debtor's motion for reconsideration of the order regarding the debtor's objection to claim, and 3) an order confirming the debtor's proposed amended plan of reorganization. The threshold issue on appeal was whether the BAP had jurisdiction over the appeal.

The BAP initially noted that of the three orders, the confirmation order was the only final, appealable order, and that the other two orders—both the order sustaining, in part, the debtor's objection to claim and the subsequent order denying the motion for reconsideration—were interlocutory orders, which alone, were not appealable without leave of the court. The BAP then noted that interlocutory orders, however, were appealable to the extent that they contributed to a final, reviewable order, e.g., a confirmation order. In a footnote, the BAP also noted that here, even if the other two orders were final, they were untimely under Bankruptcy Rule 8002(a).

With respect to the confirmation order, the BAP dismissed the appeal of that order for lack of standing because the debtor was not an aggrieved party. The BAP explained that "to have standing to appeal the decision of the bankruptcy court, an appellant must be a person aggrieved," that "a party cannot prosecute an appeal from a judgment in its favor," and that "a party may not appeal from a judgment of decree in his favor, for the purpose of obtaining a review of findings he deems erroneous which are not necessary to support the decree." The BAP concluded that because the debtor proposed a plan, obtained confirmation of the plan, and made no claim that the confirmation order was erroneous, then the debtor was not an aggrieved party, and thus, did not have the requisite standing to appeal the confirmation order.

The BAP then dismissed as moot the debtor's appeal of the other two orders. The BAP explained that "a federal court may only exercise jurisdiction over cases and controversies and lacks authority over moot issues." The BAP reasoned that because the debtor no longer had any of the collateral by the time of oral argument, then there was no meaningful relief to grant with respect to valuation of that collateral.

15. In re Diamond, 530 B.R. 451 (B.A.P. 8th Cir. 2015) (Kressel, J).

DISCHARGEABILITY COMPLAINT DISMISSED FOR LACK OF STANDING

The Eighth Circuit BAP affirmed a bankruptcy court's dismissal of a pro se plaintiff's dischargeability complaint. Initially, the pro se party claimed to be a creditor and requested an extension of the debtor's bankruptcy proceedings for sixty days, and asked the court to delay the entry of an order of discharge. The bankruptcy court denied both requests.

After the bankruptcy court entered the discharge and closed the case, the pro se party filed in the Eastern District of Pennsylvania, a dischargeability complaint against the debtor, alleging fraud and defalcation. The case was then transferred to the District Court of Missouri, and then referred back to the bankruptcy court in the Eastern District of Missouri. After the bankruptcy court directed the pro se party to file a motion to reopen the case, the pro se party appealed. The Eighth Circuit BAP reversed, holding that a bankruptcy case need not be reopened to file a dischargeability complaint.

After the bankruptcy court allowed the complaint to be filed, the court issued a show cause order for dismissal. Meanwhile, the debtor answered the complaint and requested dismissal. The bankruptcy court dismissed the complaint. The pro se party then appealed to the Eighth Circuit BAP.

The BAP affirmed the dismissal, concluding that the pro se party lacked standing. The BAP noted that the complaint alleged that the debt was owed to the limited partnerships, not to the pro se party himself. The BAP also noted that complaint alleged that the debtor's actions caused the limited partnership to lose assets, not the pro se party himself. In light of these observations, the BAP held that under the "person aggrieved" doctrine, the pro se party lacked standing to pursue the complaint because he was not personally affected by the debtor's actions. Additionally, the BAP reasoned that under Missouri law, a pro se party may not represent a limited partnership in this context.

The BAP also upheld dismissal for other reasons. The complaint sought an exception to discharge based on "fraud and defalcation," but did not reference a statute. The bankruptcy court construed the complaint as sounding under § 523(a)(4) for fraud or defalcation, and dismissed the complaint as untimely under Federal Rule of Bankruptcy Procedure 4007(c), which requires a dischargeability action for fraud and defalcation be filed within sixty days after the date first set for the meeting of creditors. Because the pro se party's complaint was filed after that sixty-day deadline, the BAP determined that dismissal of the complaint on this basis was proper. On appeal, the pro se party argued that he did not file the complaint under § 523(a)(4). Instead, he argued, the complaint was filed under § 523(a)(3)(B), which excepts unlisted or unscheduled debts from discharge. After applying the four-factored test for determining the merits of a § 523(a)(3)(B) claim, the BAP determined that the pro se party failed to meet the third factor, which requires that the plaintiff have no actual knowledge of the bankruptcy case to be able to timely file a § 523(a)(4) claim. The BAP concluded that because the pro se party knew about the bankruptcy case for more than three weeks prior to the deadline for filing a § 523(a)(4) claim,

then he had actual knowledge of the bankruptcy case in time to file a § 523(a)(4) claim. And that knowledge warranted dismissal of his § 523(a)(3)(B) claim.

16. In re Foster, 516 B.R. 537 (B.A.P. 8th Cir. 2014), *aff'd per curiam*, 602 F. App'x 356 (8th Cir. 2015).

CREDITOR LACKED DERIVATIVE STANDING SUFFICIENT TO SUSTAIN A FRAUDULENT TRANSFER CLAIM

The Eighth Circuit BAP affirmed a bankruptcy court order that dismissed a creditor's fraudulent transfer claim for a lack of standing and denied the creditor's motion for retroactive derivative standing. In the appeal, the creditor raised three issues for review: (1) that the bankruptcy court erred in its derivative standing analysis in finding that the chapter 7 trustee justifiably refused to pursue the fraudulent transfer claim; (2) that the trustee did not consent to the creditor's derivative standing; and (3) that the creditor was equitably estopped from bringing the avoidance action.

The BAP noted that derivative standing is an exception to the general rule that fraudulent transfers may only be avoided by the trustee, and that in the Eighth Circuit, a party seeking derivative standing must prove four separate factors: "(1) the trustee was petitioned to bring the claim and refused; (2) the claim is colorable; (3) permission was sought from the bankruptcy court to initiate the adversary proceeding and (4) the trustee unjustifiably refuse to pursue the claim." In applying these factors to the case, the BAP determined that the second and third factors were non-issues, and focused its discussion on the first and fourth factors.

As to the first factor, the BAP determined that there was no evidence that the trustee refused to pursue the avoidance action; the trustee had simply stated that he would need more information before pursuing it. As to the fourth factor, the BAP noted that this factor required a cost-benefit analysis to determine whether there was a clear benefit to the estate, which may be found after considering the "probability of success in litigation, potential financial recovery, expenses which could be incurred and the delay in case administration." The creditor argued that there was a clear benefit to the estate because the creditor was willing to fund the litigation of the fraudulent avoidance action and if successful in the action, all creditors would be paid in full. The BAP determined that the cost alone did not demonstrate a clear benefit to the estate inasmuch as the creditor, not the estate, would be the primary beneficiary of the avoidance action. Accordingly, the BAP determined that derivative standing should not be permitted.

The creditor argued that he had derivative standing to pursue the fraudulent transfer claim because the trustee did not formally oppose the action. Quoting Eighth Circuit law "that a creditor may proceed derivatively when the trustee (or debtor-in-possession) consents (or does not formally oppose) the creditor's suit," the BAP considered the issue of whether the trustee had consented to the creditor's fraudulent transfer action. The creditor argued that the trustee did not formally oppose the creditor's fraudulent transfer claim because the trustee entered an appearance in the adversary to monitor the case's progress. The BAP reasoned that "consent implies an affirmative action." The BAP noted that the creditor did not obtain either the trustee's informal or formal consent before filing the action. It also noted that the trustee had objected to

the creditor's motion for retroactive approval of standing. The BAP noted that, in any event, in the absence of consent and formal opposition, a bankruptcy court must still find that such suit is "necessary, beneficial, and in the best interests of the estate." The creditor failed to show that the bankruptcy court abused its discretion in finding that granting derivative standing in this instance was not necessary and beneficial to the debtor's bankruptcy case.

Lastly, the creditor argued that the debtor was equitably estopped from raising the issue standing because it was not raised until the eve of trial. The BAP reasoned that standing is an issue of subject matter jurisdiction, which may be raised at any time; therefore, the theory of equitable estoppel did not apply.

17. Westlb AG v. Kelley, 531 B.R. 783 (D. Minn. 2015) (Schlitz, J.).

A CONTINGENT FINANCIAL STAKE IN A CASE AND WEAKENED DEFENSES RESULTING FROM A BANKRUPTCY COURT'S ORDER DO NOT CREATE STANDING TO APPEAL; JUDICIAL ESTOPPEL BASED ON PRIOR PLEADINGS APPLIED TO STANDING

Four groups of lenders to Petters Company, Inc. ("PCI") appealed an order from the bankruptcy court granting the motion of the trustee requesting substantive consolidation of PCI and eight special-purpose entities ("SPEs"). In response, the trustee moved to dismiss the appeals on the basis that the appellants lacked standing to appeal because they have no claims against the bankruptcy estate. The appellants responded that the trustee should be estopped from arguing that they did not have standing and that they did in fact have standing.

The appellants rely on the trustee's statements made in earlier proceedings that the appellate court had jurisdiction over the appeal. In dismissing the appellants estoppel argument, the district court explained, " [j]udicial estoppel is an equitable doctrine under which a court may prevent a party from deliberately changing its position on a legal or factual issue during the course of a lawsuit." "Among the factors a court may consider in deciding whether to apply the doctrine are (1) whether the party's current position is "clearly inconsistent" with its former position; (2) whether the party succeeded in persuading the court to accept its earlier position; and (3) whether the party would derive an unfair advantage or impose an unfair detriment on the opposing party if it were not estopped." The court also stated, "[a]pplication of the doctrine is not warranted when the party's prior position was the product of inadvertence or mistake."

The appellants argued that because the trustee stated in his briefing supporting the motion to certify issues for immediate appeal that "[t]his Court has jurisdiction over this motion and the pending appeal pursuant to 28 U.S.C. §§ 158(a) and 1334 and Federal Rule of Bankruptcy Procedure 8001(f)," that the trustee should be judicially estopped from claiming that the appellate court did not have jurisdiction. In rejecting this argument, the district court stated that "the trustee's earlier assertion regarding jurisdiction is not 'clearly inconsistent' with his current assertion that appellants lack standing, because the trustee was earlier addressing the issue of finality, while now he is addressing the issue of standing." The district court also noted that the failure to raise the issue of standing was likely inadvertent and that the trustee gained nothing by failing to raise the issue of standing. Finally, the district court stated that "there is little prejudice

to appellants in permitting the trustee to raise the issue of standing at this stage." Therefore, the trustee was not judicially estopped from arguing that the appellants lacked standing.

The appellants also argued that they had standing, even if the estoppel argument was unsuccessful. The district court stated, "[i]n order to have standing to appeal a bankruptcy order, an appellant must be a 'person aggrieved' by that order." The district court explained that "the right to participate in proceedings before a bankruptcy court is broader than the 'person aggrieved' status necessary to have standing to appeal . . . to qualify as a 'person aggrieved,' an appellant must have a 'financial stake in the bankruptcy court's order, meaning [it was] directly and adversely affected pecuniarily by the order."

In this case, the appellants claimed that the substantive consolidation order would weaken their defenses in the avoidance actions brought by the trustee. The district court did not agree, rejecting the argument that "being deprived of a defense to an adversary action gives an appellant standing to appeal and order of a bankruptcy court." The district court also disagreed with the appellants' argument that they had "contingent claims" because if they lose the avoidance actions, they will become net losers to the Ponzi scheme and will then be able to assert claims against the estate. The district court stated "appellants' harm is too contingent and indirect to grant them status as 'persons aggrieved." Therefore, the appeals were dismissed.

18. BMO Harris Bank N.A. v. Stoebner, Civil No. 14-1748 (DWF) (D. Minn. Jan. 8, 2015) (Frank, J.).

IN FRAUDULENT TRANSFER CLAIM DISPUTE, DEBTOR DECLARED INSOLVENT AND CREDITOR WAIVED CHALLENGE TO TRUSTEE'S STANDING

The district court affirmed the bankruptcy court's orders and judgments in favor of the chapter 7 trustee in the trustee's fraudulent transfer suit against a bank. The bankruptcy court entered an order of judgment voiding transfers to the bank and an order denying the bank's motion to amend and alternative request for a new trial. On appeal, the bank argued that the bankruptcy court erred in finding that the debtor was insolvent at the time of the transfers. The bank also argued that the bankruptcy court erred in ruling that the bank waived any challenge to the trustee's standing.

First, the bank argued that the bankruptcy court relied on flawed valuation methods, flawed witness testimony, and errors in law in finding that the debtor was insolvent at the time of the transfers in question. The district court determined that the bankruptcy court's insolvency determination was not erroneous because it was supported by expert testimony and other evidence. The district court, with due deference to the bankruptcy court's evaluation of witnesses' credibility, concluded that the bankruptcy court properly relied on the testimony of the trustee's expert whom the bankruptcy court found to be more credible. The district court also held that the bankruptcy court applied the proper legal standard for insolvency under both the Bankruptcy Code and under Minnesota's Uniform Fraudulent Transfer Act.

Second, the bank argued that the bankruptcy court erred in ruling that the bank waived its challenge to the trustee's standing because a court's jurisdiction is never waived. The bank argued that the trustee lacked standing under § 544(b) to pursue the claim because the trustee failed to identify predicate creditors who had requisite standing to pursue any fraudulent transfer claims. The district court agreed with the bankruptcy court and found that the bank confused the issue of lack of standing with the issue of lack of jurisdiction. As to jurisdiction, the district court noted that, indeed, the bank acknowledged the bankruptcy court's jurisdiction over the adversary proceeding under 28 U.S.C. §§ 157, 1334 and Local Rule 1070-1. The district court concluded that the bankruptcy court correctly determined that the bank waived its challenge to the trustee's standing as it related to the existence of predicate creditors. The district court determined that the trustee carried his burden predicate creditors were named in his amended complaint. Examining the record as a whole, the district court concluded that the bank had waived its challenge to the trustee's standing. The bank did not challenge the existence of predicate creditors even after the trustee identified predicate creditors in his amended complaint. The district also observed that the bank wrote in its trial brief that the sole issue for trial was whether the debtor was insolvent.

19. In re Robb, 534 B.R. 354 (B.A.P. 8th Cir. 2015) (Kressel, J.).

DEBTOR'S FAILURE TO QUALIFY AS A PERSON AGGRIEVED MEANT DEBTOR LACKED STANDING TO APPEAL ORDER RELATING TO A CLAIM OBJECTION

After the chapter 7 trustee discovered a defect in the debtor's deed of trust, the debtor converted his case to one under chapter 13. The chapter 7 trustee then filed an unsecured proof of claim. The debtor objected. The bankruptcy court overruled his objection. The debtor then appealed. The BAP, *sua sponte*, dismissed the appeal for lack of jurisdiction.

The court held that the debtor lacked standing because he did not qualify as a "person aggrieved." The "person aggrieved doctrine" limits standing to persons with a financial stake in the bankruptcy court's order, meaning they must be directly affected pecuniarily by the order. A person qualifies as a "person aggrieved" when an order diminishes his property, increases his burden, or impairs his rights. Debtors typically lack standing to object to claims or orders relating to them due to a lack of pecuniary interest in the distribution of the estate's assets, except when an asset surplus exists that may be returned to the debtor.

Here, the debtor's obligation, a $590.00 monthly payment under the plan, remained the same despite the chapter 7 trustee's claim and the claim's impact on other creditors. Thus, the debtor lacked standing, resulting in dismissal of the case for lack of jurisdiction.

PROCEDURE

20. In re Behrens, 577 F. App'x 633 (8th Cir. 2014) (per curiam).

CAN'T CHALLENGE CRIMINAL RESTITUTION AWARD OF A CRIMINAL SENTENCE IN AN ADVERSARY PROCEEDING IN BANKRUPTCY

The Court of Appeals affirmed the BAP dismissal of the debtor's adversary complaint, summarily finding that the complaint sought to collaterally attack a final criminal judgment.

21. Kelley v. Opportunity Finance, LLC, 2015 WL 321536 (D. Minn. 2015) (Davis, J.).

A MOTION TO WITHDRAW REFERENCE BROUGHT FOUR YEARS AFTER THE CASE IS COMMENCED CONSTITUTES UNREASONABLE DELAY

The chapter 11 Petters case trustee brought an avoidance action in bankruptcy court, and the defendants sought to withdraw the reference pursuant to 28 U.S.C. § 157(d) for cause. While the district court found the defendants' motion to withdraw to be ripe as a legal question requiring no further factual development, it denied the motion as untimely because the four years the defendants waited to bring the motion constituted an unreasonable delay after "the bankruptcy court invested significant time and resources into this and hundreds of related adversary cases." In rejecting the defendants' argument that the *Bellingham* decision supported the motion to withdraw, the district court noted that "[i]f anything, *Bellingham* strengthens the basis for denying a withdrawal by affirming that *Stern* claims can be heard by the bankruptcy court and simply reviewed de novo by the district court." The district court also noted that the motion to withdraw had to be denied because the defendants failed to comply with Bankruptcy LR 5011-1, which required that the defendants first request a transfer from the bankruptcy court before bringing the motion to withdraw before the district court. Finally, the district court noted that judicial efficiency would be promoted, not undermined, by allowing the bankruptcy court to proceed even if the bankruptcy court did lack the authority to enter a final judgment.

22. In re Web2B Payment Solutions, Inc., 2015 WL 1815864 (D. Minn. 2015) (Doty, J.).

MOTION FOR INDICATIVE RULING DENIED; MOTION TO INTERVENE FOR LIMITED PURPOSE GRANTED

On appeal of a bankruptcy court judgment against the plaintiff, the district court denied the plaintiff's motion for indicative ruling and granted a third-party's motion to intervene for the limited purpose of objecting to the plaintiff's motion for indicative ruling.

After Web2B Payment Solutions, Inc. filed bankruptcy, North American Banking Company ("NABC") turned over funds that were held in Web2B's accounts to the bankruptcy trustee. Rent–A–Center East, Inc., filed an adversary proceeding against the trustee, claiming an interest in those funds. The trustee moved for summary judgment. The bankruptcy court granted

summary judgment in favor of the trustee and against Rent-A-Center, ruling that Rent-A-Center had no right to the disputed funds. Rent-A-Center appealed to the district court. The district court affirmed and denied Rent-A-Center's subsequent motion for rehearing. Rent-A-Center then appealed both orders to the Eighth circuit.

In the meantime, Rent-A-Center had also sued NABC in district court for conversion of the funds in dispute. When NABC moved for summary judgment, Rent-A-Center moved to stay the district court proceeding, pending appeal of the orders in the bankruptcy adversary proceeding. The district court granted that stay request.

While on appeal, Rent-A-Center and the trustee agreed to a settlement, subject to bankruptcy court approval and subject to the district court vacating the appealed orders. At the bankruptcy court hearing on the settlement, Rent-A-Center disclosed its intent to seek vacatur of the district court orders because, in its view, the district court made findings that would affect litigation with NABC. The bankruptcy court did not approve the settlement, stating that vacating the orders would subvert the judicial process.

In the district court, Rent-A-Center moved under Federal Rule of Civil Procedure 62.1 for an indicative ruling that the district court would vacate its orders under Federal Rule of Civil Procedure 60(b)(6) upon Eighth Circuit remand for that purpose. In response, NABC moved under Federal Rule of Civil Procedure 24(b) to intervene for the limited purpose of challenging Rent-A-Center's motion for indicative ruling. The district court explained that under Rule 24(b), "the court may permit anyone to intervene who . . . has a claim or defense that shares with the main action a common question of law or fact." Finding that the motion to intervene was timely and that common questions existed both in the district court case and the adversary proceeding, the district court granted NABC's motion to intervene. Rent-A-Center argued that the district court lacked jurisdiction over the motion to intervene because the case was on appeal. The district court, however, determined that it had jurisdiction over the motion because it was filed for the limited purpose of objecting to the motion for indicative ruling. To decide the motion for indicative ruling, the district court first determined whether sufficient cause existed to vacate its prior orders under Rule 60(b)(6). The district court found there were no extraordinary circumstances to justify relief of vacating the prior orders under Rule 60(b)(6), and that avoidance of adverse effects on other litigation did not qualify as an extraordinary circumstance to justify vacatur.

23. In re Sky Ventures, LLC, 523 B.R. 163 (Bankr. D. Minn. 2015) (Ridgway, J.).

CREDITOR CANNOT CHALLENGE THE DETERMINATIONS OF AN ORDER IF IT DID NOT TIMELY OBJECT OR APPEAL THAT ORDER; RULE 60 RELIEF IS LIMITED

About 6 weeks postpetition, this chapter 11 debtor filed a motion under § 365(a) seeking rejection of an unexpired lease of nonresidential real property with MacGillivray Ranch, LLC. The debtor had been delinquent in payment of rent and all the parties agreed that the lease qualified as an unexpired nonresidential real property lease under § 365.

The motion sought an order regarding: (1) rejection of the lease; (2) setting a retroactive date for rejection to May 14, 2014, the date of the petition; and (3) setting a claims bar date for rejection damages as thirty days from the date of the order approving the rejection motion. The landlord, MacGillivray, was properly served, but there were no objections to the motion and the order was entered approving all relief sought by the debtor. MacGillivray did not appeal the order. It did, however, file a motion requesting that the rejection date be changed from the petition date to the date of the order, and requested an administrative claim for postpetition rents and other assessments totaling $36,629.89. The debtor objected, claiming that its damages should be prepetition contract breach damages and that there should not be an allowed administrative expense. MacGillivray failed to file a rejection damages claim within the ordered 30 days but did file a proof of claim by the proof of claim deadline.

Despite discussion of Code §§ 362, 502, and 503, the bankruptcy court stated that the bottom line issue "is whether MacGillivray is precluded from advancing its claim because of the Court's prior order, one to which MacGillivray neither objected to, nor appealed from." Because MacGillivray received advance notice of the debtor's motion and it did nothing, the order became final and MacGillivray cannot challenge the determinations in the order.

MacGillivray also requested that the court reconsider its prior order under Federal Rule of Bankruptcy Procedure 9024 and Federal Rule of Civil Procedure 60. As an initial matter, the court noted that this request was procedurally improper because MacGillivray requested relief under Rule 60 in a supplemental briefing, not in a separate motion as required under Rule 60(b). However, the court also noted that even on the merits, Rule 60(b)(1) would not provide MacGillivray a basis for relief. Under Rule 60, a party must show "mistake, inadvertence, surprise, or excusable neglect." Rule 60(b)(3), which requires a showing of fraud, misrepresentation, or misconduct by the opposing party, would similarly be unavailable in this case. MacGillivray presented no basis to grant relief under either provision.

The court also considered whether the motion of MacGillivray could be deemed an informal proof of claim to satisfy its 30 day time period for the filing of a rejection damages claim. The court concluded, after discussion, "no." The motion by MacGillivray was denied in its entirety, as well as its request for allowance of its prepetition contract damages as an administrative claim.

24. In re Le, Bky. No. 13-32274 (Bankr. D. Minn. March 20, 2015) (Kishel, J.).

REMOVAL CANNOT BE INVOKED FROM A BANKRUPTCY COURT TO A DISTRICT COURT IN THE SAME DISTRICT; REMOVAL EXPLAINED

Wells Fargo Bank, N.A. filed a motion for relief from stay seeking leave to prosecute an eviction action in the Minnesota state courts. Less than twenty four hours before the hearing, debtors (pro se) filed a notice of removal to the United States District Court. A hearing was held and the court explained why the hearing was not halted in deference to the debtors' removal request. The court subsequently issued a written reprisal of that explanation regarding removal and the effect it has on the court.

The court explained, "removal of 'any claim or cause of action in a civil action . . . to the [federal] district court,' at the unilateral instance of a party . . . simply does not apply to the posture and venue of the proceeding in question, i.e., the motion for relief from stay." Removal cannot be invoked from a bankruptcy court to the district court in the same district because they are ostensibly the same court. "The 'bankruptcy court' for a particular judicial district is comprised of the bankruptcy judges in regular active service for the district. Though, as a collective the bankruptcy judges . . . 'shall constitute a unit of the district court.'" The division of labor between the bankruptcy court and the district court "do not set up the bankruptcy court as a separate court in the jurisdictional senses; i.e., they do not create a separate jurisdiction . . . ."

The court further explained, "removal takes a civil action from one court of independent and competent jurisdiction . . . to a federal district court that must have the prerequisites for exercising bankruptcy jurisdiction in its own right." Removal "does not apply between two federal court units of the same district." "Removal . . . involves crossing a line drawn by external principles of jurisdiction and venue; and in the case of two separate court units of the same federal judicial district there is no such line."

"[A] party to a proceeding in a bankruptcy case cannot itself invoke removal to push that proceeding from the bankruptcy judge presiding over it . . . to the district court that originally made the reference." "Only a district judge may bring about such a transfer . . . by pulling the proceeding back from the reference. That is done only by a party's request to the district judge, which request is made by a motion to the district court for withdrawal of reference under 28 U.S.C. § 157(d)." Because the debtors in this case did not use that procedure, the judge had no obligation to put the hearing on hold in response to the debtors' request for removal.

25. Nhut Le v. Wells Fargo Bank, N.A., 595 F. App'x 661 (2015).

DISMISSAL OF PRO SE DEBTORS' FILINGS FOR FAILURE TO MEET PLEADING STANDARDS AFFIRMED BY EIGHTH CIRCUIT

Debtors did not vacate their home after a foreclosure and sheriff's sale. Lender began an eviction action in Minnesota state court. Before lender completed the eviction, debtors filed for bankruptcy and removed the eviction to bankruptcy court. Debtors then filed an adversary proceeding against lender and its law firm (the "defendants") alleging 33 counts including civil rights violations, FDCPA violations, RICO Act violations, and treason. Debtors then filed a similar complaint in federal district court. Debtors removed the bankruptcy, adversary proceeding, and eviction action to federal district court, which consolidated the cases and referred the matter to a magistrate judge. Defendants filed a motion to dismiss the adversary proceeding and complaint for failure to meet *Twombly* and *Iqbal* pleading standards, remand the eviction to state court for lack of federal jurisdiction, and sever the bankruptcy case.

The magistrate judge recommended severing the bankruptcy, noting the debtors did not oppose the defendants' motion to sever. With regard to the eviction proceeding, the magistrate judge noted no federal question jurisdiction existed because the case raised no questions of federal law, nor was there diversity jurisdiction because the defendants (who were the plaintiffs in the eviction action) brought their claim in the debtors' state of residence. The magistrate judge recommended dismissing the adversary proceeding and accompanying (nearly identical) complaint for failure to meet pleading standards, since debtors' 90-page complaint failed to reference any factual details supporting their claims. The magistrate judge did not stop there: "it is noteworthy that many of the counts have no relevance to the circumstances of this case and were obviously included without any cogent and meaningful thought whatsoever as to how they might provide [the debtors] a means to obtain relief." *Nhut Le v. Wells Fargo Bank, NA,* 2014 WL 1672260 (page 7).

The district court adopted the magistrate judge's recommendations in their entirety. The Eighth Circuit affirmed, holding the debtors' complaint "was devoid of factual allegations and contained only conclusory legal theories." *Nhut Le v. Wells Fargo, N.A.*, 595 F. App'x 661 (2015).

AUTOMATIC STAY

26. In re Carter, 583 F. App'x 560 (8th Cir. 2014) (per curiam).

SANCTIONS UNDER § 362(k) WERE NOT APPROPRIATE WHERE THE CREDITOR'S VIOLATION OF THE AUTOMATIC STAY WAS NOT WILLFUL

The debtor was the owner and sole member of a logging company, but unbeknownst to the bank, prior to the bankruptcy filing, the husband assigned the assets of the logging company to himself. The debtor received notice of the filing of the bank's state court replevin suit, but he did not respond to the suit or file any objections until after the state court issued an order of delivery that granted the bank the right to immediate possession of the logging equipment. The debtor filed a motion alleging that the bank violated the automatic stay. The Eighth Circuit observed that the automatic stay under 11 U.S.C.A. § 362(a) becomes effective upon the filing of the bankruptcy petition and precludes any action attempting to enforce the collection of a pre-petition obligation. "Section 362(k)(1) provides that a debtor injured by a 'willful' violation of the automatic stay 'shall recover actual damages, including costs and attorneys' fees[.]' " "To recover under § 362(k), the debtor must show that the creditor's violation of the automatic stay was willful[.]" In order for the action "[t]o be willful, a creditor must take action that is deliberate and with the knowledge that a bankruptcy petition has been filed," the court said. The Eighth Circuit ruled that debtors' argument failed. "At issue in this case is the Bank's knowledge of the assignment, coupled with knowledge of [debtors'] bankruptcy petition. The Bank was unaware of the assignment or [debtors'] bankruptcy petition when it initially sought replevin. It did not become aware of either event until [the husband debtor] filed his motion in state court. Due to the Bank's lack of knowledge prior to this time, a willful violation of the stay could not have occurred," the Eighth Circuit held. Note: This material is excerpted from the January 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

27. In re Gess, 526 B.R. 798 (B.A.P. 8th Cir. 2015) (Federman, J.).

THE DEBTOR, AS THE ONLY DESIGNEE UNDER THE WILL OF THE DEBTOR'S DECEASED FATHER, WHO HAD BEEN THE RECORD TITLE HOLDER OF AN AUTOMOBILE, HAD AT LEAST AN EQUITABLE INTEREST IN THE VEHICLE, AND THUS, THE SECURED CREDITOR CORRECTLY SOUGHT STAY RELIEF TO REPOSSESS THE VEHICLE

The debtors filed a joint chapter 7 bankruptcy petition, pro se. A credit union moved for stay relief regarding an automobile, which had been owned by the father of one of the debtors, but which was in the debtors' possession. The debtors opposed the motion, but the bankruptcy court granted the credit union relief under both subparagraphs (1) and (2) of 11 U.S.C.A. § 362(d), for reasons stated on the record at the conclusion of the hearing on the motion. The BAP observed that § 362(a) generally provides for an automatic stay against taking any action against property of the estate—once a bankruptcy petition is filed. The BAP addressed the debtors' three primary arguments as to why the stay should not have been lifted: (1) that they did not have an

ownership interest in the vehicle; (2) that the credit union's lien was no good or was not enforceable against them; and (3) that the credit union's interest was adequately protected because the vehicle was insured. The BAP found the vehicle to be property of the bankruptcy estate and thus subject to the automatic stay. The debtors asserted that because the credit union failed to establish "color of title," and that they had no ownership interest in the van. Indeed, the BAP noted that the bankruptcy court found, and the debtors did not dispute, that the certificate of title on the vehicle listed the debtor's father as the sole owner. The BAP noted, as the bankruptcy court did, that if that had been the end of the inquiry, the credit union would not have needed stay relief to repossess the vehicle. But, 11 U.S.C.A. § 541(a)(1) broadly defines property of the estate to include "all legal or equitable interests of the debtor in property as of the commencement of the case." Here, by the time the debtors filed their bankruptcy case, Mr. Gess's father had passed away, leaving him as the sole designee under his father's will, which had been made part of the record. As a result, the bankruptcy court found that Mr. Gess had an equitable interest in the van, and that it was property of the estate. Accordingly, the BAP found that the credit union correctly sought stay relief before exercising its rights in the vehicle and concluded that the bankruptcy court had not clearly erred in that holding. The BAP also agreed with the bankruptcy court that the credit union had properly perfected its security interest in the vehicle. Further, the BAP concluded that because the credit union established that its interest was not adequately protected, the bankruptcy court did not clearly err in determining that cause existed for stay relief under § 362(d)(1). Finally, the BAP held that the bankruptcy court "did not clearly err in granting relief from the stay under § 362(d)(2)." Note: This material is excerpted from the May 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

28. In re Gray, 519 B.R. 767 (B.A.P. 8th Cir. 2014) (Kressel, J.), *reh'g denied*, 525 B.R. 441 (B.A.P. 8th Cir. 2014).

BANKRUPTCY COURT'S AWARD OF PUNITIVE DAMAGES REVERSED WHERE THE BANKRUPTCY COURT DID NOT MAKE SPECIFIC FINDINGS OF FACT AS TO THE LANDLORD'S MOTIVE OR EGREGIOUS CONDUCT IN VIOLATING THE STAY

The bankruptcy court awarded damages—including punitive damages—for a landlord's violation of the automatic stay. For purposes of a stay violation, the bankruptcy court had to determine two things: (1) whether the landlord had knowledge of the bankruptcy filing; and (2) whether it acted deliberately. The BAP found that both of the elements were easily met and it could not say that the bankruptcy court's finding that the landlords willfully violated the automatic stay was clearly erroneous. Nor could the BAP say that the bankruptcy court's finding of actual damages was clearly erroneous. The BAP then turned to the issue of punitive damages against the one landlord. On this component, the BAP noted that the Eighth Circuit has held that an award of punitive damages in the context of a willful stay violation requires egregious, intentional misconduct on the part of the party that violated the stay. Here, the bankruptcy court awarded the punitive damages based on the one landlord's "consistent abdication of responsibility," but the bankruptcy court did not make specific findings of fact as to the landlord's motive or egregious conduct in violating the stay. The BAP found that the landlord's

failure to appear for a trial did not satisfy the Eighth Circuit test of egregious, intentional misconduct. Accordingly, the BAP concluded that the bankruptcy court abused its discretion in awarding punitive damages. Note: This material is excerpted from the January 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

29. Ritchie Capital Management LLC v. Opportunity Finance, LLC, Court File No. 27-CV-13-17424 (Hennepin County Minnesota District Court Jan. 15, 2015) (Robiner, J.).

STATE COURTS HAVE JURISDICTION TO DETERMINE IF AUTOMATIC STAY APPLIES; THE AUTOMATIC STAY APPLIES TO ACTIONS THAT ARE DERIVED FROM ACTIONS AVAILABLE TO THE DEBTOR

This case involved the fallout from the Ponzi scheme operated by Tom Petters. On Sep. 24, 2013, in Minnesota state court, plaintiffs, late investors in Petter's Ponzi scheme, brought this case and, in broad terms, alleged that the defendants, early investors in the Ponzi scheme, had demanded that Petters accelerate repayment of loans with knowledge that Petters would have to defraud new investors to make those payments.

On Oct. 11, 2013, the defendants removed to federal court. The plaintiffs then moved for remand on the grounds of mandatory abstention while the defendants moved the federal district court to refer the case to the bankruptcy court. Around the same time, the trustee in the bankruptcy case moved to enjoin the federal district court from proceeding pending resolution of the trustee's claims against the same defendants in the bankruptcy court on similar claims. The bankruptcy court denied the trustee's request and the federal district court remanded the case back to the state court on the grounds of mandatory abstention. After remand, the defendants brought a motion to dismiss asserting that the automatic stay provisions of the bankruptcy code prevented the state court from adjudicating the plaintiffs' claim and secondarily, that plaintiffs failed to state a cause of action.

The first issue the state court considered was its own jurisdiction to rule on whether the automatic stay applied in the case. The court noted that federal courts have "original but not exclusive jurisdiction of all civil proceedings arising under title 11 or related to [a] case under title 11." The court further noted that neither the Judiciary Code nor the bankruptcy code deprives a state court of jurisdiction. The court cited Siskin v. Complete Aircraft Services, Inc. (In re Siskin), 258 B.R. 554, 563 (Bankr. E.D.N.Y. 2001), for the proposition that "the only aspect of a bankruptcy court proceeding over which district courts and their bankruptcy units have exclusive jurisdiction is the bankruptcy petition itself; in other matters arising in or relating to bankruptcy cases . . . state courts have concurrent jurisdiction, and Bankruptcy Courts are prohibited from relitigating these matters if state courts have already resolved them." The state court found that it had jurisdiction to determine whether the automatic stay provisions of § 362(a) applied to the case.

The next issue the court addressed was whether the current action was stayed as a result of the automatic stay. The defendants asserted that because the action in this case derived from an action available to the debtor, this action had to be stayed. The state court rejected the argument that the federal district court's exercise of mandatory abstention controlled this issue, stating that the abstention "does not compel an automatic stay." The state court then examined two lines of cases, establishing that the automatic stay applies to actions against third parties if "the plaintiffs' rights were 'completely derivative'" of the bankruptcy estate's claims. A claim is derivative if there is no "particularized injury traceable to the defendants," and there are "no direct duties owed by defendants to plainitiffs." If a claim is "based on separate facts, theories, and duties than the [bankruptcy estate's] . . . claims," the claims are beyond the reach of the automatic stay. The court stated, "[p]laintiffs allege facts that are virtually identical to the allegations contained in the Trustee's adversarial proceeding" and that the plaintiffs "do not allege any duty owed by Defendants to Plaintiffs; they do not allege any misconduct or misrepresentations by Defendants to Plaintiffs." The state court concluded that the automatic stay should stay this proceeding.

Finally, the court noted that it would not rule on any other defenses brought by the defendants due to the stay, but did comment on them briefly since they "underscore" the sensibility of staying the action. The state court noted numerous pleading deficiencies and that the remedies sought in this action were properly remedies sought in bankruptcy court.

EXEMPTIONS

30. In re Hardy, 787 F.3d 1189 (8th Cir. 2015) (Melloy, J.).

ADDITIONAL CHILD TAX CREDIT (ACTC) IS A PUBLIC ASSISTANCE BENFIT

The debtor sought to exempt the portion of her tax refund attributable to the Additional Child Tax Credit (ACTC) as a public assistance benefit under state law (Missouri). The bankruptcy court sustained the trustee's objection on the basis that the credit did not only benefit the needy and because the purpose of the tax credit was to ease the tax burden on working families and promote family values. The BAP affirmed the bankruptcy court, concluding that because non-needy families (married filing jointly with adjusted gross income in excess of $100,000) were potentially eligible for the credit, and because the ACTC also required a minimum income threshold that the most needy would not meet, it was not a public assistance benefit.

On appeal, the Eighth Circuit reversed, holding that because the legislative intent of ACTC, as documented through amendments, was to help low-income families, the credit at issue qualifies as a public assistance benefit. The court noted that, while defined in other parts of its code, the Missouri definitions of "public assistance benefit" did not aid in the application of the term with respect to a federal tax refund. The court next sought to determine the federal congressional intent behind the term, and agreed with the BAP that "public assistance benefit" generally means those government benefits provided to the needy. But, the court determined, after a lengthy review of the legislative history from its original passing in 1997 through each amendment, that the legislative purpose of the ACTC is to benefit low-income families, and that it has fulfilled that legislative intent in practice by overwhelmingly benefitting low-income families. The court

found that the BAP had focused too narrowly on the statute only as originally enacted without due consideration of the various amendments and legislative purposes behind those amendments.

31. In re Miller, 778 F.3d 711 (8th Cir. 2015) (Gruender, J.).

AN ANNUITY THAT THE DEBTOR PURCHASED WITH FUNDS FROM THE DEBTOR'S QUALIFIED INDIVIDUAL RETIREMENT ACCOUNT UNDER § 408(a) OF THE INTERNAL REVENUE CODE WAS EXEMPT UNDER § 522(b)(3)(C)

The debtor identified the funds in his annuity as exempt under 11 U.S.C.A. § 522(b)(3)(C), which allows a debtor to protect from creditors "retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under section . . . 408 . . . of the Internal Revenue Code." The court then observed that 26 U.S.C.A. § 408(a), (b), (e)(1), in turn, provide that an individual retirement account and an individual retirement annuity are exempt from taxation; that is, they are qualified retirement plans. "Thus, if retirement funds are held in either of these qualified retirement plans, then the funds can be exempted from creditors' claims in bankruptcy. This exemption generally applies even if the debtor transferred the retirement funds to the qualified retirement plan from another qualified retirement plan," the court said. In this case, it was undisputed that the funds used to purchase the debtor's annuity were retirement funds that came from his individual retirement account, which was a qualified individual retirement account under § 408(a) of the Internal Revenue Code. Had the debtor simply left the funds in his individual retirement account, there was no question but that the funds would be exempt, the court said. But because the debtor used the funds to purchase the annuity, the trustee contended that the funds became property of the estate. The court observed that critical to the trustee's argument was her assertion that debtor's annuity was not a qualified individual retirement annuity within the meaning of § 408(b), which enumerates several requirements for an annuity to be a qualified individual retirement annuity, two of which were at issue in this case. The first was § 408(b)(2)(A), which provides that "[u]nder the contract . . . the premiums are not fixed," and the second was § 408(b)(2)(B), which states "[u]nder the contract . . . the annual premium on behalf of any individual will not exceed the dollar amount in effect under section 219(b)(1)(A) [of the Internal Revenue Code]." Here, the cap was $6,000 for the taxable year in question. The trustee contended that the debtor's annuity failed both requirements, i.e., because debtor's annuity contract required him to pay a lump-sum amount to the insurance company, $267,319.48, the trustee characterized the annuity's "premium [ ]" as "fixed," in violation of § 408(b)(2)(A), and because the annuity contract allowed the debtor to pay more than $6,000 in one year for the annuity, the trustee argued that the annuity's "annual premium" exceeded the limit set by §§ 408(b)(2)(B) and 219(b)(1)(A). In contrast, the debtor asserted that the funds he used to purchase the annuity, which came from his qualified individual retirement account, were not a "premium" subject to § 408(b). The Eighth Circuit concluded that the debtor had the better argument. "A premium does not include funds, such as [the debtor's in this case], that are taken from a qualified individual retirement account to pay for an individual retirement annuity. Though § 408 does not define the term 'premium,' § 408(b)(2)(B) sets the maximum annual premium by incorporating the amount from § 219(b)(1)(A). This linkage of statutory provisions is significant, for it conveys that an annual premium does not encompass funds that already were contributed to a qualified retirement plan. To explain, § 219(b)(1)(A) lists the maximum 'qualified retirement contribution[ ]' that is 'allowed as a deduction. . . for the taxable year,' "

the court stated. Note: This material is excerpted from the April 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

32. Boellner v. Dowden, 2015 WL 2193045 (8th Cir. 2015) (per curiam).

EXEMPTION STACKING DISALLOWED; SUBSTANTIVE CONSOLIDATION OF SPOUSE'S CASES WHEN SUBSTANTIAL IDENITY AND HARM TO CREDITORS

The Boellner's lived separately. Marilyn's home was unencumbered and valued at $450,000.00, while Samuel's home was in the process of being surrendered to the mortgage holder. Moreover, the Boellners had separate insurance policies, separate interests in businesses, separate annuities, and separate IRAs. Samuel owned annuities and IRAs valued at more than $700,000.00. Samuel and Marilyn had individual credit card debt. In contrast, the trustee argued that the Boellners' assets, liabilities, and handling of financial affairs were substantially the same and their cases should be substantially consolidated: among other things, they shared a checking account, several credit cards and a leased car, they jointly owed taxes, and they jointly withdrew funds from IRAs. Boellner's counsel explained they filed separate petitions, because doing so allowed them to take advantage of both the federal and state exemptions. After reviewing the bankruptcy schedules and statements of financial affairs, the bankruptcy court ordered substantive consolidation. The Boellners appealed, asserting that the evidence was insufficient to support the outcome.

In affirming the bankruptcy court's order which was affirmed by the district court, the Eighth Circuit Court found sufficient evidence to support the governing issues. It explained "[i]n assessing the propriety of substantive consolidation, a court must determine: (1) whether there is a substantial identity between the assets, liabilities, and handling of financial affairs between the debtor spouses; and (2) whether harm will result from permitting or denying consolidation." "Ultimately, the court must be persuaded that the creditors will suffer greater prejudice in the absence of consolidation than the debtors (and any objecting creditors) will suffer from its imposition." The appellate court noted that the bankruptcy court determined that "the creditors will suffer great prejudice because if the exemptions were allowed to be stacked . . . [the creditors] would in all likelihood receive no distribution or significantly less distribution than they would if this was a joint case." The Eighth Circuit Court found that the bankruptcy court did not abuse its discretion in ordering joint administration and substantive consolidation and affirmed its decision.

33. In re Dmitruk, 517 B.R. 921 (B.A.P. 8th Cir. 2014) (Federman, J.).

REFUND MUST BE INTENDED TO ADDRESS THE BASIC ECONOMIC NEEDS TO BE EXEMPT UNDER MINNESOTA LAW

In this case, the debtor claimed his federal and state income tax refunds as exempt under Minn. Stat. § 550.37, subd. 14, as "government assistance based on need." The bankruptcy court, ruling on the Chapter 7 Trustee's objections to the exemptions, allowed and denied certain portions of the exemptions. The chapter 7 trustee appealed the allowance of an exemption of $1,357 based on the Minnesota K-12 Education Credit.

In affirming the bankruptcy court's decision, the Eighth Circuit BAP stated "[p]rimarily, in order to be exempt, the refund must be intended to 'address the basic economic needs of low-income recipients.'" The appellate court noted that the Minnesota K-12 Education Credit is "phased out at relatively low income levels, similar to the income thresholds applicable to the federal Earned Income Credit and the Minnesota Working Family Credit . . . ." Furthermore, the court stated that "[e]ducation–like food and medical care–is a basic need of all children in Minnesota, and we believe the Education Credit's ultimate purpose is to assist people with low incomes in providing an education for their children." Based on this reasoning, the BAP permitted the debtor's claimed exemption and affirmed the bankruptcy court.

AVOIDANCE & OTHER TRUSTEE POWERS

34. Ritchie Capital Management, L.L.C. v. Kelley, 785 F.3d 273 (8th Cir. 2015) (Bye, J.).

THE BANKRUPTCY DID NOT ERR IN APPROVING SETTLEMENT AGREEMENT IN PONZI SCHEME CASE

The Eighth Circuit began its opinion by noting that a "bankruptcy court's approval of a settlement will not be set aside unless there is plain error or abuse of discretion." The court added, however, that a settlement is not required to constitute "the best result obtainable;" instead, the standard for evaluation "is whether the settlement is fair and equitable and in the best interests of the estate" and the trial court need only ensure that "the settlement does not fall below the lowest point in the range of reasonableness." In any event, the court must consider: "'(A) the probability of success in the litigation; (B) the difficulties, if any to be encountered in the matter of collection; (C) the complexity of the litigation involved, and the expense, inconvenience and delay necessarily attending it; and (D) the paramount interest of the creditors and a proper deference to their reasonable views in the premises.'" The appellant first challenged the bankruptcy court's approval of the allocation by contending that the allocation was wholly gratuitous, that it provided nothing to the creditors of Petters's corporation, and was without consideration. The Eighth Circuit didn't buy it: the appellant's "argument again overlooks that the settlement agreement was subject to approval by the bankruptcy court and the district court prior to it being enforceable . . . and a bankruptcy court may approve a settlement even though it may not be 'the best result obtainable.'" The Eighth Circuit also rejected the appellant's argument that the chapter 11 trustee had a conflict of interest and that the settlement agreement

had been unreasonable. Finally, the circuit court rejected the appellant's assertion that the allocation ran counter to the coordination agreement which governed the relationship between the receivership and the bankruptcy estate, explaining that "[a]lthough the claims pursued by [the Chapter 11 trustee] as the trustee and the receiver against [the assignee] are similar, they stem from separate wrongful conduct. The trustee's claims are derived from . . . conduct [of Petters's corporation], while the receiver's claims are based upon Petters's conduct. Consequently, the claims are not parallel. Additionally, [the appellant's] argument regarding the lack of a recovery from the same source bank account overlooks the broad language included in the coordination agreement which does not limit the variety of claims which the trustee and the receiver can bring. In other words, merely because the circumstances of this specific case did not result in parallel claims does not preclude parallel claims from existing under other circumstances," the court said. Note: This material is excerpted from the April 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

35. Ritchie Capital Management, LLC v. Stoebner, 779 F.3d 857 (8th Cir. 2015) (Riley, C.J.).

WITHOUT ADOPTING A "PONZI SCHEME PRESUMPTION," EIGHTH CIRCUIT HOLDS THAT A SUFFICIENT NUMBER OF BADGES OF FRAUD SURROUNDED THE DEBTOR'S PRE-PETITION ENCUMBRANCE OF ITS TRADEMARKS TO GIVE RISE TO A PRESUMPTION OF FRAUD

"[O]ur cases have used the inferential 'badges of fraud' approach to determine whether a debtor acted with 'intent to hinder, delay, or defraud[ ]' a creditor regardless of whether the intent language came from a state fraudulent transfer statute or applicable bankruptcy law," and "[o]nce a trustee establishes a confluence of several badges of fraud, the trustee is entitled to a presumption of fraudulent intent. In such cases, 'the burden shifts to the transferee to prove some legitimate supervening purpose for the transfers at issue,'" namely that the transferee accepted the transfer in good faith and for value within the meaning of § 548(c). The Eighth Circuit noted that, in undertaking its badges of fraud analysis, the bankruptcy court had found five of the badges listed in the UFTA, but had observed that the badges "do not lie perfectly on their wording, for this case." The Eighth Circuit disagreed with the appellants' contention that this observation was an acknowledgment by the bankruptcy court that the badges of fraud did not apply. After considering the bankruptcy court's analysis, the Eighth Circuit stated—rather pragmatically—that while it might not have "totally agree[d] with the bankruptcy court's analysis and application of all the badges, the bankruptcy court did not err in concluding the trustee was entitled to a presumption of actual fraudulent intent." Note: This material is excerpted from the April 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

36. In re Pierce, 779 F.3d 814 (8th Cir. 2015) (Shepherd, J.).

IN A SPLIT DECISION, EIGHTH CIRCUIT HOLDS THAT THE DEFENSE FOR CONSUMER DEBTOR PAYMENTS UNDER $600 CONTAINED IN § 547(c)(8) APPLIED

During the preference period, a collection agency garnished the wages of the husband debtor, totaling $858.98, during six pre-petition pay periods. The husband's employer sent the first four garnishments, totaling $562.78, to the state court that issued the garnishment order, and that court, in turn, delivered the payments to the collection agency in accord with state garnishment law. The debtors then filed their bankruptcy petition, and notified the state court that they had done so. When the state court later received the final two garnishments, which totaled $296.20, instead of delivering those funds to the collection agency, it returned the money to the debtor's employer, which then refunded the money to the debtor. The Eighth Circuit stated that the debtors brought their preference action under 11 U.S.C.A. § 522(h), which allows a debtor to "avoid a transfer of property of the debtor" if, among other things, the trustee could avoid the transfer under 11 U.S.C.A. § 547. The court also noted that § 547(b) provides that "the trustee may avoid any transfer of an interest of the debtor in property" that meets the requirements of § 547(b). In this case, the parties agreed that these requirements were met in a prima facie sense. But the court noted, however, that the trustee's avoidance power is subject to certain defenses, including § 547(c)(8), which provides that the trustee may not avoid a transfer under § 547 "if, in a case filed by an individual debtor whose debts are primarily consumer debts, the aggregate value of all property that constitutes or is affected by such transfer is less than $600." Here, the parties disagreed about whether the § 547(c)(8) defense applied. The circuit court could not overlook the fact that the state court returned the final two garnishments, totaling $296.20, to the husband before the debtors commenced their preference action; nor could the debtors, the court said. "Their avoidance petition sought the return of only $562.78, an amount corresponding to the first four garnishments, not the return of $858.98, the total amount garnished. We find that the terms of the avoidance petition make clear that the [debtors] sought to avoid only the first four garnishments. . . Because 'the aggregate value of all property that constitutes or is affected by [the first four garnishments] is less than $600,' the section 547(c)(8) defense applies," the Eighth Circuit held. Note: This material is excerpted from the April 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

37. In re Racing Services, Inc., 779 F.3d 498 (8th Cir. 2015) (Riley, C.J.).

AVOIDANCE ACTION AGAINST NORTH DAKOTA DETERMINES THE STATE MUST RETURN TO THE BANKRUPTCY ESTATE TAXES COLLECTED PREPETITION

This case involved an appeal by North Dakota, the North Dakota Racing Commission, and three special funds administered by the commission (collectively, the "state") from a district court decision reversing the bankruptcy court's grant of summary judgment to the state against PW Enterprises, Inc. ("PWE"). The debtor, Racing Services, Inc. ("RSI"), was a state-licensed horse racing simulcast service provider that assumed responsibility for paying taxes to the state and PWE was the largest non-governmental creditor of the debtor. PWE obtained derivative standing to bring this adversary proceeding.

In 1987, the North Dakota legislature authorized parimutuel betting for live horse races in North Dakota. In addition to legalizing this form of betting, the statutory scheme included what the state called a "Takeout Statute," which allowed the state to deduct taxes from the wager pool. In 2001, the state authorized "account wagering," another form of pari-mutuel wagering "in which an individual deposits money in an account and uses the account balance to pay for parimutuel wagers." However, when the state added the authorization for account wagering, it did not amend the Takeout Statute to allow for the deduction of taxes in the case of account wagering.

In the year before RSI filed for bankruptcy, the state of North Dakota collected $5,270,101.20 in taxes from RSI for bets made under the account wagering statute. RSI filed a voluntary chapter 11 reorganization petition and later converted to chapter 7. PWE submitted proof of claim for $2,248,100.86 and the state filed a proof of claim for $6,422,243.58.

In PWE's complaint, it requested that the bankruptcy court: (1) disallow the state's claim against the bankruptcy estate for unpaid taxes, (2) deny priority to the state's claim, (3) avoid and recover allegedly preferential and fraudulent transfers (taxes paid) to the state, and (4) equitably subordinate the state's claim. On cross motions for summary judgment, the bankruptcy court granted the state's motion with respect to the first count, but denied summary judgment as to the remaining counts. PWE appealed this decision to the federal district court, which reversed and remanded, finding "'no legislative authority to collect taxes on account wagering during the time period in question.'" The state appealed that order which also required the state to return to the bankruptcy estate those taxes.

Thus, the only issue in this appeal was "whether North Dakota law <u>impliedly</u> authorized the state to collect taxes from RSI for account wagering during the period preceding RSI's bankruptcy, even though . . . 'there was no direct legislative authority to collect a tax on account wagering . . . .'" The state acknowledged the absence of affirmative legislative action to tax account wagering.

In affirming the district court, the Eighth Circuit Court of Appeals first cited the North Dakota Constitution which provides, "No tax shall be levied except in pursuance of law, and every law imposing a tax shall state distinctly the object of the same, to which only it shall be applied." The court noted that "'[t]axation of property is a legislative function, not a judicial function, and

courts may not substitute their judgment for that of the legislature.'" The court also stated, "'if the language is clear and unambiguous, the legislative intent is presumed clear from the face of the statute.'"

Even though the language was admitted by the state to be clear and unambiguous, the appellate court addressed the state's argument that the legislative history be examined to help determine the issue. However, the court further stated that even if considering the legislative history was proper, the state's evidence did not support the finding of an implied tax under North Dakota law. The state's argument that it would be absurd to authorize wagering without a corresponding bet payoff formula, and therefore a tax was created by implication, "asks too much." The court would not infer an alternative legislative intent where the statute was clear. Finally, the court rejected the state's argument that the district court's construction created constitutional infirmities.

38. In re Genmar Holdings, Inc., 776 F.3d 961 (8th Cir. 2014) (Loken, J.).

CONTEMPORANEITY UNDER § 547(c)(1) IS A FLEXIBLE CONCEPT WHICH REQUIRES A CASE-BY-CASE INQUIRY INTO ALL RELEVANT CIRCUMSTANCES

The Eighth Circuit began its discussion by noting that avoidance of preferential transfers under § 547 "is intended to discourage creditors from racing to dismember a debtor sliding into bankruptcy and to promote equality of distribution to creditors in bankruptcy," and adding that contemporaneous exchanges for new value are excepted from avoidance because they "encourage creditors to continue doing business with troubled debtors who may then be able to avoid bankruptcy altogether," and "because other creditors are not adversely affected if the debtor's estate receives new value." Further, the court observed that to qualify for the exception under § 547(c)(1), the creditor transferee must prove that an otherwise preferential transfer was "(A) intended by the debtor and the creditor . . . to be a contemporaneous exchange for new case, the transferee claimed that the § 547(c)(1) exception applied to the $65,000 settlement payment because he provided new value to debtor by conveying the boat in a contemporaneous exchange. The Eighth Circuit explained that "[t]he critical inquiry in determining whether there has been a contemporaneous exchange for new value is whether the parties intended such an exchange." The court also noted that the transferee bore the burden of proving this fact under § 547(g). The BAP affirmed the bankruptcy court's conclusion that the transferee in this case presented no evidence permitting a reasonable fact finder to find that the parties to the settlement agreement intended a contemporaneous exchange for new value and the Eighth Circuit agreed.
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39. Strauss v. Cole, 608 F. App’x 438 (8th Cir. 2015) (per curiam).

BANKRUPTCY COURT AUTHORITY AFTER *STERN* AND *ARKISON*; PROVING ACTUAL AND CONSTRUCTIVE FRAUD UNDER § 548; STAYING CIVIL PROCEEDINGS; AND MORE

The district court adopted the bankruptcy court’s findings and conclusions and independently granted a chapter 7 trustee’s motion for summary judgment on claims for avoidance of fraudulent and preferential transfers, and the court of appeals, in the above cited decision, summarily affirmed the district court, simply concluding that there was no basis for reversal.

The district court’s de novo review of the bankruptcy court’s findings of fact and conclusions of law reflects a garden-variety case of fraudulent and preferential transfer claims brought by a chapter 7 trustee against the principal/CEO of the debtor and his wife. The debtor was a corporate entity formed for the purpose of constructing and operating a manufacturing facility. The project was partly funded by bonds. The debtor never had enough money to complete the project and was never operational. Before its ultimate collapse, the CEO of the debtor accessed bond funds to pay nonexistent entities not really involved in the project and paid the funds to a personal judgment creditor and to his wife’s account for their personal expenses.

As part of the analysis, the district court noted that because a corporation can only act through its officers that, for purposes of the intent element of actual fraudulent transfer, the intent of the CEO of the debtor was attributable to the debtor. The court explained the burden shifting in an actual fraudulent transfer case. When the undisputed facts establish a confluence of badges of fraud, there is presumption of fraudulent intent, shifting the burden to the transferee to prove a legitimate purpose for the transfers, but the shifted burden does not simply require the transferee to “explain away the natural inferences;” it requires the transferee to prove “that he has not committed the objectionable acts with which he has been charged.”

The court also addressed a number of other issues including waiver of affirmative defenses; the test to be applied in deciding when to use the court’s discretion to stay civil proceedings; the standard for granting a motion under Rule 56(f) to extend time to respond to a motion for summary judgment to allow additional discovery; exclusion of evidence in the summary judgment context pursuant to Rule 56(c)(2), as hearsay, and for lack of probative value; and waiver of arguments based on failure to brief or raise issues on appeal.

40. Finn v. Alliance Bank, 860 N.W.2d 638 (Minn. 2015) (Stras, J.).

PONZI SCHEME PRESUMPTION DOES NOT APPLY TO MUFTA CLAIMS; STATUTE OF LIMITATIONS FOR "RELIEF ON THE GROUND OF FRAUD" APPLIES TO MUFTA CLAIMS BASED ON ACTUAL FRAUD

The Supreme Court of Minnesota held that the Ponzi scheme presumption, a concept already adopted in many federal courts, does not apply to MUFTA claims, and that the statute of limitations "for relief on the ground of fraud" applied to MUFTA claims based on actual fraud.

A loan finance company had sold participation interests in financed loans to financial institutions. Over time, the company's operations evolved into a Ponzi scheme when it oversold participation interests in excess of the actual underlying loans and paid out early investors with funds from late investors. Two banks sued the company, and a receiver was appointed. In an effort to "claw back" payments from the company to investors, the receiver sued various financial institutions under Minnesota's Uniform Fraudulent Transfer Act ("MUFTA"), Minn. Stat. §§ 513.41–.51 (2014), to recover certain payments made with actual fraud and constructive fraud.

The suit made its way to the Supreme Court of Minnesota. Two issues of first impression under MUFTA were presented: (1) whether the Ponzi-scheme presumption applied to MUFTA claims and (2) which statute of limitations applied to MUFTA claims—the one "for relief on the ground of fraud" under Minn. Stat. § 541.05, subd. 1(6) (2014); or the one for claims based "upon a liability created by statute" under Minn. Stat. § 541.05, subd. 1(2) (2014).

The Court held that the Ponzi-scheme presumption does not apply to MUFTA claims. It noted that the Ponzi-scheme presumption contains three components, which are presumed: (1) "the debtor had fraudulent intent;" (2) "the debtor was 'insolvent' at the time of a disputed transfer, regardless of the transfer's timing and the actual operations of the debtor;" and (3) "any transfer from a Ponzi scheme was not for reasonably equivalent value." The Court examined each component to determine whether each component had support under the statute.

In examining whether MUFTA supported the presumption that the debtor had fraudulent intent, the Court observed that MUFTA enumerated non-exhaustive factors known as "badges of fraud," which individually are not conclusive, that the Court may consider to infer actual intent. This enumeration, therefore, precluded a determination that the unlisted Ponzi-scheme presumption is conclusive of this intent. Finding no statutory justification in MUFTA for a court to infer fraudulent intent simply upon the existence of a Ponzi scheme, the Court concluded that fraudulent intent must be determined on a case-by-case basis.

Regarding the second presumption that the debtor was insolvent at the time of a disputed transfer, the Court noted that MUFTA already included a provision for the presumption of insolvency under certain circumstances, but that presumption did not hinge upon the presence of a Ponzi scheme. The Court declined to extend MUFTA's statutory presumption of insolvency to include a presumption of insolvency based upon the existence of a Ponzi scheme. The Court

also noted that even if it were assumed that a debtor operating a Ponzi scheme becomes insolvent, this assumption did not prove that the debtor was insolvent at the time of the transfer.

The Court also found no support in MUFTA for the third component of a Ponzi-scheme presumption—that a transfer from a Ponzi scheme was not for reasonably equivalent value. The Court acknowledged that for actual-fraud claims, MUFTA provides an affirmative, good-faith defense that the transferee "took in good faith and for a reasonably equivalent value." The Court reasoned that adopting the presumption that a transfer was not for reasonably equivalent value would negate that good-faith defense. In addition, the Court was unpersuaded by other arguments and principles advanced in support of this presumption.

Finally, the Court held that as to actual-fraud claims, the applicable statute of limitations was "for relief on the ground of fraud" under Minn. Stat. § 541.05, subd. 1(6) (2014), which accrues only upon discovery of facts serving as the basis of the fraud. The Court explained that just because fraudulent-transfer liability, which had long existed at common law, was later enacted by statute and codified, that codification does not re-characterize the claim into one created by statute. Instead, the Court relied upon common law precedent, which long maintained that a fraudulent-transfer claim based upon actual intent is subject to the statute of limitations for "relief on the ground of fraud." Because the constructive-fraud claim was already dismissed for pleading deficiencies, the Court declined to decide which statute of limitations applied to constructive fraud claims.

41. In re Keeley and Grabanski Land Partnership, 531 B.R. 771 (B.A.P. 8th Cir. 2015) (Federman, J.).

RECOVERY UNDER § 550 IS A REMEDY OF EQUITY AND RESTORATION, THE PURPOSE OF WHICH IS TO RESTORE THE ESTATE TO THE CONDITION IT WOULD HAVE ENJOYED BUT FOR THE TRANSFER, AND ALLOWING THE ESTATE TO PROFIT FROM AN INCREASE IN VALUE ATTRIBUTABLE TO IMPROVEMENTS OF THE GOOD FAITH TRANSFEREE DOES NOT PROMOTE RESTORING EQUITY; RULE 59 REVIEWED

The debtor was lessor on a lease of farm land. The bankruptcy trustee successfully avoided the lease as a fraudulent transfer because the rent under the lease was below fair market value. On appeal, the issue was the bankruptcy court's calculation of recovery under § 550. The BAP held that "[t]he remedy for avoidance of a lease does not fit so comfortably in § 550" because it was not possible to order the return of a portion of a leasehold interest that had been consumed, in this case a portion of a year and a half by the time of avoidance. Instead, the trustee is allowed to recover the market value of the lease (in contrast to the lower contract rate) for the period of consumed time, because the property itself is not recoverable. And, because the lease only had value until it was terminated by the avoidance, possession of and rights in the property reverted to the trustee not as a § 550 remedy but simply because the lease was no longer in effect.

With respect to the lessee's right to offset under § 550(e), the BAP explained that the purposes of setoff are equity and restoration, and also specifically to prevent a windfall to the estate or creditors, and held that the lessee was entitled to setoff for the lesser of the cost of improvements

or the increase in value as a result of the improvements. But, if there is no value to the improvement, such as a crop developed on the land during the lease, then that zero value is the lesser value, and there can be no setoff of the costs of the improvement. Payment of property taxes, however, is a defined improvement under § 550 and therefore the cost and the value are equivalent and subject to setoff. Crops are not a defined improvement, but the parties agreed, without citing authority, that the lessee, as a good faith transferee, would at least be entitled to the value of the crop, but not the costs associated with it. In any event, the BAP concluded that under applicable state law the lessee had the right to plant the crop and was entitled to the proceeds of that crop regardless of whether he was a good faith transferee under § 550(e).

The court also conducted an analysis of Fed. R. Civ. P. 59 to determine whether the bankruptcy court erred in denying the trustee's request for a new trial based upon newly discovered evidence that the lease in this case was actually executed postpetition and therefore void. The BAP set forth the elements necessary to prevail on a Rule 59(e) motion: "(1) the evidence was discovered after trial; (2) the movant exercised due diligence to discover the evidence before the end of the trial; (3) the evidence is material and not merely cumulative or impeaching; and (4) a new trial considering the evidence would probably produce a different result." The court noted that the analysis is the same under Rule 60(b)(2), and that the moving party "bears a heavy burden." The bankruptcy court found in favor of the trustee as to the first three elements, but as to the fourth concluded that the result would be the same even accounting for the newly discovered evidence. The BAP agreed, and explained that even if the lease was executed postpetition, it would not be void, but voidable as an unauthorized postpetition transfer, and that the result would not be different. Whether avoided pursuant to § 548 or § 549, the lease was in place when the crops were planted and the crop was planted under its authority, not by a squatter entitled to nothing.

42. Seaver v. Ashenfelter (In re MSP Aviation, LLC), 531 B.R. 795 (Bankr. D. Minn. 2015) (Ridgway, J.).

TRUSTEE'S EQUITABLE RECHARACTERIZATION CLAIM FAILS

The bankruptcy court for the District of Minnesota declined to recharacterize loans from the defendant to the debtor as equity contributions.

The debtor, a company that provided jet repair and services, filed for chapter 7 bankruptcy. The chapter 7 trustee filed an adversary proceeding against a founding member of the debtor for equitable relief under 11 U.S.C. § 105(a) and for declaratory relief under 28 U.S.C. § 2201(a), seeking to have certain loans made by the member to the company recharacterized as equity contributions, and seeking to recover payments made by the debtor to the member as unauthorized transfers under Minn. Stat. § 322B.54, subd. 1.

When determining whether the court should recharacterize the loans as equity contributions under the doctrine of equitable recharacterization, the court noted that the Eighth Circuit had not yet determined whether the bankruptcy court's equitable powers under § 105(a) included the power to recharacterize a loan as equity. The court declined to decide whether equitable recharacterization was an appropriate remedy. Nonetheless, the court found that even if equitable recharacterization was a viable option, after analyzing the case under the eleven-

factored test for equitable recharacterization from Roth Steel Tube Co. v. Commissioner of Internal Revenue, 800 F.2d 625, 630 (6th Cir. 1986), the facts of the case did not support equitable recharacterization. The court analyzed the following eleven factors:

> (1) the names given to the instruments, if any, evidencing the indebtedness;
> (2) the presence or absence of a fixed maturity date and schedule of payments;
> (3) the presence or absence of a fixed rate of interest and interest payments;
> (4) the source of repayments;
> (5) the adequacy or inadequacy of capitalization;
> (6) the identity of interest between the creditor and the stockholder;
> (7) the security, if any, for the advances;
> (8) the corporation's ability to obtain financing from outside lending institutions;
> (9) the extent to which the advances were subordinated to the claims of outside creditors;
> (10) the extent to which the advances were used to acquire capital assets; and
> (11) the presence or absence of a sinking fund to provide repayments.

After analysis, the court found that many of the factors weighed in favor of the defendant. The court found that the following facts did not support recharacterization: documents evidencing the transaction described the transaction as a loan; the note stated a fixed rate of interest, which went unpaid due to the subordination of the debt to only one other creditor; the loan was secured; the company was adequately capitalized; and the advances were not used to acquire capital assets. The court also declined to apply the doctrine of quasi-estoppel to the transactions because the trustee failed to show alleged benefits that the defendant received from the transaction. Because the equitable recharacterization claim did not survive, the court dismissed the claims for declaratory judgment and for recovery of an unauthorized transfer.

43. Kelley v. Opportunity Finance, LLC (In re Petters Co.), ADV 10-4301 (Bankr. D. Minn. June 11, 2015) (Kishel, J.).

MOTION TO DISMISS BASED ON 2012 MUFTA AMENDMENTS EXCLUDING TRANSFERS TO CHARITIES IS DENIED

As part of the ongoing litigation surrounding Petters Company, Inc.'s ("PCI") bankruptcy, a group of defendants consisting of the Northwestern Foundation, the Minneapolis Foundation, and the Sabes Family Foundation (the "charity-defendants") brought a motion to dismiss based on the 2012 amendments to Minn. Stat. § 513.41(12), under the Minnesota Uniform Fraudulent Transfer Act ("MUFTA"). These defendants had all received money from one or more of the debtors in the course of the Petters Ponzi scheme. The trustee was seeking to recover these payments through fraudulent transfer actions.

In 2012, a change was made to MUFTA's definitional provision, Minn. Stat. § 513.41(12). Prior to the 2012 amendment, the definition of "transfer" read solely: "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with an asset or an interest in an asset, and includes payment of money, release, lease, and creation of a lien or other encumbrance." The 2012 amendment added that a "[t]ransfer does not include a contribution of money or an asset made to a qualified charitable or religious organization or entity unless the

contribution was made within two years of commencement of an action under 513.41 to 513.51 against the qualified charitable or religious organization . . . ." In addition to this provision, the legislation provided that the amendment was "effective on the day following final enactment and applie[d] to a cause of action existing on, or arising on or after, that date." As a practical matter, this meant that the amendment applied to any litigation pending on Apr. 4, 2012, including this adversary proceeding.

Based on this new provision, the charity-defendants argued that the case for avoidance against them fails to the extent that the payments of money on which the trustee sued took place more than two years before the debtor's bankruptcy filing. In response, the trustee argued that transfers at issue were not "contributions" as defined by the 2012 amendment because the payments made to these charitable organizations were made "under color of a financial instrument to which the [charity-defendants] were entitled as payees to receive money from PCI." In the alternative, the trustee argued that the transfers to the charity-defendants were not contributions, but rather were returns on investment because the charity-defendants were assigned promissory notes from third parties that had originally invested in the debtor and its related entities.

Addressing the trustee's first arguments, the court noted that in the complaint, the trustee pleaded "that all three of the charity-defendants received payment from the [d]ebtors in the same transactional sequence: they had received and then held a specific form of intangible asset previously issued by the [d]ebtors, that later generated the payments that they received from the [d]ebtors." In other words, the trustee alleged that a "contribution" under the Minnesota statute, if any, was made when the charity-defendants received the right to payments from third-parties, but payments made by the debtors to the charity-defendants were made in order to "discharge their facial obligations under the notes." The court ruled that because the facts pleaded by the trustee are assumed to be true under Fed. R. Civ. P. 12(b)(6), the complaint was not dismissed.

As for the trustee's argument that the transfers were returns on investment, while the court weighed in on the trustee's pleading, the court decided that "this ultimate substantive issue is not before the court on this motion . . . it is best addressed on a developed record of specific historical fact, as to the charity-defendants' acquisition, holding, and intentional exploitation (if any) of the rights to payments under all of the notes before they were satisfied in full." Therefore, the defendants' motions to dismiss were denied.

44. Running v. Goodspeed, 535 B.R. 302 (Bankr. D. Minn. 2015) (Constantine, J.).

FRAUDULENT TRANSFER ACTION DISMISSED FOR LACK OF INSOLVENCY; NO RECOVERY WHEN NO BENEFIT TO THE ESTATE

Chapter 7 trustee sought to avoid debtor's pre-divorce alleged fraudulent transfer to his former wife. Before his divorce, debtor mortgaged two properties and the proceeds were used to purchase a third property titled solely in the name of his wife (the defendant). While the divorce was pending, the debtor filed for bankruptcy. The defendant asserted the proceeds represented her non-marital property, but the case turned on the trustee's failure to satisfy MUFTA's insolvency requirements.

The court discussed MUFTA's insolvency provisions at length, including the statutory definitions of words used within those provisions. The court also noted that 11 U.S.C. § 550(a) requires a trustee's recovery of an avoided transfer to benefit the estate. While this case was under advisement, the trustee filed a notice stating that the amount of money on hand for distribution to creditors exceeded the total amount of outstanding claims and expenses. Accordingly, the court discussed that the only party to benefit from avoiding the transfer would be, inappropriately, the debtor – since any proceeds from avoiding the transfer would be paid to the debtor. Moreover, a payment to the debtor could infringe on marital property issues more appropriately handled in the state court divorce case.

DISCHARGE & DISCHARGEABILITY

45. Venture Bank v. Lapides, __ F.3d. __, 2015 WL 5011704 (8th Cir. 2015) (Loken, J.).

POST-DISCHARGE CHANGE-IN-TERMS AGREEMENTS WERE NOT ENFORCEABLE § 524(c) REAFFIRMATION AGREEMENTS; INDEED, THEY VIOLATED THE DISCHARGE INJUNCTION

The Eighth Circuit explained that it "need not consider whether a promise not to foreclose on a mortgage is adequate consideration under [state] law if the Change in Terms Agreements were contrary to § 524(c). The Agreements served no purpose other than reaffirmation agreements in which [the debtor] agreed to repay all of his discharged personal debt. . . Instead of continuing to accept [the debtor's] voluntary payments, a post-discharge arrangement both parties were free to continue, [the] Bank insisted that [the debtor] again promise to repay the entire discharged personal debt in order to continue the refinancing negotiations. . . When a post-discharge agreement does nothing but obligate a debtor to repay a discharged debt, it is inconsistent with § 524(c), a statute declaring that agreements removing specific personal debts from the benefits of discharge must be negotiated and filed with the court before discharge, when a debtor has the protection of his bankruptcy attorney and the bankruptcy court. . . We simply conclude that the post-discharge Change in Terms Agreements are unenforceable because they were nothing more than reaffirmation agreements that did not comply with § 524(c)," the court held. Next, the court turned to the issue of whether the bank violated the discharge injunction, noting that as the bankruptcy court and the district court recognized, the bank did not necessarily violate the discharge injunction simply because it accepted monthly payments made pursuant to Change in Terms Agreements that were unenforceable. The court stated that while § 524(a)(2) provides that a discharge "operates as an injunction against. . . an act, to collect, recover or offset any [discharged] debt as a personal liability of the debtor," § 524(f) provides that a discharge does not "prevent[ ] a debtor from voluntarily repaying any debt." In this case, the bankruptcy court concluded that the bank had violated the discharge injunction because the "Bank's communications and post-petition conduct were designed to obtain payments and enforce the debt" and therefore the debtor's monthly payments under the post-discharge Change in Terms Agreements were involuntary. The Eighth Circuit agreed, explaining that "ample evidence of pressure and inducement supports the bankruptcy court's finding of involuntariness. The Bank encouraged [the debtor] to believe that, if he made regular payments, it would consider helping

him refinance his home. It then required him to sign agreements obligating him to repay the entire discharged debt, rather than continue to make monthly payments, and sent numerous emails reminding him that payments were "due" and seeking payment of additional principal and interest. . . [But the] Bank did not refinance the three mortgages on the [debtor's] home. It simply dangled the possibility of refinancing to induce [the debtor] to sign agreements promising to repay the entire discharged debt. The bankruptcy court did not clearly err in finding that [the debtor's] payments were not voluntary within the meaning of § 524(f)." Thus, the Eighth Circuit concluded that the district court did not err in affirming the bankruptcy court's decision that the bank violated the discharge injunction. Note: This material is excerpted from the October 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

46. In re Walker, 528 B.R. 418 (B.A.P. 8th Cir. 2015) (Schermer, J.).

NO DEBT ARISES FROM AN UNCONSCIONABLE AGREEMENT; NO § 523 OR §727 STANDING FOR A NON-CREDITOR; ELEMENTS OF JUDICIAL ESTOPPEL

The debtor, an entertainer, entered into a management agreement with Joseph R. Wilson. The agreement was for a 25-year term with an option to extend for four periods of two years. The contract provided compensation to Wilson of 50% of the debtor's revenues and, if Wilson died, the right of Wilson's benefactor to hire a replacement manager under the contract and obligating the debtor to continue to pay Wilson's benefactor and the replacement under the agreement. In addition, the contract provided that the debtor was solely responsible for his expenses and was only allowed to work at such times and places as were approved in writing by Wilson.

Wilson filed for bankruptcy in March 2008. The debtor fired Wilson in September 2008. In August 2009, the debtor's wife launched Precious Princess Productions to receive the debtor's revenues. In August 2012, the debtor's wife established a successor company, Unchained Productions LLC, to receive the debtor's income. In July 2012, the debtor declared bankruptcy.

Wilson filed an adversary proceeding in the debtor's bankruptcy case claiming § 523 nondischargeable debt arising from the management agreement and seeking denial of discharge under § 727. The bankruptcy court ruled in favor of the debtor and related defendants, finding no debt to Wilson because the management contract was void as unconscionable, and that therefore no action under § 523 or § 727 could be maintained by Wilson. The court denied Wilson's requests for amended findings, a new trial, and to amend judgment. Wilson appealed.

The BAP affirmed the bankruptcy court's determination of unconscionability based upon unreasonable term length, excessive manager compensation, the debtor's inability to terminate the contract, and the manager's power to choose his own replacement. The BAP rejected the argument that unconscionability was not properly raised at trial, concluding that it was tried with the implied consent of Wilson. The BAP rejected a statute of limitations argument because it was not raised until Wilson's post-judgment motion.

Wilson also argued that he was a creditor of the debtor based upon funds he had invested in the debtor. In affirming the bankruptcy court, the BAP stated that because Wilson failed to disclose in his own bankruptcy case any debt owed to him by the debtor, Wilson was judicially estopped from claiming that he was owed funds from any investment in the debtor prior to his bankruptcy case. Moreover, the BAP noted, the record did not support any investment by Wilson in the debtor or that the debtor owed any debt to Wilson. Finally, the BAP held that because Wilson was not a creditor of the debtor, he lacked standing to bring an action under § 727.

47. Nielsen v. ACS, Inc. (In re Nielsen), 518 B.R. 529 (B.A.P. 8th Cir. 2014) (Schermer, J.).

STUDENT LOAN DEBT HELD NON-DISCHARGEABLE

The BAP ruled that the bankruptcy court did not abuse its discretion in determining that under the Eighth Circuit's "totality-of-the-circumstances" analysis, the debtor failed to meet her burden of proving an undue hardship under § 523(a)(8) for purposes of obtaining a discharge of her student loans. The BAP declined to consider some of the issues presented on appeal by the debtor either because those issues were not presented at trial or were not germane.

To obtain a discharge of student loan debt under § 523(a)(8), the debtor must show that excepting the student loan debt from discharge constitutes an undue hardship. In the Eighth Circuit, to determine whether an undue hardship exists, the standard to be applied is a totality-of-the-circumstances analysis, which examines "(1) a debtor's past, present, and reasonably reliable future financial resources; (2) a calculation of the debtor's and [debtor's] dependent's reasonable necessary living expenses; and (3) any other relevant facts and circumstances surrounding each particular bankruptcy case."

In this case, the debtor argued that the bankruptcy court failed to consider the negative effects of mold exposure into the undue hardship analysis. Upon review, the BAP ruled that there was nothing in the record to contradict the bankruptcy court's detailed findings that there was insufficient evidence that the mold exposure constituted an undue hardship.

The debtor also argued that the bankruptcy court incorrectly assessed her income and expenses. The BAP stated that the court's assessment of the debtor's finances was supported by the record, and the BAP found no error with the bankruptcy court's assessment.

The BAP likewise found no error with the bankruptcy court's determinations the debtor's future income potential weighed against undue hardship, since the debtor had good employment prospects, her debtor's employment limitations were largely self-imposed, she was of young age, that she lacked substantial physical or mental impairments, and that she had a number of marketable degrees.

Lastly, the debtor argued that the bankruptcy court should not have considered her failure to participate in an available Income Contingent Repayment Plan ("ICRP"). The BAP held that the bankruptcy court properly analyzed the ICRP as but one factor in its undue hardship analysis because whether an ICRP exists as an alternative form of debt repayment is a separate issue

under the totality of the circumstances analysis in the Eighth circuit. Further, a debtor's potential adverse consequences of an ICRP were not determinative of that issue.

48. Huonder v. Champion Milking Systems, LLC, ADV 14-3089 (Bankr. D. Minn. July 10, 2015) (Kishel, J.).

DEBTORS' ACTION FOR POST-DISCHARGE INJUNCTION VIOLATIONS SURVIVES SUMMARY JUDGMENT, DESPITE NO SUPPORT FOR CAUSAL LINK BETWEEN VIOLATIONS AND EMOTIONAL DAMAGES

A prepetition creditor, Champion Milking Systems (CMS) sent debtor post-discharge invoices and began a conciliation court action to collect a prepetition debt. CMS withdrew the conciliation court action before the first hearing. CMS's CEO then appeared at the Huonders' (the debtors') home. The parties dispute what happened during the visit. CMS claimed its CEO personally apologized. The Huonders claimed the CEO berated John Huonder and pressured him to pay the prepetition debt. After the visit CMS' CEO sent a letter to the Huonders, which stated CMS sent the post-discharge invoices by mistake. The Debtors filed an action for post-discharge injunction violations against CMS, alleging the violations caused emotional damages. The parties then conducted discovery, culminating in CMS' motion for summary judgment.

The bankruptcy judge denied summary judgment, holding the Huonders had put just enough evidentiary material in the record for their case to survive. However, the court pointed out the debtors had yet to introduce any facts which could prove a causal link between the alleged post-discharge injunctions and debtors' damages: "the bottom line . . . CMS does not have a knockout on this lawsuit, as a matter of law, notwithstanding the Debtors' failure to produce a formal medical diagnosis to corroborate their own belief that CMS's acts caused the numerous physical symptoms of which John Huonder complains." The court noted Eighth Circuit case law dictated a debtor may recover attorney fees when: "the fees were incurred in obtaining relief against a creditor in enforcement of the debtor's legally-cognizable protections and prerogatives within the bankruptcy process, even where the debtor does not prove up actual, pecuniary damages resulting from a creditor's adjudged violation."

PLANS, DISMISSAL, & CONVERSION

49. Harris v. Viegelahn, 135 S. Ct. 1829 (2015) (Ginsburg, J.).

A DEBTOR WHO CONVERTS TO CHAPTER 7 IN GOOD FAITH IS ENTITLED TO RETURN OF ANY POSTPETITION WAGES NOT YET DISTRIBUTED BY THE CHAPTER 13 TRUSTEE

The Court also observed that many Chapter 13 debtors do not successfully complete a Chapter 13 plan; Congress accorded Chapter 13 debtors a nonwaivable right to convert to Chapter 7 "at any time" under 11 U.S.C.A. § 1307(a). To accomplish such a conversion, the debtor need only file a notice with the bankruptcy court; no court order is needed. Additionally, the Court noted that conversion from Chapter 13 to Chapter 7 does not commence a new bankruptcy case. Instead, the case continues, albeit under a different path, but without "effect[ing] a change in the

date of the filing of the petition" under 11 U.S.C.A. § 348(a). But conversion does immediately "terminate[] the service" of the Chapter 13 trustee, who is replaced with a Chapter 7 trustee under § 348(e).

Next, the Court turned to § 348(f), which Congress added to the Bankruptcy Code in 1994. Section 348(f)(1)(A) provides that in a case converted from Chapter 13, the debtor's postpetition earnings and acquisitions do not become part of the new Chapter 7 estate: "[P]roperty of the [Chapter 7] estate in the converted case shall consist of property of the estate, as of the date of filing of the [initial Chapter 13] petition, that remains in the possession of or is under the control of the debtor on the date of conversion." And the Court mentioned § 348(f)(2), which provides an exception for debtors who convert in bad faith: "If the debtor converts a case [initially filed] under chapter 13 . . . in bad faith, the property of the estate in the converted case shall consist of the property of the estate as of the date of the conversion." At this point the Court said that § 348(f) "makes one thing clear: A debtor's postpetition wages, including undisbursed funds in the hands of a trustee, ordinarily do not become part of the Chapter 7 estate created by conversion. Absent a bad-faith conversion, § 348(f) limits a converted Chapter 7 estate to property belonging to the debtor 'as of the date' the original Chapter 13 petition was filed. Postpetition wages, by definition, do not fit that bill."

The Court reasoned that by "excluding postpetition wages from the converted Chapter 7 estate, § 348(f)(1)(A) removes those earnings from the pool of assets that may be liquidated and distributed to creditors. Allowing a terminated Chapter 13 trustee to disburse the very same earnings to the very same creditors is incompatible with that statutory design." In this regard, the Court found § 348(f)(2)'s exception for bad-faith conversions instructive, since § 348(f)(2) provides that in the bad-faith conversion scenario, the converted Chapter 7 estate "consist[s] of the property of the [Chapter 13] estate as of the date of conversion."

The Court stated that § 348(e) was also informative: "Conversion [from Chapter 13 to Chapter 7] terminates the service of [the Chapter 13] trustee." But since a core service provided by a Chapter 13 trustee is the disbursement of "payments to creditors" under 11 U.S.C.A. § 1326(c) , "[t]he moment a case is converted from Chapter 13 to Chapter 7 . . . , the Chapter 13 trustee is stripped of authority to provide that 'service,'" the Court said, adding that "[r]eturning funds to a debtor, however, is not a Chapter 13 trustee service as is making 'paymen[t] to creditors.' "
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50. In re Bowman, 526 B.R. 802 (B.A.P. 8th Cir. 2015) (Nail, J.).

A DISMISSED CASE CANNOT BE REOPENED UNDER § 350(b)

Debtors filed a petition for relief under Chapter 11 on November 5, 1999. The debtors proposed several plans of reorganization, but failed to confirm a plan. The bankruptcy court dismissed the debtors' case on September 28, 2004, on a motion made by the U.S. Trustee (UST). The debtors did not appeal the dismissal order, and the case was closed on May 5, 2005. More than nine years later, on September 15, 2014, the debtors filed a motion to reopen their case "to pursue Confirmation of their current Plan[.]" The UST and a creditor objected, and on September 24, 2014, without holding a hearing, the bankruptcy court entered a text order denying the debtors' motion. The BAP noted that 11 U.S.C.A. § 350 provides: "(a) After an estate is fully administered and the court has discharged the trustee, the court shall close the case. (b) A case may be reopened in the court in which such case was closed to administer assets, to accord relief to the debtor, or for other cause." In this case, the bankruptcy court held that "section 350 should not be used to reopen a case that was dismissed for cause before it was fully administered." The BAP agreed, stating that "a dismissed case cannot be reopened under § 350(b)[.]" For that reason alone, the BAP said it could not say that the bankruptcy court's denial of the debtors' motion to reopen their dismissed case was an abuse of discretion. The BAP added in a footnote that: "Several other factors also support the bankruptcy court's decision, including the nearly ten-year gap between the dismissal of Debtors' case and the filing of their motion to reopen, Debtors' failure to demonstrate reopening their case would not be futile, and Debtors' failure to offer a legitimate reason why they could not file a new bankruptcy case." Note: This material is excerpted from the May 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

51. In re Sowell, 535 B.R. 824 (Bankr. D. Minn. 2015) (Ridgway, J.).

DEBTOR WHO CONVERTS FROM A CHAPTER 13 TO 7 AND LACKS A CONFIRMED PLAN IS NOT ENTITLED TO THE RETURN OF THE AMOUNT LEFT IN CHAPTER 13 TRUSTEE'S HANDS; ORDER EXPRESSLY DIRECTING THE REMAINING FUNDS IN CHAPTER 13 TRUSTEE'S HAND BE PAID TO ATTORNEY WOULD BE INAPPROPRIATE

The debtor voluntarily converted his chapter 13 case to one under chapter 7. No plan had been confirmed. After the chapter 13 trustee's "Final Report and Account" indicated that $1,855.03 was "on hand," the debtor's attorney sought approval of his fees and court authorization for the trustee to disburse the amount on hand. The trustee asked the court to hold a hearing on the fee application to consider the issues raised in *Harris v. Viegelahn*, a Supreme Court case involving a confirmed chapter 13 plan that held,"[A] debtor who converts to Chapter 7 is entitled to return of any postpetition wages not yet distributed by the Chapter 13 trustee."

The bankruptcy court reasoned that the rationale of *Harris* applies in a case that lacked a confirmed plan.

First, the bankruptcy court addressed the debtor's argument that the trustee did not have standing to challenge the fee request. The court relied upon § 1302(b)(1), which incorporates § 704(a)(2) & (7), as the basis for a chapter 13 trustee to appear and be heard on this matter. Next, the court determined that a chapter 7 trustee's "no distribution" report failed to moot a question concerning the return of undistributed funds by a chapter 13 trustee.

Finally, the court held that *Harris* controlled, and that an order directing that funds remaining in the hands of the chapter 13 trustee upon conversion be paid to satisfy attorney's fees would be inappropriate.

52. In re Stewart, 536 B.R. 273 (Bankr. D. Minn. 2015) (Ridgway, J.).

"SURRENDERS" AND "VESTING" IN § 1325(a)(5)(C) & § 1322(b)(9), RESPECTIVELY, MAY WORK IN TANDEM WHEN PROVIDING FOR THE TREATMENT OF A SECURED CLAIM IN A CHAPTER 13 PLAN

The chapter 13 debtor sought court authorization allowing the transfer of encumbered real property to the secured creditor in full satisfaction of its claim. The debtor owned real property in Maryland that was subject to a mortgage, a lien for real estate taxes, and a lien for homeowner's association assessments. The debtor's confirmed plan stated plan confirmation vests the property in the mortgagee and the confirmation order constitutes a deed of conveyance of the property and, when recorded at the registry of deeds, the secured claims will be paid by the surrender of the collateral real property.

The bankruptcy court interpreted the interaction between "surrenders" in 11 U.S.C. § 1325(a)(5)(C) and "vesting" in 11 U.S.C. § 1322(b)(9), concluding, with the support of case law, that "surrenders" and "vesting" in §§ 1325(a)(5)(C) & 1322(b)(9), respectively, may work in tandem when providing for the treatment of a secured claim in a chapter 13 plan. The court also relied upon § 1327(a) and the holding in *Bullard v. Blue Hills Bank*, 575 U.S. ___, 135 S. Ct. 1686 (May 4, 2015), that the provisions of a confirmed plan bind all the parties in interest.

PROPERTY OF THE ESTATE

53. In re Lien, 527 B.R. 1 (Bankr. D. Minn. 2015) (Ridgway, J.).

DEBTORS CONVERTED FROM CHAPTER 13 TO 7 IN BAD FAITH TO AVOID POSTPETITION INHERITANCE FROM COMING INTO THE ESTATE, AND PROPERTY OF THE ESTATE IS THEREFORE DETERMINED AS OF THE TIME OF CONVERSION

Applying the totality of the circumstances analysis, the bankruptcy court determined that the debtors acted in bad faith in converting to chapter 7 in order to shield a substantial post-confirmation inheritance from creditors. The court found that the debtors could have continued making plan payments without hardship; that the debtors' claim that they did not realize that the inheritance would have any effect on their obligations under the plan was unconvincing; and that the debtors also omitted several other assets acquired pre-conversion. Under the totality

analysis, the debtors' conduct indicated manipulation of the Code in an effort to obtain a windfall at the expense of creditors. Moreover, the court found that pursuant to § 348(f)(2), the property of the estate in the case converted in bad faith consists of property of the estate at the time of the bad faith conversion. Accordingly, the court ordered non-exempt property as of the date of conversion to be turned over to the chapter 7 trustee.

54. In re Hennessy, 526 B.R. 806 (Bankr. D. Minn. 2015) (Ridgway, J.).

INHERITED "529" COLLEGE TUITION SAVINGS ACCOUNTS MAY BE EXCLUDED FROM PROPERTY OF THE CHAPTER 7 ESTATE SUBJECT TO 11 U.S.C. § 541(b)(6)

On a chapter 7 trustee's motion for turnover of estate property, the bankruptcy court concluded that an inherited 529 plan is distinguishable from an inherited IRA because the heir to the 529 possesses only the same rights as the 529 settlor. Therefore, subject to satisfying the other requirements of § 541(b)(6) (qualified plan, proper beneficiaries, timing and size of contributions), an inherited 529 plan is excluded from property of the estate. An inherited IRA presents the debtor heir with "an opportunity for consumption," whereas an inherited 529 plan continues to serve its original purpose whether owned by the settlor or the heir.

SANCTIONS

55. In re Young, 789 F.3d 872 (8th Cir. 2015) (Melloy, J.).

BANKRUPTCY COURT'S IMPOSITION OF RULE 9011 SANCTIONS AGAINST CHAPTER 13 DEBTOR'S ATTORNEY, INCLUDING FINES AND SUSPENSION, FOR MISREPRESENTATIONS AND CERTIFICATIONS MADE REGARDING DOMESTIC SUPPORT OBLIGATIONS FOR PURPOSES OF OBTAINING CONFIRMATION, UPHELD AS WITHIN THE COURT'S SANCTION POWER AND AS APPROPRIATE IN SEVERITY

In this case, counsel for a chapter 13 debtor intentionally mischaracterized the debtor's past due postpetition domestic support obligations as past due prepetition obligations in order to avoid dismissal, and falsely certified that the debtor was current on the obligations, and misleadingly represented that the debtor would "continue" to remain current on the obligations, in order to trick the chapter 13 trustee into withdrawing his objection to confirmation. The ruse succeeded and the debtor's plan was confirmed. The bankruptcy court discovered the false and inaccurate statements, entered a show cause order, and ultimately entered sanctions, including barring the attorney from practicing in Arkansas bankruptcy courts for six months and a fine of $1,000. The court also imposed a concurrent suspension and separate $1,000 fine for misrepresentations during the show cause hearing, but the BAP reversed those additional sanctions because the attorney was not provided notice and an opportunity to defend against those sanctions.

On appeal the BAP otherwise affirmed the sanctions, and the Eighth Circuit also affirmed. The court noted the preferential provisions and significant consequences in the Code regarding domestic support obligations, especially in chapter 13 cases. In reviewing the award of

sanctions, the court examined the facts and agreed that the attorney's misconduct was "calculated and disingenuous" such as to justify the sanctions imposed. The court agreed that the attorney had "no basis in law or in fact for her assertions" and "obtained an impermissible benefit" for the debtor as a result of her manipulation of "the Code, the court, and the bankruptcy system."

The court opined that "Rule 9011 is critical for the bankruptcy system to function because," due to high volume caseloads and time limitations, "the bankruptcy judge must rely on counsel to act in good faith." The court rejected the "pure-heart-and-empty-head defense," in favor of the Rule 9011 requirement that attorneys must conduct reasonable inquiries into facts and law to support representations made to the court because the "potential for mischief to be caused by an attorney who is willing to skirt ethical obligations and procedural rules is enormous." The court concluded that the sanction in this case was appropriate because it was commensurate with the severity of the attorney's deception and limited to what was sufficient to "deter repetition of comparable conduct." Notably, the court found that the bankruptcy court was authorized to impose the sanction of suspension from practice of law not only because a local rule so provided, but also pursuant to Rule 9011(c)(2).

56. In re Clink, 770 F.3d 719 (8th Cir. 2014) (Kelly, J.).

A CHAPTER 7 DEBTOR'S ATTORNEY VIOLATED § 526(a)(2) BY ADVISING THE DEBTOR TO OMIT FROM HER BANKRUPTCY PETITION A $3,000 CHECK THAT THE DEBTOR HAD WRITTEN TO HER MOTHER AS PART OF A $5,000 REPAYMENT ON A LOAN AND THE ATTORNEY VIOLATED § 707(b)(4)(C) & (D) BY FAILING TO DISCLOSE HORSES THAT THE DEBTOR OWNED AND BY FILING AMENDED SCHEDULES THAT DIFFERED SIGNIFICANTLY FROM THOSE SIGNED BY THE DEBTOR

The bankruptcy court credited the debtor's testimony and determined that her attorney violated § 707(b)(4) by failing to list the horses she owned on Schedule B. The bankruptcy court found that either the attorney knew of the horses and advised debtor not to list them, or he unreasonably failed to ask the debtor about any animal ownership. Based on the testimony at the hearing, the Eighth Circuit could not conclude that the bankruptcy court's factual findings were clearly erroneous, and noted that it could affirm the sanctions under § 707(b)(4) on that basis alone. But the bankruptcy court also concluded that the attorney violated § 707(b)(4)(C) by attaching to the bankruptcy petition schedules that differed significantly from the schedules that the debtor had signed. The attorney "admitted that he made some of the changes [the debtor] had suggested on the draft petition, but he did not have her review and sign the petition filed with the bankruptcy court. Nor did he have her sign an amended petition he later filed that included different schedules listing new creditors and assets. So even if [the attorney] did not know that [the debtor] still owned horses . . . , he admitted that he filed various documents without [the debtor's] signature in violation of § 707(b)(4). Again, we see no clear error in the bankruptcy judge's findings, and we affirm the sanctions against [the attorney] under § 707(b)(4) on this basis, as well," the Eighth Circuit ruled. Note: This material is excerpted from the December 2014 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2014 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

57. Needler v. Casamatta (In re Miller Automotive Group Inc.), __ B.R. __, 2015 WL 4746246 (B.A.P. 8th Cir. 2015) (Saladino, J.).

BAP AFFIRMS SANCTIONS AGAINST ATTORNEY, INCLUDING DISGORGEMENT AND INDEFINITE SUSPENSION FROM PRACTICE, FOR NUMEROUS CODE, RULES AND PROFESSIONALISM VIOLATIONS, AND BECAUSE AN ATTORNEY WHO SHOULD HAVE KNOWN, BEFORE FILING THE PETITION, THAT REORGANIZATION WAS FUTILE, HAS RENDERED NO SERVICE TO THE ESTATE AND SHOULD THEREFORE NOT BE COMPENSATED FOR SUCH SERVICE; ALSO, NOTHING IN § 350 OR RULE 5010 REQUIRES NOTICE AND A HEARING PRIOR TO REOPENING A CASE

Counsel for the chapter 11 debtor in this case was not admitted to practice in the district but his employment was approved pro hac vice over the objection of the UST. During the pendency of the case, the attorney never sought or obtained approval of fees or expenses. The case fell apart as a result of counsel's ineffective representation during which he violated a number of local rules and was demonstrably incompetent in general. The case was dismissed on the debtor's motion. The UST filed a motion to reopen the case having received from the debtor and the debtor's principals a complaint concerning counsel's misconduct and mishandling of the case. The bankruptcy court granted the motion without a hearing and the UST filed a motion for sanctions, including disgorgement and indefinite suspension from practice in the district. Pursuant to order, counsel filed a final fee application.

The bankruptcy court held an evidentiary hearing and thereafter denied counsel's fee application and granted the UST's motion for disgorgement and sanctions. The attorney's motion for reconsideration was denied. Affirming the bankruptcy court, the BAP found that the attorney was provided with the requisite notice and opportunity and noted that counsel filed objections, at least two preliminary hearings were held, and he participated in the evidentiary hearing and was invited to submit a post-trial brief. In the analysis under Rule 9011(c)(1)(B) and 11 U.S.C. § 105(a), the BAP determined that the evidence overwhelmingly supported the bankruptcy court's conclusion that the attorney not only failed to provide value to the debtor's estate, but that his services were not reasonably likely to do so and his only success was stringing along a case that should never have been filed.

In support of the indefinite suspension from practice and revocation of electronic filing privileges, the BAP found that the evidence overwhelmingly supported the bankruptcy court's findings and sanctions. "The record in the case was replete with examples of [counsel's] violations of not only the Bankruptcy Code, Bankruptcy Rules, and Local Rules, but basic tenets of legal representation as well," including failure to inform the client about pleadings and the status and progress of the case, failing to disclose to the client a pre-existing business relationship with the broker sought to be employed, failure to obtain client authorization before taking action in the case, failure to perform reasonable investigation into the facts contained in the petition and case filings, failure to enter into a written fee agreement with the client and misleading the client's principals about expected total fees, and concealing the source of retainer.

The attorney's interactions with the debtor's representatives were "deplorable" and described as bullying. The BAP was also compelled by the bankruptcy court's finding that in at least eight unrelated published opinions in cases involving this attorney, "a pattern of professional misconduct, procedural noncompliance, and ethical violations" by the attorney was apparent. The BAP concluded that, because the attorney was a repeat offender in multiple jurisdictions, the indefinite nature of the suspension was a sanction reasonably suited to the violations.

Finally, the attorney argued that the bankruptcy court lacked jurisdiction because the motion to reopen was granted without notice and a hearing, and because the case, as a case dismissed prior to being fully administered, should not have been reopened. The BAP noted that nothing in 11 U.S.C. § 350 or its implementing Rule 5010 required notice and hearing; that the applicable local rule in the Western District of Missouri, which requires notice and a hearing, applies only to debtor motions to reopen; and that the Eighth Circuit's decisions in *Bowman* and *Finch* do not stand for the proposition that a case dismissed for cause prior to being fully administered cannot ever be reopened under § 350(b), but that § 350 clearly provides statutory authority to reopen a closed case when the purpose of reopening is to resurrect a closed file so that some type of request for relief can be received and acted upon and not as an opportunity to create and enforce rights that did not exist at the time the case was originally closed (such as to set aside a dismissal).

58. In re Living Hope Southwest Medical Services, LLC, 525 B.R. 95 (B.A.P. 8th Cir. 2015) (Federman, J.).

A PARTIAL CORRECTION OF AN OFFENSIVE PLEADING DOES NOT TRIGGER A NEW SAFE HARBOR PERIOD; SANCTIONS THAT DETER ARE NECESSARY TO REMIND THOSE WHO NEED REMINDING THAT A COURT IS NOT A PLACE TO VENT UNSUPPORTED FRUSTRATION

Stephens was the owner of two entities, each one the debtor in two different bankruptcy cases. In an adversary proceeding brought by the trustee of one debtor against the other and Stephens, the parties stipulated to dismissal of Stephens as a defendant from the adversary. The adversary concluded with allowance of a claim against the other defendant-debtor entity. Notwithstanding Stephens' dismissal from the case, he appealed that and related orders. While his appeal was pending, Stephens filed a motion for relief from judgment under Rule 60(b) and (d) in the bankruptcy court. The trustee filed a Rule 9011 motion claiming that the Rule 60 motion's allegations of fraud on the court, including attorney misconduct and collusion (between counsel for the trustee and the other defendant-debtor entity), were flagrantly false and malicious. The bankruptcy court denied the Rule 60 motion for lack of standing (because Stephens had been dismissed from the adversary proceeding as a defendant) and granted the Rule 9011 motion and awarded sanctions. Stephens filed a motion for reconsideration of the sanctions order and the court denied the motion.

On appeal of the order denying reconsideration of the order awarding sanctions, Stephens argued that the trustee had violated the Rule 9011(c)(1)(A) safe harbor provision by proceeding with the motion for sanctions after Stephens had corrected the original Rule 60 pleadings within the safe harbor time period. In fact, Stephens had filed only a corrected brief, and moreover he only

removed some but not all of the allegations of fraud on the court. The BAP, reviewing the bankruptcy court for abuse of discretion, concluded that "filing a corrected pleading which retains the substance of the allegedly-offensive material does not withdraw or appropriately correct a pleading under the Rule and does not trigger a new safe harbor period."

The BAP set forth a thorough analysis of the procedural requirements and substantive elements of Rule 60(b) and (d) and Rule 9011 motions, including the nature and serious significance of allegations of collusion, corruption and fraud on the court, and including a complete discussion of the purposes of sanctions and the proper means to calculate and award an appropriate sanction under Rule 9011(a)(1)(A), including that an award under this section is best characterized as a fee-shifting provision and that ability to pay is not relevant. The bankruptcy court held a two-day trial and determined that Stephen's allegations were unfounded assumptions and blatant illogical fallacies, and awarded monetary sanctions, notwithstanding Stephen's claim that he used harsh language only to match the requirements of the rule but not to suggest inappropriate behavior on behalf the attorneys involved. Applying an objective standard of reasonableness under the circumstances, the BAP affirmed the bankruptcy court, agreeing that Stephen's allegations were not plausible, not objectively reasonable, and not supported by the evidence.

FEE APPLICATIONS

59. Baker Botts L.L.P. v. ASARCO LLC, 135 S.Ct. 2158 (2015) (Thomas, J.).

SUPREME COURT HOLDS THAT § 330(a)(1) DOES NOT PERMIT BANKRUPTCY COURTS TO AWARD FEES TO § 327(a) PROFESSIONALS FOR DEFENDING THEIR FEE APPLICATIONS

The debtor hired the petitioner law firms under 11 U.S.C.A. § 327(a) to assist it in carrying out its duties as a Chapter 11 debtor in possession. When the debtor emerged from bankruptcy, the law firms filed fee applications requesting fees under 11 U.S.C.A. § 330(a)(1), which permits bankruptcy courts to "award . . . reasonable compensation for actual, necessary services rendered by" § 327(a) professionals. The debtor challenged the applications, but the bankruptcy court rejected its objections and awarded the law firms fees for time spent defending their applications. The debtor appealed to the district court, which held that the law firms could be awarded fees for defending their fee applications. An appeal to the Fifth Circuit followed.

The Fifth Circuit dealt with two fee-related issues: (1) whether the bankruptcy court abused its discretion in authorizing a 20% premium fee enhancement to one law firm and a 10% premium fee enhancement to another firm for their unusually successful fraudulent transfer litigation in the debtor's case; and (2) whether the bankruptcy court had been authorized, consistent with 11 U.S.C.A. § 330, to award attorney's fees to the firms for defending their fee applications. The Fifth Circuit affirmed the fee enhancements, but reversed the additional fee awards for litigation related to the fee applications. The Supreme Court granted certiorari on the latter issue and affirmed the judgment of the Fifth Circuit, holding that § 330(a)(1) does not permit bankruptcy courts to award fees to § 327(a) professionals for defending their fee applications.

The Court began its analysis by noting that the American Rule provides the "'basic point of reference'" for awards of attorney's fees: "Each litigant pays his own attorney's fees, win or lose, unless a statute or contract provides otherwise." Because the "American Rule has roots in our common law reaching back to at least the 18th century," and because "[s]tatutes which invade the common law are to be read with a presumption favoring the retention of long-established and familiar [legal] principles," the Court would not deviate from the American Rule "'absent explicit statutory authority.'" The Court also noted that departures from the American Rule have been recognized only in "specific and explicit provisions," most often containing language that authorizes the award of "a reasonable attorney's fee," "fees," or "litigation costs," and referring to a "prevailing party" in the context of an adversarial "action."

The Court found that "Congress did not expressly depart from the American Rule to permit compensation for fee-defense litigation by professionals hired to assist trustees in bankruptcy proceedings. Section 327(a) authorizes the employment of such professionals, providing that a 'trustee, with the court's approval, may employ one or more attorneys, accountants, appraisers, auctioneers, or other professional persons, that do not hold or represent an interest adverse to the estate, and that are disinterested persons, to represent or assist [him] in carrying out [his] duties.'" Stated another way, "§ 327(a) professionals are hired to serve the administrator of the estate for the benefit of the estate," the Court said. In turn, § 330(a)(1) authorizes compensation for such professionals as follows: "After notice to the parties in interest and the United States Trustee and a hearing, and subject to sections 326, 328, and 329, the court may award to a trustee, a consumer privacy ombudsman appointed under section 332, an examiner, an ombudsman appointed under section 333, or a professional person employed under section 327 or 1103—(A) reasonable compensation for actual, necessary services rendered by the trustee, examiner, ombudsman, professional person, or attorney and by any paraprofessional person employed by any such person; and (B) reimbursement for actual, necessary expenses."

The Court explained that "§ 330(a)(1) provides compensation for all § 327(a) professionals—whether accountant, attorney, or auctioneer—for all manner of work done in service of the estate administrator. More specifically, § 330(a)(1) allows 'reasonable compensation' only for 'actual, necessary services rendered.' . . . That qualification is significant. The word 'services' ordinarily refers to 'labor performed for another.'" And in a case addressing § 330(a)'s predecessor, the Court concluded that the phrase "'reasonable compensation for services rendered' necessarily implies loyal and disinterested service in the interest of" a client. "Time spent litigating a fee application against the administrator of a bankruptcy estate cannot be fairly described as 'labor performed for'—let alone 'disinterested service to'—that administrator," the Court said, adding that "[h]ad Congress wished to shift the burdens of fee-defense litigation under § 330(a)(1), it could have done so, as it has done in other Bankruptcy Code provisions, e.g., § 110(i)(1)(C)."

The Court was not persuaded by the various theories offered for why § 330(a)(1) should override the American Rule in the fee-defense context. Accordingly, the Supreme Court affirmed the Fifth Circuit. Editor's Note: The Court's decision was far from unanimous, e.g., three Justices dissented. Note: This material is excerpted from the August 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

60. In re Next Generation Media, Inc., 524 B.R. 824 (Bankr. D. Minn. 2014) (Kressel, J.).

CHAPTER 11 COUNSEL's APPLICATION FOR COMPENSATION APPROVED OVER OBJECTIONS OF THE CHAPTER 7 TRUSTEE AND THE U.S. TRUSTEE

This case began as a chapter 11 case but later was converted to chapter 7 and became administratively insolvent. After conversion, the bankruptcy court approved the application for compensation of chapter 11 counsel and overruled objections of both the UST and the panel trustee. Prior to filing chapter 11, the debtor gave a $25,000 retainer to its chapter 11 counsel. One month after filing, the court approved employment of the chapter 11 counsel. The employment order authorized counsel to submit monthly bills to the debtor and authorized the debtor to pay counsel up to 80% of fees and 100% of costs pending court approval. Under that order, counsel collected $25,000 in fees and costs from the debtor, thereby exhausting the retainer. Two months after filing, the case was converted to chapter 7. After conversion, the chapter 11 counsel requested compensation. The chapter 7 trustee objected to the chapter 11 counsel's retention of the $25,000 retainer, arguing that counsel should disgorge the retainer because the estate was administratively insolvent. The UST also objected and requested turnover of the retainer, arguing that the retainer was property of the estate and that the retainer was subject to pro rata distribution under 11 U.S.C. § 726. The UST also argued that some of the fees were not reasonable and necessary. In overruling both objections, the court determined that the retainer was not property of the estate and that there was no legitimate basis to order turnover or disgorgement. The court explained that under Eighth Circuit law, any unearned portion of a prepetition retainer constitutes property of the estate, but that here, because counsel had already drawn upon the retainer and exhausted it, then there was no unearned portion left to be considered as property of the estate. The court further reasoned that § 726 did not grant the court authority to recover the professional fees. When analyzing § 726, the court reasoned that the statute concerned the distribution of estate property, and that it lacked any reference to "turnover" or "disgorgement." The court concluded that there was no statutory basis for recovering estate property. After applying the lodestar method, the court determined that the fees were reasonable and necessary, overruling both objections to the propriety of the fees.

61. In re Premier Healthcare Services, Inc., 2015 WL 1221975 (Bankr. D. Minn. 2015) (Ridgway, J.).

CHAPTER 11 COUNSEL'S APPLICATION FOR COMPENSATION APPROVED OVER OBJECTIONS OF THE U.S. TRUSTEE

After this chapter 11 case converted to chapter 7 and became administratively insolvent, the bankruptcy court partially approved the application for compensation of chapter 11 counsel. Shortly after filing, the court approved employment of counsel for the debtor. The employment order authorized counsel to submit monthly bills to the debtor and authorized the debtor to pay counsel up to 80% of fees and 100% of costs pending court approval. During the chapter 11 administrative period, the court granted counsel's first application for compensation. One month later, the case converted to chapter 7. The chapter 7 trustee did not employ chapter 11 counsel

after conversion. The chapter 11 counsel filed another application for compensation for both pre-conversion services and post-conversion services. Counsel also sought permission to apply collected payments to accrued fees and costs in accordance with the employment order. The UST objected to the application and requested turnover of the collected payments. The UST argued that the collected payments constituted property of the estate because they were not yet approved by the court and because counsel's receipt of the payments enabled counsel to receive an amount in excess of its pro rata distribution under the priority scheme of § 726. The court denied counsel's request for compensation with respect to post-conversion services, citing § 330's bar on compensation to attorneys who have not been employed by the trustee. As to counsel's request for pre-conversion services, the court reasoned that under the facts of the case, there was no statutory basis to order turnover or disgorgement. The court agreed with a line of reasoning in other bankruptcy cases that § 726 does not serve as a basis to order turnover of compensation for purposes of pro rata distribution when an asset case is converted and becomes administratively insolvent. In overruling the objection, the court applied the Eighth Circuit lodestar method for determining the reasonableness of fees and determined that the pre-conversion fees were reasonable and necessary.

CLAIMS

62. In re Wigley, 533 B.R. 267 (B.A.P. 8th Cir. 2015) (Nail, J.).

LANDLORD CLAIMS: NEW TEST FOR CLAIMS BEYOND STATUTORY CAP OF § 502(b)(6)

Lariat Companies, Inc. ("Lessor"), entered into a ten-year lease with Baja Sol Cantina EP, LLC ("Baja Sol"). The Debtor, Michael Wigley ("Debtor") personally guaranteed the lease. Baja Sol defaulted under the lease and was evicted in July 2010. In state court, Lessor sued Baja Sol and the Debtor and was awarded $2,224,237.00 in damages, plus pre- and post-judgment interest and attorney fees. Lessor then sued the Debtor's wife and the Debtor for various fraudulent transfers. As a result, the Debtor and his wife were found liable to Lessor in the amount of $795,098.00, plus statutory interest, costs, and disbursements.

In February 2014, the Debtor filed a chapter 11 petition. Lessor filed a proof of claim for $1,734,539.00. The Debtor objected on two grounds: (1) the amount sought based on Debtor's personal guaranty of the lease exceeded the amount allowable under 11 U.S.C. § 502(b)(6); and (2) the amount sought based on the various fraudulent transfers from the Debtor to his wife were duplicative of, and subject to the same limitation as, the amount sought based on Debtor's personal guaranty. The claim was then amended to $1,610,787.00. The bankruptcy court sustained the Debtor's objection and the Lessor appealed.

Section 502(b)(6) limits the "claim of a lessor for damages resulting from the termination of a lease of real property . . . ." Recognizing that the operative question in the case was whether the damages "result[ed] from the termination of a lease," the BAP set out a test for making that determination: "would the landlord have the same claim against the tenant if the lease had not been terminated?" The BAP referred to the test suggested by the 9th Circuit but noted that test

was applied when there was a postpetition rejection of a lease, unlike here where there was a prepetition termination of a lease.

Lessor's claim was comprised of four elements: (1) unpaid rent, common area maintenance, and late fees through the eviction date and interest thereon; (2) post eviction rent and interest thereon; (3) attorney fees, costs, and disbursements, including interest thereon; and (4) Debtor's liability for the various fraudulent transfers to his wife and for interest thereon.

With respect to a portion of the first element of Lessor's claim, that is, the late fees and interest, the BAP disagreed with the bankruptcy court that this part of the claim was limited by § 502(b)(6). The BAP stated, "[b]ecause these items accrued prior to termination of the lease, they cannot be said to have resulted from termination of the lease . . . the interest therein cannot be said to have resulted from termination of the lease, either."

As for the second element, the BAP agreed with the bankruptcy court that this part of the claim is limited by § 502(b)(6). "If the lease had not been terminated, [Lessor] would not have a claim for future rents, and without a claim for future rents, [Lessor] would not have a claim for interest thereon."

Applying its new test, the BAP disagreed with the bankruptcy court that the third element was limited by § 502(b)(6), "at least to the extent of the attorney fees, costs, and disbursements the district court awarded [Lessor] in the state court action to recover damages under the lease and guaranty." The BAP further explained, "[b]ecause the damages comprising the first element of [Lessor's] claim . . . accrued prior to termination of the lease . . . the related attorney fees, costs, and disbursements-and the pre-petition interest thereon-likewise cannot be said to have resulted from termination of the lease." However, the BAP noted that the debtor also objected to this element of Lessor's claim on the basis that "[Lessor] had not identified any basis on which the Debtor could be held liable for [Lessor's] attorney fees, costs, and disbursements, other than those awarded Lessor in the state court action." The BAP remanded this issue of entitlement for the fees not awarded by the state court and then the application of its new test.

Finally, the BAP agreed with the bankruptcy court that the fourth element was duplicative of the earlier state court judgment awarding damages for breach of the lease. The BAP stated, "[t]he Uniform Fraudulent Transfer Act . . . does not create a 'new' claim. 'The Minnesota Uniform Fraudulent Transfer Act is not substantive in nature, but instead merely confers an alternate remedy for protecting preexisting creditor rights. The creditor rights a party seeks to enforce must exist under independent law, such as contract law.'"

63. In re Sylva Corp., 519 B.R. 776 (B.A.P. 8th Cir. 2014) (Saladino, J.).

THE THRESHOLD ISSUE THE BANKRUPTCY COURT SHOULD HAVE DECIDED, BEFORE HAVING UNDERTAKEN AN ANALYSIS OF AN EQUIPMENT LESSOR'S ADMINISTRATIVE CLAIM, WAS WHETHER THE DEBTOR HAD WAIVED THE RIGHT TO ASSERT THAT A LEASE WAS NOT IN FACT A TRUE LEASE BUT A DISGUISED SECURITY AGREEMENT

The issue in this case was whether the bankruptcy court erred in analyzing the lessor's motion for allowance of an administrative expense using only the legal standards and evidentiary burdens under § 503(b)(1)(A) instead of those under § 365(d)(5). In its motion, the lessor requested the allowance of an administrative expense for the lease payments due under the lease agreement from the petition date to the date the lease agreement was rejected, plus attorney's fees and expenses related to reclamation. The lessor asserted in its motion that it was entitled to the administrative expense claim under both § 365(d) and § 503(b). The BAP observed that the operative language of both sections is identical: "The trustee shall timely perform all the obligations of the debtor . . . under an [any] unexpired lease . . . until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this title." Both statutes require the trustee to timely perform all of the debtor's post-petition obligations under unexpired leases until such time as the lease is either assumed or rejected. But there are some differences, the BAP pointed out: "Section 365(d)(3) deals with unexpired leases of nonresidential real property, whereas § 365(d)(5) deals with unexpired leases of personal property. The obligation to perform in § 365(d)(5) begins 'from or after 60 days after' bankruptcy filing, whereas the obligation in § 365(d)(3) begins 'from and after' the order for relief. Finally, § 365(d)(5) contains an important exception to the performance obligation since it concludes with the clause 'unless the court, after notice and a hearing and based on the equities of the case, orders otherwise.'" Here, the bankruptcy court expressly declined to consider § 365(d)(5), notwithstanding that the lessor expressly argued in its motion that it was entitled to an administrative expense claim under § 365(d)(5)—a position it had consistently taken throughout the bankruptcy case. The BAP found that the written record supported the lessor's request that its motion be considered under § 365. The BAP also noted that under § 503(b)(1), the burden of proof under this statute is on the claimant seeking the administrative expense claim, but that under § 365(d)(5), "the entitlement to the administrative expense claim is automatic unless the debtor or objecting party can show that the court should order otherwise based on the equities of the case." Thus, the BAP held that by declining to consider the lessor's motion under § 365(d)(5), the bankruptcy court erred as a matter of law by effectively shifting the burden of proof from the objecting party to the claimant. Finally, the BAP stated: "Of course, the foregoing discussion regarding § 365(d)(3) and (d)(5) would be applicable only if the 'lease agreement' were a true equipment lease and not a secured financing arrangement . . . Thus, we believe that is the threshold issue that must be decided before any analysis under § 365 or § 503." Note: This material is excerpted from the January 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

64. In re McCormick, 523 B.R. 151 (B.A.P. 8th Cir. 2014) (Shodeen, J.).

§ 506(b) DOES NOT REQUIRE THAT THE RIGHT TO FEES BE PROVIDED IN THE AGREEMENT UNDER WHICH THE CREDITOR BECAME OVERSECURED NOR DOES IT REQUIRE THAT IT BE IN ALL AGREEMENTS THAT MAKE UP THE SECURED CLAIM OF THE CREDITOR

The BAP began by noting that § 506(b) permits payment of attorney's fees and costs to an oversecured creditor: "To the extent that an allowed secured claim is secured by property the value of which, after any recovery under subsection (c) of this section, is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement or State statute under which such claim arose." The statute requires that four factors be established: "(1) the claim must be an allowed secured claim; (2) the creditor holding the claim must be over-secured; (3) the entitlement to fees, costs, or charges must be provided for under the agreement or state statute under which the claim arose; and (4) the fees, costs and charges sought must be reasonable in amount." Once the four factors are shown, the "statute plainly states that payment of reasonable fees, costs or charges 'shall be allowed.'" In this case, the bankruptcy court's decision was based solely on the third factor. Thus, the BAP's review was limited to the third factor, which required the bankruptcy court to decide whether the agreement under which the claim arose provided for the payment of attorney's fees and costs. The lender argued that the bankruptcy court erred in holding that the state court judgments made the lender oversecured, and thus the judgments constituted the "agreement" under which the lender's claim arose. Instead, the lender argued that the loan documents, the workout agreement, and the debtors' confirmed plan should be considered collectively to constitute the requisite "agreement" required by § 506(b). The BAP found the bankruptcy court's reliance upon the judgments as the "agreement" under which the lender's right to payment of its fees arose was misplaced. The BAP explained that it "[h]ere, the judgments happen to give [the lender] a lien on real property of the judgment debtors in the counties where the judgment was entered, which increases the collateral for [the lender's] claim but does not change the instruments under which the right to claim attorney fees arose." The case was remanded to the bankruptcy court for a determination of the reasonableness and timeliness of the lender's fee request. Note: This material is excerpted from the February 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.

MISCELLANEOUS

65. Bowles Sub Parcel A, LLC v. CW Capital Asset Mgmt. LLC (In re Bowles Sub Parcel A, LLC), 792 F.3d 897 (8th Cir. 2015) (Kelly, J.).

DEFAULT-INTEREST RATE PROVISION WAS A PRESUMPTIVELY VALID LIQUIDATED-DAMAGES PROVISION

The Eighth Circuit held that the bankruptcy court did not err in finding that a default-interest rate provision was a presumptively valid liquidated-damages provision under Minnesota law.
The debtors filed for chapter 11 bankruptcy. The creditor filed timely proofs of claim for default interest in the amount of $1,516,739.80. The debtors objected to the proofs of claim, arguing that the default interest was based upon an unenforceable default interest rate provision. The loan documents contained a provision which stated that the default-interest rate would be 5% in addition to the 5.04% non-default interest rate. The bankruptcy court and, later, the district court, overruled the objection and found that the debtors failed to overcome the presumption that under Minnesota law, the default-interest rate provision was a valid liquidated-damages provision.

On appeal, the debtors argued that the default-interest provision was an impermissible penalty under Minnesota law. Under Minnesota law, liquidated damages are presumed valid, unless it is shown that the liquidated damages provision is an unreasonable penalty. To determine whether "a provision is a valid liquidated damages provision or an impermissible penalty" under Minnesota law, "courts consider whether (1) the amount so fixed is a reasonable forecast of just compensation for the harm that is caused by the breach; and (2) the harm that is caused by the breach is one that is incapable or very difficult of accurate estimation."

Upon review, the Eighth Circuit found ample support in the record for a determination that the liquidated-damages provision was valid. It pointed to language in the promissory notes, which stated "that it would be extremely difficult or impracticable to determine Lender's actual damages resulting from any late payment or default, and such late charges and default interest are reasonable estimates of those damages and do not constitute a penalty." It also pointed to the bankruptcy court's finding that the parties to the notes were "sophisticated businesses knowledgeable about commercial lending practices." The Eighth Circuit also pointed to unrefuted testimony in the record, which stated that damages were difficult to ascertain and that the 5% interest rate was consistent with the default-interest rate of similar loans.
The debtors also argued that the default interest was greatly disproportionate to actual damages because the default interest covered costs already considered in other provisions. In rejecting that argument, the Eighth Circuit referred to unrebutted testimony that the default-interest rate provision compensated for specified, unreimbursed costs resulting from default.

The debtors also argued that the bankruptcy court erred in finding that the default interest was valid, citing a line of cases as support for their proposition that actual damages resulting from promissory note breach are always ascertainable. The Eighth Circuit disagreed and distinguished this case from those cases cited by the debtors, noting that unlike the present case, the cases relied upon by the debtors did not involve securitized commercial loans. The Eighth Circuit

further reasoned that securitized commercial loans have "unique costs that are difficult to quantify."

66. In re Peet, 529 B.R. 718 (B.A.P. 8th Cir. 2015) (Nail, J.).

THERE IS NOTHING IN THE BANKRUPTCY CODE THAT PROVIDES FOR SEVERANCE OF JOINT TENANCY BECAUSE OF A JOINT TENANT'S BANKRUPTCY FILING, AND NOTHING UNDER MISSOURI LAW SO PROVIDES EITHER

The debtors held property in joint tenancy with others pre-petition and at the time of filing under chapter 13, then converted to chapter 7, and the non-debtor joint tenants died shortly thereafter. The chapter 7 trustee sought to sell the entire property for the benefit of the estate (in excess of the applicable, available exemption). The debtors argued that their bankruptcy filing severed the joint tenancy and resulted in the property being held in divisible shares by tenancy in common, such that only their proportionate shares constituted property of the estate subject to liquidation. Under Missouri law, joint tenancy can be destroyed by conveyance by one or more joint tenants during the lifetime of the cotenants. The debtors argued that filing a bankruptcy case constituted a conveyance of title to the chapter 7 estate.

The BAP disagreed, described the debtors' argument as a concept "from the fantasy world of make believe or born as a result of wishful thinking," and explained that the trustee's power of sale derived from avoidance or strong-arm authorities granted under §§ 542—547 of the Code. The BAP noted, however, that while there is no bankruptcy law that renders a bankruptcy a severance of joint tenancy, and nothing under Missouri law, the law of other states may vary, such as Minn. Stat. § 500.19 subd. 5 which specifically provides "A severance of a joint tenancy interest in real estate by a joint tenant shall be legally effective only if . . . (4) a severance is effected pursuant to bankruptcy of a joint tenant."

67. In re Polaroid Corporation, 529 B.R. 887 (Bankr. D. Minn. 2013) (Kishel, J.), *report and recommendation adopted in part by*, Stoebner v. PNY Technologies Inc., 2015 WL 1954373 (D. Minn. 2015) (Schiltz, J.).

UNDER MINNESOTA LAW, IF A CONFLICT EXISTS BETWEEN TWO CONTRACT PROVISIONS, A CONTRACT'S SPECIFIC TERM CONTROLS OVER A GENERAL TERM

The trustee of the Polaroid bankruptcy estates sought recovery from a third party, PNY, of royalties it owed to Polaroid. PNY argued that Polaroid sold its rights in the license as part of an asset purchase agreement. The bankruptcy court acknowledged the claim to be a related proceeding as a classic third-party action that has a relationship to a bankruptcy case but which does not involve one of the core functions of bankruptcy in the adjustment of the debtor-creditor relationship, and held that that, lacking the consent of PNY, the decision of the bankruptcy court would be in the form of a report and recommendation. Judge Kishel found that the APA did not apply to pre-sale royalties and in fact specifically included a carve-out of royalties due, owing and accruing on or before the APA closing date as assets retained by Polaroid. Moreover, that

provision included language that it applied notwithstanding anything else to the contrary in the APA. The district court adopted the report and recommendation, except that it stayed entry of judgment pending determination of PNY's claim in the main case for purposes of setoff.

68. In re Gatewood, 533 B.R. 905 (B.A.P. 8th Cir. 2015) (Saladino, J.)

FILING A PROOF OF CLAIM ON A STALE DEBT IS NOT AN FDCPA VIOLATION

The Eighth Circuit BAP held that the filing of a timely and facially accurate proof of claim on a stale debt in a bankruptcy case, alone, is not a prohibited "false, deceptive, misleading, unfair, or unconscionable" debt collection practice under the Federal Debt Collection Practices Act ("FDCPA").

The debtors filed chapter 13 bankruptcy on October 7, 2013, and listed medical debts on their schedules. One such medical creditor filed a timely proof of claim. The debtors sued the creditor, arguing that collecting on the medical debt was beyond the applicable Arkansas statute of limitations, and that the filing of a proof of claim on a stale debt constitutes a violation of the FDCPA.

The bankruptcy court granted the provider's motion for summary judgment. The court applied Eighth Circuit authority which stated that unless there is actual litigation or the threat of litigation, there is no FDCPA violation when attempting to collect on an otherwise valid, time-barred debt. Under that standard, the bankruptcy court held that the filing of the proof of claim did not violate the FDCPA because it did "not rise to the level of actual or threatened litigation."

The BAP affirmed, but under a different standard. The BAP determined that filing a proof of claim on a stale debt, alone, refutably invokes litigation, and constitutes an action to collect a debt, but that the ultimate determination was whether such filing was false, misleading, deceptive, unfair, or unconscionable under the FDCPA. The BAP cited a standard from the Middle District of Tennessee, which reasoned that while not every filing of a proof of claim on a stale debt is an automatic violation of the FDCPA, an FDCPA violation could exist in the bankruptcy claims process. Applying that rationale to this case, the BAP found that the debtors listed the debt in their schedules, the creditor filed a timely proof of claim, and that the claim was facially accurate and not misleading, and that the debtors did not object to the claim. On this record, the BAP determined that the filing of the proof of claim on the stale debt, alone, did not violate the FDCPA because there was no prohibited "false, misleading, deceptive, unfair, or unconscionable debt collection practice."

69. In re RFC and RESCAP Liquidating Trust Actions, 2015 WL 3408120 (D. Minn. 2015) (Nelson, J.).

DISTRICT COURT ALLOWS SUBPOENA OF THIRD-PARTY EMPLOYERS OF BORROWERS ON STATED INCOME LOANS

This case involved the defendants' sale of allegedly defective mortgage loans to the plaintiff, RFC. RFC asserted breach of contract and indemnification claims, based on numerous loans that were purchased as "stated income" or "stated income/stated asset" loans from certain defendants. As part of the discovery for this action, RFC proposed to issue subpoenas to the third-party employers of borrowers of stated income loans.

The defendants opposed this request on several grounds. Defendants argued that the discovery request was not relevant and that the request was unduly burdensome and could potentially harm the borrowers. In response, the plaintiffs argued that the information was relevant, that the request was not unduly burdensome, and that the defendants had no standing to quash the third-party subpoenas. Finally, if the district court granted the plaintiffs' request, the defendants requested additional time to rebut plaintiffs' breach allegations based on the information discovered as a result of the subpoenas until plaintiffs revise the breach allegations or confirm they will not be revising the allegations.

In granting the plaintiffs' subpoena requests, the district court first addressed relevance. "Federal Rule of Civil Procedure 26(b) provides for the discovery of non-privileged matter relevant to any party's claim or defense. This standard is liberal in scope and interpretation, 'extending to those matters which are relevant and reasonably calculated to lead to the discovery of admissible evidence.'" Based on the plaintiffs' assertions that the subpoenas may help establish breaches of representations, breaches of warranties, and the reliability of the parties' reunderwriting experts in assessing the reasonableness of any borrower's stated income, the district court found the proposed discovery relevant under the broad scope of relevance as provided in the Federal Rules.

In response to the defendants' argument that the subpoenas would create an undue burden and create potential harm to borrowers, the district court stated that "these arguments are conclusory and speculative, and are not sufficiently particularized to establish good cause under Fed. R. Civ. P. 26(c). Rule 26(c) permits the court to "issue an order to protect a party or person from annoyance, embarrassment, oppression, or undue burden or expense . . ." for good cause shown. The district court also noted that it "must balance [d]efendants' arguments for a protective order against [p]laintiffs' arguments for the relevance of and need for the requested information." Based on this reasoning, the district court found that the balance weighed in favor of issuing the subpoenas.

As for the defendants' request for additional time to rebut the allegations, the district court stated that "if newly acquired information comes into a either party's possession, or for good cause shown, the parties may seek leave of Court to amend their earlier disclosures.

70. Heritage Bank v. Woodward (In re Woodward), __ B.R. __, 2015 WL 4923520 (B.A.P. 8th Cir. 2015) (Schermer, J.).

ABSOLUTE PRIORITY RULE APPLIES IN INDIVIDUAL CHAPTER 11 CASES

After the debtor filed for relief under chapter 7, she acquired her principal residence from the Elliotts. The debtor signed a promissory note in their favor, and also granted them a security interest in the property. Subsequently, the Elliotts agreed to modify the due date of the balloon payment by extending it a year.

After the case converted to one under chapter 11, the Elliotts filed a secured proof of claim. Heritage Bank, an unsecured creditor, objected to the proof of claim based on the filing's timeliness. The bankruptcy court overruled the objection, and allowed the claim. Heritage Bank also objected to the Elliotts voting as an impaired class because their claim was a postpetition claim. The bankruptcy court ruled that the Elliotts held an allowed secured claim, and because the plan altered the treatment of their claim, the Elliotts were an impaired class entitled to vote on the plan.

The Elliotts voted in favor of the debtor's fifth amended plan. The bankruptcy court confirmed this plan. Heritage Bank appealed, arguing that the plan should not have been confirmed because: (1) an impaired class did not accept it; (2) it violated the absolute priority rule; and (3) it did not call for payment of all of the debtor's disposable income.

The BAP held that an impaired class of claims accepted the plan, and that the absolute priority rule applies in individual chapter 11 cases.

The BAP determined that the Elliotts held an allowed claim, and that it entitled them under the plain language of § 1126(a) to vote on the plan. The BAP explained that the Elliotts indeed were impaired because the balloon payment's deadline had been extended. The court also held that § 1123(b)(5)'s prohibition against the modification of a security interest in a debtor's principal residence can be waived. Thus, the Elliotts, as holders of an allowed claim, and as the sole members of an impaired class, satisfied the requirements of § 1129(a)(10).

The BAP held that the absolute priority rule applies in individual chapter 11 cases to prevent debtors from retaining prepetition property. The following supports the holding: (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 the absolute priority rule; and (3) the weight of existing authority.

71. Bank of America, N.A. v. Caulkett, 135 S. Ct. 1995 (2015) (Thomas, J.).

DEWSNUP DICTATES THAT A CHAPTER 7 DEBTOR MAY NOT VOID A JUNIOR MORTGAGE LIEN UNDER § 506(d) WHEN THE DEBT OWED ON THE SENIOR MORTGAGE LIEN EXCEEDS THE CURRENT VALUE OF THE COLLATERAL

The Court held that the reasoning of Dewsnup dictates that a Chapter 7 debtor may not void a junior mortgage lien under § 506(d) when the debt owed on the senior mortgage lien exceeds the current value of the collateral. Note: This material is excerpted from the July 2015 issue of the Bankruptcy Current Awareness Alert newsletter, with permission. Copyright (c) 2015 Thomson Reuters/West. For more information about this publication please visit www.legalsolutions.thomsonreuters.com.