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<u>Nine material falsehoods in Debtors' bankruptcy petition leads to denial of discharge for husband, but not wife</u>

<u>In re Bren</u>, No. 04-1522 (8th Cir., Jan. 27, 2005) (Unpublished). Bruce and Barbara Bren ("Debtors"), equal and sole shareholders of Bruce Bren Homes, Inc., jointly filed bankruptcy in December of 2001. Michael Jordan ("Jordan") had signed a residential building contract with Bruce Bren Homes, Inc., which Jordan later terminated because of an alleged failure of performance. After the Debtors filed their bankruptcy petition, Jordan objected to the dischargeability of certain debts, and generally to the Debtors' discharge. The issue before the Bankruptcy Court was whether the Debtors should be denied a discharge for knowingly and fraudulently making a false oath or account in, or in connection with, a bankruptcy case pursuant to Section 727(a)(4)(A) of the Bankruptcy Code. Nine material falsehoods were found in the Debtors' petition. Because of the complexity of their affairs, the fact the schedules were mostly accurate, and the Debtors did not hide the errors once called to their attention, Judge Kressel determined that the Debtors lacked the intent to defraud. Jordan appealed, and the BAP reversed, holding that the Bankruptcy Court's finding of a lack of fraudulent intent was clearly erroneous. The Debtors appealed.

The Eighth Circuit Court of Appeals split the BAP's decision and held that only Bruce Bren had the requisite intent to defraud. Of significant importance for the majority opinion, the Court of Appeals observed that Bruce Bren exercised control over the financial affairs of the business, Barbara Bren only signed checks from time to time. Noting first that the complexity of one's financial affairs is not a basis for a sloppy bankruptcy petition, the Court of Appeals then determined that Bruce Bren's deliberate and obstinate ignorance regarding his company's financial affairs was reckless, and perhaps willful, thus indicating Bruce Bren's fraudulent intent. On the other hand, while Barbara Bren was also ignorant about her own financial affairs, she came forward with information regarding a modest inheritance. The Court of Appeals found this admission to be strong evidence that there was no evidence of fraudulent intent. The BAP was thus affirmed in part and reversed in part.

Judge Smith, Circuit Judge, disagreed with the conclusion that there was strong evidence Barbara Bren lacked fraudulent intent. Because Barbara Bren was equally cavalier in her attitude toward the bankruptcy petition's accuracy, did not read her petition, and made no attempt to correct any errors in the petition, Judge Smith found the majority's opinion rendered Barbara Bren's oath virtually meaningless. Judge Smith believed the subject matter of Barbara Bren's false oath was also material, and felt that she should also be denied a discharge.

<u>Trustee Avoids Postpetition Payments to Spouse</u>

<u>Cox v. Griffin (In Re Griffin)</u>, Case No. 04-6052WA (8th Cir. Bankruptcy Appellate Panel, Jan. 27, 2005). The BAP affirmed the Bankruptcy Court's Order avoiding the Debtor's post-petition payments to his spouse. The Debtor and his spouse ("Mrs. Griffin") executed a prenuptial agreement in April 2000 that purported to transfer a parcel of real property (the "Property") to Mrs. Griffin. The Debtor also gave Mrs. Griffin a quitclaim deed for the Property. The couple married two days later. In December 2000, the Debtor purchased a liquor store business located on the Property. Though the Debtor formed an LLC to hold the liquor store

assets, he never transferred the assets to the LLC.

The Debtor filed for Chapter 11 in January 2002. The case was converted to Chapter 7 on February 5, 2003. Mrs. Griffin filed her quitclaim deed on February 20, 2003. Post-petition, but prior to conversion, the liquor store made payments of $5,000 a month to Mrs. Griffin. Following conversion, the Trustee filed an adversary proceeding against Mrs. Griffin seeking the $65,000 in post-petition payments she received from the liquor store. Mrs. Griffin claimed that she owned the Property, and the $5,000 payments were rent. The Trustee contended that the prenuptial agreement failed to convey an interest in the Property to Mrs. Griffin, and even if it did, Mrs. Griffin failed to record the quitclaim deed prior to the commencement of the case. The BAP held that since the quitclaim deed was filed post-petition, the Trustee had a superior interest in the Property under Section 544(a)(3) of the Bankruptcy Code, and Mrs. Griffin did not have a right to receive rent.

Spouse's Income May Not Be Considered Where Debtor Has No Income

In Re: Mike Rysso, Bky. No. 04-43622 (Bankr. D. Minn., Jan. 28, 2005). The Bankruptcy Court held that it is not "substantial abuse" under 11 U.S.C. § 707(b) to grant relief to a debtor who has no income and limited prospects, even where the debtor's spouse has substantial income.

The Debtor had been a pilot for Northwest Airlines and was convicted of tax evasion in May 2003. As a result of that conviction, he is no longer employable in the airline industry and had been unemployed since June 2003. The Debtor's wife, however, is employed as a physician with a gross monthly income of $16,564.67. After average monthly deductions and household expenses, the couple had approximately $1,600 in disposable monthly income.

The Debtor filed a voluntary Chapter 7 bankruptcy petition on June 29, 2004 listing $68,807 in consumer debt. The U.S. Trustee filed a motion to dismiss the case on the grounds that granting the Debtor a discharge would constitute substantial abuse under Section 707(b). The U.S. Trustee asserted that the Debtor could fund a Chapter 13 plan and could repay a substantial portion of his unsecured debts within three years. Although the Debtor had no regular income to fund a Chapter 13 plan, the U.S. Trustee argued that the Debtor's wife's income should be considered and that it was sufficient to create the necessary disposable income to fund a plan.

The Court noted that generally in cases where the debtor is married and the spouse has not filed bankruptcy, it is accepted practice to include the non-debtor spouse's income in determining the debtor's disposable income. However, in all such cases both the debtor and nondebtor spouse had income. In this case the Debtor had no income to contribute. The Court explained the formula for calculating disposable income as follows: debtor's gross income (I) minus state and federal withholding taxes (W) minus necessary expenses for maintenance of debtor and debtor's dependents (E) equals disposable income (DI). The Court held that, in calculating disposable income, the non-debtor spouse's income is used to reduce joint household expenses, but cannot be considered as an increase in the debtor's income.

A substantial abuse analysis in the Eighth Circuit must focus on whether the debtor has the ability to pay a portion of the debtor's unsecured debt with future income. In the present case since the spouse paid all of the household expenses, the formula calculation looked like this: zero (I) minus zero (W) minus zero (E) equals zero (DI). The court concluded that the Debtor had no disposable income. Even after considering his wife's income, the Debtor still had no income with which he could fund a Chapter 13 plan. Granting the Debtor a discharge would not, therefore, be a substantial abuse of the provisions of Chapter 7.

Debtor's Church Pension Is Not Excluded From Estate.

In re Clifford, Bky. No. 04-33909 (Bankr. D. Minn., Feb. 2, 2005). The Bankruptcy Court was asked to determine whether a debtor's employer-sponsored pension fund, which contains language sounding in a spendthrift trust clause, should be excluded from the debtor's estate pursuant to 11 U.S.C. §541(c)(2), which provides:

> A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.

The Debtor's pension fund contained the following anti-alienation provision:

> Benefits May Not Be Assigned or Alienated. Except as otherwise expressly permitted by the Retirement Plan, or required by law, the interests of participants and their beneficiaries under the Retirement Plan or this Agreement may not in any manner whatsoever be assigned or alienated, whether voluntarily, directly or indirectly.

The Debtor's pension fund was a defined contribution plan under Internal Revenue Code § 403(b)(9), a church plan. The Bankruptcy Court did not find a federal or state statutory source of enforcement for the anti-alienation provision (The plan was not governed by ERISA, in which case it would have been excluded). The Debtor argued that Minnesota's spendthrift trust law was a source of enforcement. The Bankruptcy Court disagreed and held that Minnesota's spendthrift trust laws were fashioned in equity and premised on a recognized right of a benefactor to control the gift of the benefactor's own property. Stated differently, the Court found a benefactor's interest in directing his or her gift to a beneficiary was of paramount importance. Absent the benefactor/beneficiary relationship, the Minnesota Supreme Court has never allowed a debtor to be protected by a spendthrift trust clause.

In reaching its decision, the Bankruptcy Court characterized the employer's contributions to the Debtor's pension fund as "deferred compensation" as opposed to "gifts" from a benefactor. Due to this characterization, the Bankruptcy Court stated that "the rationale underpinning Minnesota spendthrift trust protection simply does not apply." The Bankruptcy Court went on to say "[t]he anti-alienation language is gratuitous and not enforceable under [the Minnesota spendthrift trust] law."

Judge Kressel Offers A Clinic On Minnesota Breach Of Contract Law

In re Health Risk Management, Inc. (Moratzka v. Loop Corp.), Bky. No. 01-43354 – 01-43357, Adv. No. 03-4113 (Bankr. D. Minn., Jan. 13, 2005). Judge Kressel explores Minnesota contract law in detail. Beginning with the basic elements necessary to prove breach of contract, the opinion focuses on three of the defenses raised by defendants: (i) mutual mistake; (ii) misrepresentation; and (iii) rescission. If you are specifically in need of a detailed treatise on misrepresentation, this decision is the place to look.

NEWS

CM/ECF Update From The Bankruptcy Court Clerk's Office

The Bankruptcy Court continues its migration to the new case management and electronic case filing system, CM/ECF. Systems staff are focusing on conversion of nearly two million images to the new system, mapping the current data dictionary to CM/ECF, and developing new forms. Systems staff are also preparing to shift from a Solaris to a Linux operating system in preparation for the conversion later this year.

Case management staff are involved in a series of training programs to enhance their understanding of CM/ECF and upgrade their customer service skills as they prepare to assist attorneys in the conversion process. Case administrators will be serving as attorney trainers and test filing monitors, and will continue to provide telephone assistance on the help desk.

In the near future the Court will announce a series of attorney training options for the new system from online computer based training modules to hands-on training at the Minneapolis Courthouse. Since conversion to CM/ECF will occur over a weekend, the Court will require simple test filings to help users understand the differences between ERS and CM/ECF and ensure a smooth transition to the new system. Training information will be emailed to all ERS registered attorneys and trainees and will also be posted on the Court's web site, www.mnb.uscourts.gov.

In preparation for the conversion the Court is also attempting to update its attorney database with current post office and email addresses. Since electronic noticing will be required with CM/ECF, accurate email addresses will be critical. Attorneys are asked to review and update their personal information in ERS using option "4" on the ERS Filing Option menu.