Bankruptcy Bulletin

A Publication of the Minnesota State Bar Association Bankruptcy Section

November-December 2007

IN THIS ISSUE

TAX REFUNDS NOT EXEMPT UNDER MISSOURI LAW

In In re Benn, Jr. (Benn Jr. v. Cole), and In re Mohrhard (Mohrhard v. Cole), No. 06-2217 (8th Cir. July 10, 2007), the Eighth Circuit held in the two consolidated cases that tax refunds are not exempt under Missouri law.

The debtors contended that tax refunds were exempt under the following Missouri statute:

> Every person by or against whom an order is sought for relief under Title 11, United States Code, shall be permitted to exempt from property of the estate any property that is exempt from attachment and execution under the law of the state of Missouri or under federal law, other than Title 11, United States Code, Section 522(d), and no such person is authorized to claim as exempt property that is specified under Title 11, United States Code, Section 522(d).

Missouri Rev. Stat. § 513.427. The debtors and trustees agreed that Missouri opted out of the bankruptcy code exemptions under this provision. The debtors also contended that the statute provide that certain property was exempt, namely property that is not subject to attachment and execution. Because tax refunds are not subject to attachment or execution, the debtors argued that the tax refunds were exempt under Missouri law. The Bankruptcy Court disagreed and entered an order finding that the refunds were property of the estates. The BAP reversed.

The Eighth Circuit noted that "exemption" is a term of art in bankruptcy and means "laws enacted by the legislative branch which explicitly identify property [that] judgment-debtors can keep away from creditors for reasons of public policy." Id. at 5 (quoting In re Benn, 340 B.R. 905, 914 (8th Cir. BAP 2006) (Kressel, J. dissenting)). The court held that a plain reading revealed that the Missouri statute did not announce new exemptions as the debtors contended. Id. at 5-6. This reading was bolstered by existence of the specific exemptions found in other Missouri statutes. Id. at 6. Finally, debtors' reading would create illogical results. For example, it would exempt a debtor's interest in a limited liability company as it is only subject to a charging order, not attachment or execution. Id. at 7.

JUDGMENT FOR RETALIATION IS HELD NON-DISCHARGEABLE

In the case of *Sells v. Porter (In re Porter)*, Nos. 07-6008 and 07-6013 (8^{th} Cir. B.A.P. Sept. 21, 2007), the BAP affirmed the bankruptcy court's decision that a civil judgment entered against the debtor on Holly Sells' claims for sexual harassment and retaliation was excepted from discharge under 11 U.S.C. § 523(a)(6).

Prior to his bankruptcy filing, the debtor and Huffer were co-owners of Mr. Speedy Car Care Center, and Sells was Mr. Speedy's employee. Huffer sexually harassed Sells by calling her repeatedly, asking for sex, and grabbing parts of her body. When Sells complained to the debtor, she was told that she should not flirt with Huffer. Sells was eventually fired when she refused to sign a memo prepared by the debtor that purported to acknowledge that the sexual contact was consensual, that both were at fault, and that it would not take place again.

Following a trial in Arkansas, the jury awarded Sells compensatory and punitive damages for sexual harassment and retaliation, finding that the debtor and Huffer acted with "malice or reckless indifference" to Sells' rights. The debtor filed for bankruptcy and Sells commenced a non-dischargeability proceeding against the debtor for "willful and malicious injury" under 11 U.S.C .§ 523(a)(6). The bankruptcy court granted Sells' summary judgment motion on the basis of collateral estoppel.

On appeal, the BAP considered the elements of collateral estoppel and the debtor's argument that the issues in the district court case were not the same as the ones in the dischargeability proceeding. The BAP also noted that malice and willfulness are two different elements that must be established to prevail under Section 523(a)(6), and that it is the intent to cause both injury and harm that results in a willful and malicious injury. In considering this standard, the BAP determined that the debtor had taken purposeful action against Sells in order to force her to surrender her rights and that he intended to harm Sells when he retaliated against her. The BAP also refused to consider Sells appeal that Huffer's action should be imputed to the debtor by virtue of their partner relationship because the bankruptcy court had already found in her favor.

EIGHTH CIRCUIT BAP AFFIRMS PROPOSED CHAPTER 13 PLAN DESPITE SHORTENED REPAYMENT PERIOD

The Eighth Circuit BAP recently affirmed a payment period in a Chapter 13 plan for less than 60 months for a debtor who earned above his local average median income, even though the plan would not provide full payment for the debtor's unsecured creditors. Such a result arguably conflicts with one of the purposes of BAPCPA to require higher-income debtors to pay 100% of their unsecured claims, or provide for a 60-month payment plan. The BAP relied on a strict textual approach to reach this result.

The debtor calculated his disposable income, as required by BAPCPA amendments, by using Official Form 22C, which relies on a six-month window of debtor's income and calculates debtor's expenses using IRS national and local standards. The results from Form 22C indicated the debtor had an income above the median income for his locality (Arkansas), however, the debtor also had negative disposable income. This differed from the Bankruptcy Schedules I & J filed by the debtor that showed he had an actual monthly surplus of $600.

The debtor proposed a 48-month plan for $600 a month, which would provide for administrative costs, secured debts, and priority tax claims that existed, as well as a 75% pro rata distribution for unsecured claims. The parties agreed that under BAPCPA, if a debtor has negative disposable income, it is not required to make any payments to unsecured creditors under the plan. Nonetheless, the Chapter 13 Trustee argued, without citing a supporting statute, that since the debtor's earnings were above the median income in Arkansas, the Court could not confirm anything less than a five-year plan.

The statute provides that if the Trustee objects to the plan, the Court can confirm the plan only if the "plan provides that all of the debtor's projected disposable income to be received in the applicable commitment period beginning on the date that the first payment is due under the plan will be applied to make payments to unsecured creditors under the plan." 11 U.S.C. § 1325(b)(1). For an above-median debtor, the "applicable commitment period" is defined as five years. 11 U.S.C. § 1325(b)(4).

The material issue in this case was the meaning of "projected disposable income." Prior to BAPCPA, the court interpreted "disposable income" by subtracting the debtor's reasonable expenses disclosed on Schedule J from the debtor's income disclosed in Schedule I. The Chapter 13 Trustee here advocated a similar approach. Under the BAPCPA amendments, Disposable income is defined as "current monthly income received by the debtor," less any reasonable support expenditures for any dependants. 11 U.S.C. § 1325(b)(2). BAPCPA also defines the term "current monthly income," which, according to the Eighth Circuit BAP, "Chapter 13 debtors calculate by using official Form 22C." 11 U.S.C. § 101(10A).

The court noted that the BAPCPA term "projected disposable income" is not specifically defined, and courts have varied in their application. Some courts continued to apply Schedules I and J while others rely on applying Official Form 22C.

The courts following the Official Form 22C approach also rely on the requirements set forth for confirmation of Chapter 11 plans which require that "the value of the property to be distributed under the plan is not less than the projected disposable income of the debtor (as defined in Section 1325(b)(2)) to be received during the 5-year plan period." 11 U.S.C. § 1129(a)(15). Courts found that the link for "projected disposable income" in Section 1129 to the definition of "disposable income" in Section 1325 shows that Congress intended "projected disposable income" and "disposable income" to be the same concept.

The Eighth Circuit BAP adopted this reasoning and found that projected disposable income is simply "annualized disposable income," and the applicable commitment period serves as a multiplier for the disposable income, dependent on the amount the debtor must pay to the unsecured creditors. Since debtor had a negative disposable income, there was no required amount to pay to the unsecured creditors, and thus no obligation to carry on the plan beyond what was required to pay the other administrative costs, secured debts, and priority tax claims.

STUDENT LOANS NOT DISCHARGEABLE

In Matthew E. and Julie E. Collins v, Education Credit Management Corporation and The Educational Resources Institute, Inc., In re Collins, Adv. 06-3492 (J. O'Brien) (Bankr. D. Minn. 2007) the Bankruptcy Court ordered that the student loan debts of Matthew E. Collins ("Collins") owing to Education Credit Management Corporation ("ECMC") do not constitute an undue hardship and are nondischargeable.

Collins commenced an adversary proceeding seeking discharge of his student loans pursuant to 11 U.S.C. 523(a)(8). In reaching its decision, the Bankruptcy Court applied the totality of circumstances test under which "the court considers (1) the debtor's past, present and future financial resources, (2) the debtor's reasonable and necessary living expenses, and (3) any other relevant circumstances". In re Reynolds, 425 F.3d 526, 529 (8^{th} cir. 2005). The court went on to quote Reynolds further, stating that "if the debtor's reasonable future financial resources will sufficiently cover payment of the student loan debt – while still allowing for a minimal standard of living – then the debt should not be discharged." Id. at 532.

In applying the totality of circumstances test to Collins, the court noted that (i) Collins is a doctor of chiropractic, (ii) in each year between 2000-2006, Collins earned over $50,000, except 2003 when he earned $28, 250 and 2004 when he earned $49,744, (iii) Collins is only 33 years old and is in good health, (iv) Collins' wife is only 30 years old, has a college education and is in good health, as are their three children, and (v) the field of chiropractic is prosperous and growing in Minnesota.

ECMC argued that Collins' strong earning capacity, now and going forward, and the availability of the Income Contingent Repayment Plan were sufficient to allow Collins and his family to weather their financial difficulties until their situation improved. The Bankruptcy Court agreed, noting that "Significant earning capacity is a fact which the court must consider in the undue hardship analysis." In re Winsborough, 341 B.R. 14, 18 (Bankr. W.D. Mo. 2006). Further, the Bankruptcy Court stated that Collins' financial burden was a "bump in the road" and that the general discharge along with "a combination of belt tightening and income maximization will provide substantial opportunity for full financial rehabilitation in due time."

The court reiterated that Collins and his wife are young, health, highly educated and in Collins' case, employed in a growing and lucrative career field. In holding that Collins student loan debt was nondischargeable, the Bankruptcy Court stated that "this case presents precisely the sort of debt the discharge of which §523(a)(8) was designed to preclude."

ATTORNEY'S FEES DISGORGED FOR RETAINER AGREEMENT THAT VIOLATED LOCAL RULE

In the companion cases of *In Re Deanna Bullen*, Bankr. D. Minn., No 05-31011 and *In Re Brendan Y. Huynh*, Bakr. D. Minn., No 05-37994 (Sept. 18, 2007) (J. O'Brien), the Bankruptcy Court for the District of Minnesota held that the retainer agreement used by the debtors' attorney ("Attorney") violated Local Rule 9010-3(e)(4) and that all fees received by Attorney in connection with the two cases should be disgorged. The court further held that Attorney was enjoined from any further use of the improper retainer agreement and that any revised retainer agreement be subject to the Court's approval.

The United States Trustee filed the motions before the court in this case because the UST believed Attorney was either negligently or intentionally filing inaccurate 2016(b) statements which indicated she was paid far less in fees than the amounts she was actually paid. As a result of these statements, the UST filed motions asking the court for relief in the form of disallowance and disgorgement of all fees Attorney received in these two cases, as well as other sanctions.

Upon review of the two cases and their respective 2016(b) statements, the court held that the evidence did not support the accusations brought by the UST, nor the accompanying requested sanctions. The court found that the inaccurate disclosures constituted nothing more than inadvertent error.

This did not end the inquiry however, as the court decided to review the propriety of Attorney's retainer agreement even though it was not an issue raised by the UST. The court held that the language in Attorney's agreement regarding withdrawal of the attorney violated the Local Rule 9010-3(e)(4) which stipulates that the attorney is to represent the debtor in all matters in the debtor's main bankruptcy case unless and until a valid substitution of counsel is filed or there is an order from the court granting withdrawal. Because Attorney's retainer agreement informed the client that the attorney was permitted to withdraw for any reason, including nonpayment of fees by the client and contained language indicating that any appearances by the attorney beyond the first meeting were subject to further fees, the agreement violated the local rule, and was "misleading" and "intimidating" to the client/debtor.

The court rejected Attorney's proposed revised retainer and instead provided an "acceptable" "Withdrawal of Attorney" provision for her revised retainer:

> WITHDRAWAL OF ATTORNEY. Attorney reserves the right, upon nonpayment of Client of any fees or costs incurred pursuant to this agreement to ~~require~~ *request that* Client ~~to~~ obtain alternative counsel ~~or~~ *and*, if Client fails to do so within a reasonable time, to apply to the Bankruptcy Court for permission to withdraw. Until substitute counsel or Bankruptcy Court permission to withdraw is obtained, Attorney will continue to provide legal services to Client in connection with Client's bankruptcy case to the extent required by Local Bankruptcy Rules 9010-3(e)(4), which requires that.
>
> (4) Effect of Failure to Comply.
>
> *Until a substitution is filed or an order is entered allowing the original attorney to withdraw, the original attorney is the client's attorney of record and the original attorney shall represent the attorney's client in bringing and defending all matters or proceedings in the bankruptcy case other than adversary proceedings in which the original attorney has not yet made an appearance. Failure to receive advance payment or guarantee of attorney's fees is not grounds for failure to comply with this subsection.*

Additionally, because an improper retainer agreement was used for both debtors' cases, the court ordered disgorgement of the fees received by Attorney for both debtors.

The following summaries are reprinted from the Case Law Update and Bankruptcy Trends materials from the MSBA's 2007 Bankruptcy Institute with the permission of Judge Robert J. Kressel and Faye Knowles, whom the Bankruptcy Bulletin wishes to thank.

CREDITOR WAIVES RIGHT TO ENFORCE ARBITRATION CLAUSE BY PARTICIPATING IN BANKRUPTCY LITIGATION Lewallen v. Green Tree Servicing, LLC, 487 F.3d 1085 (8th Cir. (Mo.) 6/4/07) (Gibson, J.)

The Eighth Circuit affirms the district court conclusion that a creditor who extensively participated in the debtor's adversary proceeding waived its right to enforce the arbitration clause in its credit agreement with the debtor. A Chapter 13 debtor objected to her secured creditor's claim and raised consumer protection counter-claims in August of 2004. At the creditor's suggestion in March 2005, the court dismissed the claim objection and the debtor filed an adversary proceeding. Both parties served discovery requests while the creditor sought and obtained several extensions of time to answer. In late July 2005, the creditor moved to dismiss or to compel arbitration under the arbitration clause in the credit agreement. The lower court ruled that the creditor had waived its right, having (a) known of the arbitration right, (b) acted inconsistently with it, and (c) prejudiced the other party by its inconsistent acts.

The Eighth Circuit affirms, acknowledging the strong federal policy in favor of arbitration, but finding that the creditor did waive its arbitration right. The creditor's participation in litigation, begun at its own suggestion, was inconsistent with its known arbitration right. The creditor argued that it invoked the right only two months after the adversary was commenced, but the court concludes that it should have done so in 2004 in response to the claim objection that raised affirmative causes of action against the creditor. In addition, the creditor's service of discovery and participation in the claim objection and litigation processes prejudiced the debtor. Although participation in discovery is not per se prejudicial, the creditor "sent [the debtor] down the road of trial preparation at a time when she can ill afford to waste resources."

MISSOURI OPT-OUT STATUTE CANNOT BE BROADLY CONSTRUED TO PROVIDE EXEMPTION FOR TAX REFUND <u>Benn v. Cole</u> (In re Benn), 2007 WL 1976071 (8th Cir. (Mo.) 7/10/07) (Colloton, J.)

The Eighth Circuit Court of Appeals reverses the BAP decision that the debtors' tax refund is exempt under Missouri law, and agrees with the original bankruptcy court decision and the BAP dissent that no applicable statute provides such an exemption. Missouri "opted out" of the so-called federal exemptions of Code § 522(d). The Missouri opt-out statute states that a bankruptcy debtor may exempt "any property that is exempt from attachment and execution" under Missouri law or non-bankruptcy federal law." Other Missouri statutes define property that is exempt, and do not expressly include tax refunds. A divided BAP majority concluded that this language in the opt-out statute exempted tax refunds because (a) when the case was filed the refunds were "contingent" and contingent interests cannot be attached under Missouri law, or (b) Internal Revenue Code provisions prohibit assignment to a third party so the funds are not subject to attachment and execution.

Reversing and adopting the reasoning of Chief Judge Kressel's BAP dissent, the Court of Appeals notes that "exemption" is a term of art in bankruptcy used to "explicitly identify property that judgment-debtors can keep away from creditors for reasons of public policy." The language of the opt-out statute does not do this, but rather makes reference to other statutes that create exemptions. The BAP majority equated the phrase "exempt from attachment" with "not subject to attachment," thereby misinterpreting the meaning of "exempt." Use of that term was intended to refer to those Missouri statutes explicitly creating exemptions. Because the opt-out statute does not create an exemption and tax refunds are not made exempt elsewhere in Missouri law, they are not exempt in bankruptcy, despite the fact that creditors in this situation might not have been able to execute on them under state law. The court was not troubled by the argument that this interpretation could include in the bankruptcy estate some assets unavailable to a non-bankruptcy creditor. The legislature could have intended that in exchange for bankruptcy relief, a debtor give up some common law rights.

DEBTOR HAS NO RIGHT TO COUNSEL IN HOMESTEAD EXEMPTION DISPUTE AND OBJECTION IS SUSTAINED
Eagle v. Bank of America (In re Eagle), 2007 WL 2278902 (8th Cir. BAP (Ark.) 8/10/07) (Schermer, J.)

The Eighth Circuit BAP affirms the order sustaining a creditor's objection to the pro se debtor's homestead exemption and rules that the debtor had no constitutional right to court-appointed counsel in the dispute. Prior to bankruptcy, the debtor used an NSF check to obtain a cashier's check to redeem property, and the bank sued and filed notice of lis pendens against the property. The soon-to-be-debtor later sold the property to a third party, apparently retaining a leasehold interest, then filed Chapter 7. The case was dismissed for failure to file schedules, but at the debtor's request was reinstated. At the reinstatement hearing, the bankruptcy court noted that the creditor was "fixing to come after" the debtor and urged him to obtain counsel, to which the debtor responded with the now-familiar famous last words "bring it on." The creditor did, objecting to the debtor's claimed homestead exemption in the property he had sold pre-petition. At the hearing, the court again remarked on the debtor's pro se status and the debtor replied that he would like an attorney, but when the court was reminded by the creditor of the prior hearing exchange, the objection exemption hearing went forward. Finding that the debtor had no exemptible interest in the property, the court sustained the objection.

On appeal, the BAP affirms. Having transferred the property prior to filing, the debtor had no ownership interest and is not entitled to a homestead exemption in property he does not own. Nor did he have a constitutional right to counsel, which exists only in favor of an indigent whose physical liberty is at stake.

AFTON DEBTOR'S PROPERTY IS RURAL, NOT URBAN
In re Engstrom, 2007 WL 1775255, (Bank. D. Minn. 6/20/07) (Kishel, C.J.)

The debtor's homestead property contained approximately 5 acres of land and was located just outside the village limits of Afton, Minnesota. The debtors had less than $200,000 of equity in the property and sought to exclude the entire property on the grounds that the property was rural in nature. A creditor objected on the grounds that the size of the parcel of real estate exceeded that which may be exempted under Minnesota statute given the location and characteristics of the property. After an exhaustive discussion of the location and attributes of the property in question, Judge Kishel determined that the property was not a platted portion of the city of Afton and that the property maintained enough characteristics of rural land to permit the debtors to exempt their entire interest in their homestead under Minn. Stat. 510.02. This case has been superseded by statutory amendment.

POSTPETITION TESTAMENTARY DISTRIBUTION TO SPENDTHRIFT TRUST DOES NOT BECOME PROPERTY OF THE DEBTOR'S ESTATE
Iannacone v. Katusky (In re Katusky), 2007 WL 2248049, (Bank. D. Minn. 8/6/07) (O'Brien, J.)

The debtor was a beneficiary of his mother's inter vivos trust, which provided that upon the mother's death, the trust would distribute all of its remaining property to her children in equal shares. The trust contained a spendthrift provision which restricted alienation. The debtor's mother died within 180 days after the debtor filed for bankruptcy, and her will transferred some of her property to the trust. The debtor did not receive a testamentary bequest. Judge O'Brien ruled that postpetition transfers received though inter vivos trusts are not within the scope of 11 U.S.C. § 541(a)(5)(A). Judge O'Brien also ruled that the debtor's contingent beneficial interest in the trust was excluded from the bankruptcy estate by virtue of 11 U.S.C. § 541(c)(2) which provides that restrictions of transfers of beneficial interests of the debtor in a trust are enforceable in bankruptcy proceedings.

INCARCERATION IS NOT AN EXCUSE FOR FAILURE TO OBTAIN PREPETITION FINANCIAL COUNSELING In re Rendler, 368 B.R. 1 (Bank. D. Minn. 5/10/07) (Kishel, C.J.)

Judge Kishel denied the debtor's request to waive financial counseling and debtor education requirements due to exigent circumstances. The debtor was incarcerated and could not receive counseling either via phone or internet. Granting him an exemption, which results in a 30-day extension of time to complete the counseling requirement, would be useless because the debtor would be unable to receive counseling in that time period. The statute provides absolution of the requirement only if the debtor is mentally incapacitated, physically disabled, or on active duty in a military combat zone. As the debtor is in none of these categories, he cannot receive a full absolution of the counseling requirement and his case must be dismissed.

DETERMINATION OF HOUSEHOLD SIZE INCLUDES EVERYONE OCCUPYING A HOUSING UNIT
In re Ellringer, 2007 WL 1976750, (Bank. D. Minn. 6/20/07) (Kressel, J.)

The U.S. Trustee brought a motion to dismiss the debtor's chapter 7 case under 707(b) because the debtor had above median income for a household of one and disposable income sufficient to fund a plan. Using the Census Bureau's definition of "household" which includes all of the people that occupy a housing unit, Judge Kressel ruled that the debtor resided in a household of two at the time she filed her petition. The debtor did not need to include her partner's income in her calculation of current monthly income because her partner's income was not used for the support of the debtor or the debtor's dependents. The debtor's income alone was below the median income for a household of two in Minnesota, and thus the U.S. Trustee was barred from bringing a motion. Even if the debtor had above median income, the presumption of abuse would not have arisen because the debtor was entitled to deduct both the mortgage on her homestead and the mortgage on her investment property that had undergone a foreclosure sale subsequent to the debtor's bankruptcy petition. Judge Kressel ruled that 707(b)(2)(A)(iii) permits the debtor to deduct secured payments due in the 60 months following the date of the petition regardless of whether the debtor intends to surrender the secured property post-petition.

UNITED STATES TRUSTEE'S MOTION TO DISMISS DENIED BASED ON HIS FAILURE TO COMPLY WITH THE STATUTE In re Robertson, 2007 WL 1977154, (Bank. D. Minn. 7/3/07) (Kishel, C.J.)

Judge Kishel denied the U.S. Trustee's motion to dismiss the debtor's case pursuant to § 707(b) because the trustee failed to file a statement as to "whether the debtors' case would be presumed to be an abuse under 707(b)" as required under § 704(b)(1)(A). The U.S. Trustee had filed a statement which indicated that because the debtor had not filed all of the required means testing documents, the U.S. Trustee was unable to make a determination as to whether the debtor's case is presumed abusive under section 707(b). However, Judge Kishel found that this did not meet the requirement under § 707(b) because it was not a determination of whether the debtor's case was abusive. Because the statute does not provide for a "placeholder" determination, the U.S. Trustee could not bring a motion to dismiss under 707(b).

REPEAT FILER FAILS TO OBTAIN AN EXTENSION OF THE AUTOMATIC STAY Novack v. Wurst (in re Novack), 2007 WL 2060515, (D. Minn. 7/16/07) (Montgomery, J.)

Judge Montgomery affirmed orders of the bankruptcy court which denied the debtor's expedited motion to extend the automatic stay, granted the creditor's motion for confirmation of relief from the automatic stay, and denied the debtor's subsequent motion for reconsideration. The automatic stay terminated after 30 days in the debtor's case because the debtor had filed another bankruptcy case pending and dismissed within the preceding year. The debtor failed to serve all of his creditors with notice of his motion and provided only 2 days notice to the creditors which he did serve. Judge Montgomery ruled that Judge Dreher did not abuse her discretion by denying the debtor's motion to extend the automatic stay based on deficient notice and found no reason why the debtor should have been granted relief on an expedited basis. Judge Montgomery also held that 11 U.S.C. § 362(c)(3)(A), which terminates the automatic stay after 30 days for debtors who have had a case pending and dismissed within the past year, applied to the debtor's case, and therefore the bankruptcy court was justified in granting the creditor's motion of confirmation of termination of the automatic stay.

CONSTRUCTIVE TRUST AND DAMAGES UPHELD FOR PRINCIPALS' BREACH OF FIDUCIARY DUTIES Lange v. Schropp (In re Brook Valley VII, J.V.), 2007 WL 2230065 (8th Cir. (Neb.) 8/6/07) (Colloton, J.)

The Eighth Circuit Court of Appeals affirms the lower court holdings that debtors' principals breached fiduciary duties in the transfer of real estate, and that later sale proceeds were subject to a constructive trust. The court also affirms the BAP's increase in damages awarded against the principals. Several debtor real estate entities were controlled by two principals. Early in the Chapter 11 cases, the debtors consented to foreclosure against property and, over a creditor's objection, the bankruptcy court approved the foreclosure sale process. The debtors' principals arranged for a company they controlled to purchase at the foreclosure sale for a price less than recent appraisals - in part making an unauthorized "credit bid" - and later sold the property at a significant profit. They did not disclose their control of the buyer and later denied it in court documents. With assets gone, the cases were converted to Chapter 7 and the trustee brought an action against the principals alleging breach of fiduciary duty and requesting a constructive trust and other damages. The bankruptcy court found that the principals breached their fiduciary duties and imposed a constructive trust on the proceeds of the later re-sale of the property. The court also found that the estate was damaged in the amount of the "credit bid" and of the net cash flow from the property prior to foreclosure. However, the bankruptcy court excused the principals from paying these damages if they complied with the constructive trust. On appeal, the BAP affirmed and also awarded the trustee the additional damages, finding that the bankruptcy court clearly erred in suspending those damages.

The Eighth Circuit affirms the BAP, rejecting arguments that relief from stay for foreclosure divested the debtors of any interest in the property and that the court-approved foreclosure sale was conclusive as to property value. The court notes that the validity of the foreclosure sale was not under attack; the issue was breach of fiduciary duty and the principals' consenting to the sale and securing financing for their own benefit rather than for the debtors and creditors. The estate retains a property interest after stay relief is granted and until the foreclosure sale is complete. By secretly bidding at the foreclosure sale, the principals breached fiduciary duties of loyalty in this particular case, although the court declined to adopt a rule that insider participation in a sale is per se a breach. The court then ruled that creation of the constructive trust in the later re-sale proceeds was a proper remedy, rejecting the argument that the buyer is entitled to the increase in value during the three years between the foreclosure purchase and the later sale. The principals breached their duties to the debtors by orchestrating the foreclosure, when the debtors and creditors could have benefited from the estate holding the property to reorganize. Finally, the court concludes that the BAP did not abuse its discretion in enforcing the other two elements of damage. The unauthorized "credit bid" diminished the estate, and the bankruptcy court gave insufficient reason for declining to award the net cash flow amount as additional damages.

WHILE THE DEBTOR'S HOME WAS DESTROYED BY ARSON, THE DEBTOR DID NOT KNOW OF THE ARSON AT THE TIME AND DID NOT COMMIT FRAUD WHEN SHE MADE AN INSURANCE CLAIM
Minnesota Fair Plan v. Neumann (In re Neumann), Adv. 05-5005 (Bankr. D. Minn. 8/17/07) (Kishel, C.J.)

After a hotly contested trial at which the debtor denied that her home had been destroyed by arson, Judge Kishel found that her home was, in fact, destroyed by arson, but that she was not involved in the act of arson nor was she aware that it had occurred. As a result, when she made her insurance claim, she did not knowingly make any false statements and therefore she did not perpetrate a fraud on the insurance company. As a result, any claim by the insurance company against her was not excepted from her discharge.

TERMINATION OF PENSION PLANS AFFIRMED AS TERMINATION WAS A CONDITION FOR NECESSARY EXIT FINANCING Pension Benefit Guaranty Corporation v. Falcon Products, Inc. (In re Falcon Products, Inc.), 2007 WL 2317355 (8th Cir. 8/15/2007) (Shepherd, J.)

The Eighth Circuit Court of Appeals affirms the district court ruling and holds that the debtors could terminate their three pension plans under the ERISA reorganization test under 29 U.S.C. § 1341(c)(2)(B)(ii)(I)-(IV). The bankruptcy court and the district court ruled that the pension plans as an aggregate could be terminated because the debtors could not afford to pay the required pension plan contributions and also continue their business after reorganization. The PBGC asserted that ERISA required that the debtors' three pension plans be evaluated on a plan-by-plan basis rather than in the aggregate. The Eighth Circuit holds that the pension plans could be terminated whether analyzed in the aggregate or on a plan-by-plan basis because the exit financing in the case was conditioned on termination of the pension plans and the business could not continue after reorganization without the exit financing. Without the exit financing, the debtors would be forced to liquidate and the pension plans would have been terminated anyway. The Eighth Circuit does not reach a decision on whether ERISA mandates a plan-by-plan or aggregate approach under the reorganization test for distressed termination of a pension plan as the Third Circuit recently did in In re Kaiser Aluminum Corp., 456 F.3d 328 (3rd Cir. 2006) (determining that aggregate approach was appropriate under reorganization test).

APPROVAL OF CONTESTED SETTLEMENT MUST BE SUPPORTED BY EVIDENCE AND FINDINGS
Velde v. First International Bank & Trust, 2007 WL 1650581 (8th Cir. BAP (Minn.) 6/8/07) (McDonald, J.)

The Eighth Circuit BAP reverses the bankruptcy court's approval of a settlement that was contested by a creditor. The trustee proposed to compromise a large preference claim against a creditor and another creditor objected. At the hearing, the attorneys made their arguments, but the court did not hear testimony, although the objecting creditor stated that it had a witness to testify against the compromise. The court ruled that the settlement fell within the range of reasonableness, but did not make findings of fact or conclusions of law regarding the settlement factors set out in In re Flight Transp. Corp., 730 F.2d 1128 (8th Cir. 1984). Reversing the order, the BAP notes that the trustee had the burden of proof by a preponderance of the evidence, but the parties did not present evidence and the court did not make findings or conclusions based on the standards applicable to settlements.

CONTRACT FOR DEED DEFAULT CURE NEED NOT BE MADE WITH CERTIFIED FUNDS In re Edina Development Corp., 2007 WL 1748393, (Bank. D. Minn. 6/8/07) (Kishel, C.J.)

The debtor was in default of a contract for deed in which it was the purchaser. The debtor attempted to cure the default by tendering payment via counter check of the past due amount. However, the vendor refused the payment because 1) the payment did not include $6.70 of property taxes that came due after the notice of default but before the expiration of the cure period, and 2) the payment was not tendered by cashier's check or certified funds. Judge Kishel ruled that neither the deficiency in the payment nor the fact that the payment was made with uncertified funds rendered the cure ineffective. Minnesota law only requires that the remediation of all of the events of default identified in the notice of default plus the making of all payments owed to the seller. Because the $6.70 was not noted in the notice of default and was not owed to the seller, it was not required to cure the default. In addition, Minnesota law does not require cure payments to be made with certified funds. Thus, the debtor's counter check was an acceptable method to proffer a cure amount.

ANNOUNCEMENT FROM THE UNITED STATES TRUSTEE:

NOTICE OF INTEREST ASSESSMENT

Pursuant to 31 U.S.C. §3717, the United States Trustee Program will begin assessing interest on unpaid Chapter 11 quarterly fees charged in accordance with 28 U.S.C. §1930(a) effective October 1, 2007. Interest assessed on past due amounts will first appear on their October 2007 statement. The interest rate assessed is the rate in effect as determined by the Treasury Department at the time their account becomes past due.

If payment of the full principal amount past due is received within thirty (30) days of the date of the notice of initial interest assessment, the interest assessed will be waived.

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