The 34th Annual Bankruptcy Year in Review Seminar

Co-Sponsored by the Bankruptcy Law Section

Friday, March 1, 2019

NEW MEXICO
STATE BAR FOUNDATION
CENTER FOR LEGAL EDUCATION

Agenda and CLE Information

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The issues discussed herein are intended as illustrative of the types of issues which can arise in the course of representation and are not intended to address, nor do they address the broad range of substantive issues which could potentially arise in the scope of such representation.

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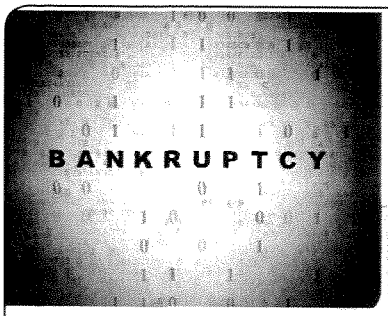

34th Annual Bankruptcy Year in Review Seminar

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Friday, March 1, 2019 • 8:30 a.m. – 5:00 p.m.
State Bar Center, Albuquerque

$99 Non-members and those not seeking CLE credit
$278 Co-sponsoring section members, government and legal services attorneys, Young Lawyers Division and Paralegal Division members
$309 Standard/Webcast fee

Registration and payment for the program must be received prior to the program date. A $20 late fee will be incurred when registering the day of the program. This fee applies to live registrations only and does not apply to live webcasts.

Co-sponsor: Bankruptcy Law Section

The seminar focuses on developments in case law on bankruptcy issues in 2018, both nationally and locally, with special emphasis on decisions by the U.S. Supreme Court, 10th Circuit Court of Appeals, 10th Circuit B.A.P. and U.S. Bankruptcy Court for the District of New Mexico. Also included are presentations by the Bankruptcy Judges for the District of New Mexico, representatives of the Office of the U.S. Trustee for the District of New Mexico, the Clerk of Court, and an ethics or professionalism presentation.

8 a.m.	Registration and Refreshments
8:30 a.m.	**Annual Bankruptcy Case Review** *James A. Askew, Askew & Mazel LLC; Michael K. Daniels, Michael K Daniels Esq; Paul M. Fish, Modrall Sperling Roehl Harris & Sisk PA; and Thomas D. Walker, Walker & Associates PC*
10 a.m.	Break
10:15 a.m.	**Annual Bankruptcy Case Review (continued)**
11 a.m.	**Discussion from the Bench** *Hon. Robert H. Jacobvitz, U.S. Bankruptcy Court; and Hon. David T. Thuma, U.S. Bankruptcy Court*
11:30 a.m.	**Presentation by Clerk of the Bankruptcy Court** *Lana Merewether, U.S. Bankruptcy Court*
Noon	Lunch (provided at the State Bar Center) Bankruptcy Section Annual Meeting
1 p.m.	**Presentation by the Office of the United States Trustee** *Ilene J. Lashinsky, Office of the U.S. Trustee; Alice Nystel Page, Office of the U.S. Trustee; and Leonard Martinez-Metzgar, Office of the U.S. Trustee*
1:30 p.m.	**Annual National Review** *Jeffrey H. Davidson, Pachulski Stang Ziehl & Jones*
2:45 p.m.	Break
3 p.m.	**Chapter 13 Case Review and Update on Chapter 13 Issues** *Tiffany M. Cornejo, Chapter 13 Standing Trustee; and Gerald R. Velarde, Law Office of Gerald R Velarde PC*
4 p.m.	**Ethics and Professionalism** *William D. Slease, Disciplinary Board of the New Mexico Supreme Court; Leslie D. Maxwell, Maxwell Law P.C.*
5 p.m.	Adjournment and reception

Presenter Biographies

Presenter Biographies

James Askew has developed a reputation as an aggressive and practical bankruptcy attorney. He brings 32 years of experience representing secured creditors, business debtors, creditor committees, trustees and other parties in interest in bankruptcy proceedings and out-of-court workouts. Additionally, he has an active commercial and business ligation practice. Askew served as a law clerk to the Hon. Stewart Rose, U.S. Bankruptcy Judge, District of New Mexico, from 1987-1989. Askew is listed in *Best Lawyers in America* for his expertise in Bankruptcy and Creditor-Debtor Rights Law. Askew has achieved the highest Martindale-Hubbell rating.

Michael K. Daniels is a sole practitioner whose practice is primarily limited to representing debtors and creditors in chapter 7, 11 and 13 bankruptcy cases. Before forming his own practice in 1991, Daniels was employed by Behles & Davis, P.C. for almost five years. During law school, Daniels clerked at several law firms and performed a judicial externship during the summer of 1984 at the New Mexico Supreme Court for Justice Harry Stowers. Before law school, Daniels was employed at McKercher Rehabilitation Center, a sheltered workshop for handicapped adults for five years after college. Daniels is a member of the New Mexico Bar, the Federal Bar for the State of New Mexico, and the Tenth Circuit Bar. Daniels was admitted to the Supreme Court bar, although only to defend an application for certiorari.

Paul M. Fish is a shareholder of the Albuquerque law firm of Modrall Sperling Roehl Harris & Sisk, P.A., where his practice focuses on commercial litigation, including creditor representation in commercial bankruptcy proceedings. He received a B.A. degree from Drake University and his J.D. degree from Harvard Law School. Fish is a member of the State Bar of New Mexico (past chairman, Bankruptcy Law Section), is a fellow of the American College of Bankruptcy, has been named as a "*SuperLawyer*" for the past several years, and has been listed in every edition of the *Best Lawyers in America*. Fish has several times served as a member of the Judicial Selection Panel for the 10th Circuit Court of Appeals for the Selection of a new Bankruptcy Judge. He is a frequent speaker on creditor's rights in bankruptcy law.

Thomas D. Walker is a shareholder in the Albuquerque law firm of Walker & Associates, P.C., where he concentrates his practice in the areas of bankruptcy law, commercial litigation and real estate law. He regularly represents businesses, individuals, committees and trustees in bankruptcy cases and represents parties in business litigation and transactions, foreclosure actions, workout negotiations, real estate and lease negotiations and other commercial matters. Walker speaks frequently on bankruptcy and other business litigation topics.

He received an undergraduate degree in economics from Tulane University in 1981, attended the Institute of Political and Economic Studies in London, England, and received his J.D. degree from the University of New Mexico School of Law in 1985. He has been a member of the State

Bar of New Mexico since 1985 and is a member of the United States District Court for the District of New Mexico and the Tenth Circuit Court of Appeals.

Walker is a past chair of the Bankruptcy Law Section of the State Bar of New Mexico, and has served on its Board of Directors since 1990. Walker is "AV" peer-review rated in the Martindale Hubbell Law Directory, is listed in *Best Lawyers in America* in the areas of Bankruptcy and Creditor-Debtor Rights, was awarded Best Lawyers "Lawyer of the Year" in 2015 in the areas of Bankruptcy and Creditor-Debtor Rights/Insolvency and Reorganization Law for Albuquerque, and is recognized as a SuperLawyer in the areas of Bankruptcy and Creditor-Debtor Rights in the SuperLawyers national corporate counsel edition and the Southwest edition. Walker & Associates, P.C. is recognized as one of the "Best Law Firms" in New Mexico as published in U. S. News and World Report, and as among the "Best Law Firms" in Albuquerque in the *2018 Edition Best Lawyers* in the areas of Bankruptcy and Creditor-Debtor Rights/Insolvency and Reorganization Law for Albuquerque.

Hon. Robert H. Jacobvitz is Chief Judge of the U. S. Bankruptcy Court for the District of New Mexico and a judge on the Tenth Circuit Bankruptcy Appellate Panel. Judge Jacobvitz earned his J.D. from the University of Iowa College Of Law in 1979, Order of the Coif; and his B.A. in Philosophy from the University of Colorado in 1975, Phi Beta Kappa and with High Distinctions. He is the Tenth Circuit representative on the Board of Governors of the National Conference of Bankruptcy Judges and is chair of its Technology Committee. In 2008, he was inducted as a Fellow in the American College of Bankruptcy. In 2004 and 2010 he taught bankruptcy law courses at the University Of New Mexico School Of Law as an Adjunct Professor. Before his appointment to the bench on Aug. 10, 2009, he was in private practice in Albuquerque, o for about 30 years, including 16 years as a partner of Jacobvitz, Thuma & Walker P.C. He practiced mainly in the areas of bankruptcy law, out-of-court workouts, business transactions, real estate matters, and commercial litigation. He served as lead counsel for numerous debtors in possession, as well as for creditors and creditor committees.

Hon. David T. Thuma is a U.S. Bankruptcy Judge for the District of New Mexico. He was sworn in on Aug. 14, 2012. Judge Thuma grew up in Indianapolis, Indiana. He received his undergraduate degree from the University of Chicago in 1980 and his law degree from Duke University in 1984. Judge Thuma practiced law in a large Indianapolis firm for five years before moving to New Mexico. He practiced law in New Mexico between 1989-2012, concentrating in bankruptcy and commercial litigation.

Judge Thuma lives in Albuquerque. He is married to Rebecca Thuma; they have one daughter, Kate Thuma, born in 2003. In his free time Judge Thuma enjoys reading, bird watching, cars and ferrying Kate from one activity to the next.

Lana Merewether is the clerk of court for the U.S. Bankruptcy Court in the District of New Mexico. Merewether was appointed to the position in Oct. 2017. She has been with the federaljudiciary since July 1995.

Merewetherhas served in a variety of positions in the court including court automation trainer, serving ten years as the court's information technology manager and spending five years in the chief deputy role.

Alice Nystel Page is employed as one of the trial counsel for the Office of the U.S. Trustee in Albuquerque. Immediately prior to rejoining the UST program in June, 2004, she was employed for four and a half years as one of the corporate counsel for Sun Healthcare Group, Inc. in Albuquerque, Nystel Page worked for Rodey, Dickason, Sloan, Akin & Robb in Albuquerque from 1995-2000, was a Senior Attorney/Advisor and Assistant U.S. Trustee from 1991-1995 for the Office of the U.S. Trustee in Regions 6 and 16 (Dallas, San Bernardino, and Los Angeles), and was in private practice in Dallas from 1983-1991, specializing in bankruptcy practice. She earned her J.D. degree from Texas Tech University in 1983 and her B.A. degree in English from Texas Tech University in 1979.. Nystel Page was the Section chair for the Bankruptcy Law Section for 2005 and the editor of the Bankruptcy Law Section newsletter from 1996-2004,was a member of the Bankruptcy Law Section board of directors from 1998-2007 and 2010-13 and was a member of the Local Rules Advisory Committee from 1996-1998. She has been a speaker at the Section's Bankruptcy Year in Review programs, the State Bar Annual Meeting program on bankruptcy legislation in 2001, and the 2007 State Bar Annual Meeting program on bankruptcy and the elderly. She has also been a speaker for the U.S. Trustee program at the National Advocacy Center. She is a member of the State Bar of Texas as well as the State Bar of New Mexico.

Leonard Martinez-Metzgar is a trial attorney with the United States Trustee Office. He has a B.S. degree in Psychology; a MA degree in Psychology; a Master's in Business Administration; and a J.D. degree received from the University of New Mexico in 1982. Prior to joining the UST program he was a criminal attorney for five years. Over the last three decades, he has presented at various bankruptcy seminars and at the DOJ Training Center in Columbia, South Carolina.

Ilene Lashinsky is currently serving as the United States Trustee for Region 14 (District of Arizona) since November 18, 2002. Between January 2, 2004 and February 2008, she also served as the Interim United States Trustee for Region 18 (Washington, Oregon, Montana, Idaho and Alaska). Lashinsky became the United States Trustee for Region 20 (Kansas, Oklahoma and New Mexico) for an interim period, effective April 30, 2018.

Immediately before her appointment as Region 14 U.S. Trustee, Lashinsky was of counsel to the Scottsdale, Arizona firm of Hymson & Goldstein, P.C. where her practice focused on

representing creditors and debtors in complex commercial bankruptcy matters and commercial litigation. For the previous 17 years, she was a partner at the bankruptcy law firm of Davis & Lowe, P.C. in Phoenix. During a leave from Davis & Lowe, between June 1998 and June 1999, Lashinsky served as resident bankruptcy advisor to the CFED- USAID Macedonia Commercial Law Project, assisting in workouts of major financially distressed Macedonian businesses and advising ministry representatives regarding the government's role in the transition to a free market economy.

Before joining Davis & Lowe, P.C., she practiced commercial and bankruptcy law with Leslie L. Miller, P.C. and with Streich Lang. As the first Director of Continuing Legal Education of the State Bar of Arizona, Lashinsky helped design and develop legal education curricula and material.

She is also an adjunct faculty member for Arizona State University's Melikian Center for Russian and East European Studies. Lashinsky received her law degree cum laude in 1972 from Arizona State University College of Law, Tempe, Arizona and her undergraduate degree in 1969, also from Arizona State University.

Jeffrey H. Davidson is a partner in the Los Angeles office of Pachulski Stang Ziehl & Jones LLP and has a national practice in bankruptcy reorganizations and out-of-court restructurings. He has frequently served as lead counsel representing both public and private business entities in a variety of industries. In addition, he commonly represents hedge funds and other significant holders of securities in connection with complex chapter 11 reorganizations and workouts, and has handled many insolvency-related sales and acquisitions. He is a fellow of the American College of Bankruptcy and is a member of its Board of Regents, chair of its Ninth Circuit Council, a past member of its Nominating Committee, and immediate past chair of its Ninth Circuit Educational Programs Committee. Davidson was named a "Lawyer of the Year" for Bankruptcy and Creditor Debtor Rights / Insolvency and Reorganization Law in the 20th edition of *Best Lawyers in America*, and again for Litigation - Bankruptcy in the 21st edition. He has been listed by *the Best Lawyers in America* every year since 2001; by Chambers USA in the practice area of Bankruptcy / Restructuring; by Southern California Superlawyers in the practice area of Bankruptcy & Creditor/Debtor Rights every year since 2004; and by Who's Who in America; and Who's Who in American Law. Davidson has published and lectured on a variety of bankruptcy-related topics. For several years he has presented annual bankruptcy update programs for the Financial Lawyers Conference, for the Bankruptcy Section of the State Bar of New Mexico, and previously for the Business Law Section of the State Bar of California. He has also presented several educational programs for ALI-ABA, ALI CLE, American Bankruptcy Institute, Association of Insolvency and Restructuring Advisors, California Continuing Education of the Bar, Renaissance American Management, Beard Group, and Turnaround Management Association.

Davidson received his J.D. degree, cum laude, from Harvard Law School and his B.A., cum laude, from Harvard College, where he was a member of Phi Beta Kappa.

Tiffany Cornejo, Chapter 13 Standing Trustee of New Mexico received her Bachelor of Science in Journalism (B.S.J.) degree at the University of Kansas, Lawrence, Kansas in 2002 and then remained there to obtain her Juris Doctorate (J.D.) in 2005. Cornejo was awarded the Dean's Scholarship Award and Bremeyer Scholarship Award. During law school Cornejo was a voting member of the Admission's Committee for the 2005-2006 incoming class.

While in law school Cornejo worked as a law clerk for Cloon Legal Services (Baldwin, Kansas), a bankruptcy firm practicing solely in consumer bankruptcy law. From there Cornejo was asked by one of the Partners to aid in the start-up of his own firm; Cornejo accepted and continued her work as a law clerk for The Law Office of Garret & Coons (Lawrence, Kansas) practicing primarily consumer bankruptcy law.

After graduating law school Cornejo worked as an Associate for Shapiro & Mock (Overland Park, Kansas) representing mortgage companies in the areas of foreclosures, bankruptcy, creditors' rights, commercial litigation, collections, replevins, evictions, and landlord–tenant law, all in both Kansas and Missouri.

From there, Cornejo moved to Saint Louis, Missouri to accept her current position as Senior Staff Attorney for Russell C. Simon, Standing Chapter 13 Trustee in the Southern District of Illinois where she not only represents the Trustee and trust, but supervises four paralegals, two mortgage administrators and a legal clerk. Cornejo was in this position for nine years.

On December 1, 2017, Cornejo was appointed as the Chapter 13 Trustee in New Mexico.

Cornejo is admitted to practice in the Federal District Courts of Kansas, Western Missouri and Southern District of Illinois, and in the states of Kansas, Missouri and Illinois.

Gerald "Jerry" Velarde is a sole practitioner in Albuquerque. His practice mainly involves consumer and small business bankruptcy or workouts. Velarde serves as on the Chapter 13 Plan Revision Committee appointed by the Bankruptcy Court. He serves as a board member for the Bankruptcy section of the State Bar and is a past chairperson of the section. From 1980-1991, Velarde practiced bankruptcy law in Dallas, Texas. Since moving back to New Mexico in 1991, he has practiced bankruptcy law mainly as a sole or small-firm practitioner. He earned his B.S in Chemical Engineering and J.D. degrees from the University of New Mexico. Velarde has been a speaker at several Annual Bankruptcy Year in Review seminars presented by the Bankruptcy Law Section of the State Bar of New Mexico and other seminars dealing with consumer bankruptcy matters.

Velarde has prepared numerous papers which accompany his presentations. He has also co-authored an article with Judge James Starzynski entitled: When Worlds Collide Bankruptcy and Domestic Relations: When to go to (Bankruptcy) Court and When Not to.

William D. Slease is chief disciplinary counsel for the New Mexico Supreme Court Disciplinary Board. In addition to his duties as chief disciplinary counsel, he serves as an adjunct professor at the University of New Mexico School of Law where he had taught ethics, trial practice skills and employment law. He also chairs the Supreme Court of the State of New Mexico's Proactive Attorney Regulation Committee, the Court's Lawyer's Succession and Transition Committee and serves on the State Bar of New Mexico Commission on Professionalism which is responsible for operating and administering the "Bridge the Gap: Transitioning Into the Profession Program" for new Lawyers in New Mexico. He is a member and the 2017-18 immediate past president of the National Organization of Bar Counsel.

Leslie D. Maxwell was born and raised in Albuquerque, owns a thriving solo practice representing debtors and small creditors primarily in consumer bankruptcies at Maxwell Law, P.C. She received her B.A. in Anthropology from Emory University in 2003 and her Juris Doctor from the University of New Mexico School of Law in 2006. At UNM, she was a judicial extern for the Hon. James S. Starzynski, from Bankruptcy Judge for the District of New Mexico. Expect for a brief stint in litigation defense litigation, Maxwell has practiced primarily in bankruptcy law since 2006.

Maxwell is the chair of the board of directors of the Bankruptcy Section of the State Bar on which she has served since 2010. She served on the Board of Directors of the New Mexico Chapter of the Federal Bar Association and is a member of the H. Vearle Payne Inn of Court. In 2006, she won the American Bankruptcy Institute Medal of Excellence in Bankruptcy and published the article, "Being a Professional Responsible Debt Relief Agent: How Do You Respect a Law That Can Get You Disbarred?" in the October 2006 issue of the Norton Bankruptcy Law Adviser.

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SUMMARY NUMBER: 1
MKD

KEY CODE SECTION(S): n/a
KEY TOPIC(S): Abstention & Remand

COURT and JUDGE: US Bankruptcy Court, NM, David T. Thuma
CASE NAME and CITE: Sky Country Estates POA v. Sky Country Estates, LLC
CASE NUMBER: 7-17-11617 TR; Adv. No. 17-1069; Docket No. 32
DATE DECIDED: August 10, 2018

NOTEWORTHY ISSUE:

Does mandatory or permissive abstention justify a remand to state district court?

HOLDING: No; Judge Thuma will hear the dispute.

Mandatory abstention requires:

1. A timely motion for abstention.
2. The matter must be based on a state law claim or cause of action.
3. An action was commenced in state court.
4. The action can be timely adjudicated in state court.
5. The claim is within the Court's non-core jurisdiction.
6. There is no independent source of federal jurisdiction outside bankruptcy.

The first three factors are clearly present; timeliness concerned the Court. The state court case had been pending for five years and included a jury demand; additionally the original trial judge became a federal magistrate, so a new judge was assigned. The dispute seems to be a core matter (POA filed a proof of claim); to the extent the fraud claim seeks to recover fraudulent conveyances or impose liability through veil piercing that may also be core, as the creditors lose their standing to bring these causes of action to the Trustee in bankruptcy when the case is filed. The requirements for mandatory abstention are not met.

Permissive abstention and remand factors include:

1. The effect abstention would have on bankruptcy estate administration.
2. The extent to which state law issues predominate.
3. The difficulty or unsettled nature of applicable state law.
4. The presence of a related proceeding in state court.
5. The federal jurisdictional basis of the proceeding.
6. The degree of relatedness of the proceeding to the main bankruptcy case.
7. The substance of the asserted core proceeding.
8. The feasibility of severing the state law claims.
9. The burden the proceeding places on the bankruptcy court's docket.
10. The likelihood that proceeding in bankruptcy court involves forum shopping.
11. The existence of a right to jury trial.
12. Presence of nondebtor parties in the proceeding.

Judge Thuma in a nice table analyzes the factors; the only factor favoring remand was the predominance of state law issues in the dispute.

FACTS:

Sky Country Estates, LLC, is a NM LLC formed in January of 1998. Sky Country owned and developed a residential subdivision in Otero County, NM called Sky Country Estates, containing 67 lots ranging from 2.5 to 27.8 acres. Debtor signed a Disclosure Statement for the subdivision in 1997. Between 1997 and 2006 Debtor sold all but 4 of the lots. By 2014 eight lots had been developed with single family houses and had full time occupants; fourteen lots were occupied part time. Debtor built a water system; some owners call it inadequate.

June 23, 2009 some lot owners formed Sky Country Estates Property Owners Association ("POA"), a NM nonprofit corproation. In 2012 the POA sued Debtor in NM 12th Judicial District Court, for breach of contract, unjust enrichment and fraud, all related to the water supply dispute. Summary judgment motions were exchanged and are pending. Debtor filed Chapter 7 on June 23, 2017. On September 19, 2017 some members removed the state court action to this court; POA timely moved for remand. POA filed a $2.5 million claim (cost of repairing the water system). The estate owns 4 vacant lots, the water system, some cash and possibly the fraud claim.

SUMMARY NUMBER: 2

PMF

KEY CODE SECTION(S): 305(a); 28 U.S.C. § 1334(c)(2)
KEY TOPIC(S): Dismissal, Abstention

COURT and JUDGE: United States Bankruptcy Court, D. New Mexico, Judge Thuma

CASE NAME and CITE: *In re: Sky Country Estates, LLC*

CASE NUMBER and DOCKET NUMBER: 17-11618-t17 Doc 47

DATE DECIDED: August 13, 2018

NOTEWORTHY ISSUE: Should an allegedly two party dispute Chapter 7 be dismissed or should the bankruptcy court abstain.

HOLDING: The motion to dismiss was denied. The case was not a two party dispute. It involved a number of parties. The ruling stated that dismissal under §305(a) was an unusual remedy, and the movant had the burden of proof. Each case must be decided on its own merits, and dismissal must benefit both the debtor and creditor. J. Thuma listed 18 factors. He decided that the factors weighed against abstention, particularly because abstention was not in the interests of the debtor.

The dismissal was also sought under the theory that the bankruptcy was two party dispute. The court said that the cases cited related to dismissal under § 1112(b) or relief from stay, not abstention. The movant also cited a bad faith filing case, which was not relevant. Finally, the court identified all the interested parties and stated the case was not merely a two party dispute.

Abstention under 28 U.S.C. § 1334(c)(2) was also not warranted because it only applies to adversary proceedings, not bankruptcy cases.

FACTS: Debtor, an LLC with 10 members, developed a residential subdivision. The residents formed a home owners association which sued the debtor and its members for problems relating to water and other matters. The LLC filed and a Chapter 7 trustee was appointed. Some of the members of the LLC removed the case, and the homeowners association moved to dismiss the bankruptcy or have the court abstain.

SUMMARY NUMBER: 3

KEY CODE SECTION(S): 28 U.S.C. §1334(c); 28 U.S.C. § 1452(b)

PMF

KEY TOPIC(S): Abstention

COURT and JUDGE: United States Bankruptcy Court, D. New Mexico. Judge Thuma

CASE NAME and CITE: *In Re Kearney; Kearney v. Abruzzo*

CASE NUMBER and DOCKET NUMBER: Adversary No. 18-1068, Doc. 17

DATE DECIDED: October 11, 2018

NOTEWORTHY ISSUE: Should the court abstain from a removed proceeding and remand to state court.

HOLDING: The court remanded under both mandatory and permissive abstention grounds.

(1) The court ruled that abstention was mandatory. It ruled as follows:

1. The motion for abstention was timely, being filed 3 days after the action was removed.
2. The action is based on state law.
3. The action was commenced in state court.
4. The action can be timely adjudicated in state court. The court found it could, applying the following 7 factors:

    a. Calendar backlog. The state court could hear the matter promptly. Favors remand.
    b. Status of proceeding before removal. The state court had already heard weeks of trial testimony on the dispute between these parties. Favors remand.
    c. Status of the proceeding in bankruptcy court. The matter had only been referred to the bankruptcy court six days earlier. Favors remand.
    d. Complexity of the issues. The factor favors a timely adjudication. The facts in dispute are complicated, but the state court is familiar with them. Favors remand.
    e. Whether the parties consent to this Court entering judgment. The matter was so new that the Court does not know, so the factor is neutral.
    f. Whether a jury demand was filed. One was, but that would favor state court.
    g. Whether the case is a reorganization or state court. This factor, if it applies, favors timely adjudication. This does not really apply in this case.
5. The claim is not a core proceeding.

6. There is no independent source of federal jurisdiction. The case had been removed asserting such, but the district court ruled the claim "frivolous" and a "sham litigation tactic."

The court also noted that the debtor argued that the state court would commit reversible error. The record was insufficient for the court to so find.

(2) The court ruled that the court should exercise its discretion to grant permissive abstention, considering the following 12 factors:

1. The effect of abstention on the efficient administration of the estate. The state court could hear the matter promptly. Favors remand.
2. Predominance of state court issues. Totally state law, so favors remand.
3. The difficulty or unsettled nature of applicable state law. Does not favor remand. The issues are not difficult or unsettled.
4. Presence of a related proceeding in state court. Favors remand since tied to existing case.
5. Federal jurisdiction. Favors remand. District court found removal under § 1332 a "sham litigation tactic."
6. Degree of relatedness. Very related, but the issues relate to the spendthrift trust and a division of labor makes sense. Favors remand.
7. Core? No. Favors remand.
8. Feasibility of severing. Favors remand. Only state court issues.
9. Burden on bankruptcy court docket. Favors remand. State court is up to speed, bankruptcy court is not.
10. Likelihood of forum shopping. Favors remand. No question but that removal was effort to find another judge.
11. Right to a jury. Neutral. Does not appear to be a right to jury as demanded by debtor, but if so, better in state court.
12. Presence of no-debtor parties. Favors remand. Remainder beneficiaries are in the state court, even though debtor attempted to ignore them in the removal process.

Factors heavily weigh in favor of remand on permissive abstention.

(3) Remand on equitable grounds. § 1452(b) allows remand on any equitable ground. The court found based on the factors for permissive abstention that equity called for remand.

FACTS: The debtor was the income beneficiary of a spendthrift trust. The only asset in the trust was stock in a corporation in which the trustees of the trust, the debtor's former brothers-in-law were officers. The debtor sued the trustees for breach of fiduciary duty in state court. The trustees counterclaimed for the debtor's misconduct. After 4 years and two week long trials, the debtor had lost pretty much everything. He filed Chapter 11 the day before what might have been the final hearing in the case. In the bankruptcy, the UCC filed a plan that would have provided for a sale of the stock, a contribution from the principal of the trust to the estate to pay admin claims and creditors, and a release of the trustees and the corporation from future litigation. The plan was contingent on the state court determining that the trustees

were not violating their fiduciary obligations by performing the acts called for in the UCC Plan. The debtor went through enormous gymnastics to avoid the state court from hearing the issue, including appealing the stay lift order, seeking a stay of the stay lift from first the bankruptcy court and then the district court while that appeal was pending, and removal of the request of the trustees for instructions to the district court as if it was a new action and diversity existed.

The particular ruling here was the remand of that removed action.

SUMMARY NUMBER: 4 KEY CODE SECTION(S):28 U.S.C. § 158(d)(2)(A)
PMF KEY TOPIC(S): Appeals

COURT and JUDGE: United States Bankruptcy Court, D. New Mexico, Judge Jacobvitz

CASE NAME and CITE: *In re: Otero County Hospital Association, Inc., Debtor. United Tort Claimants v. Quorum Health Resources, LLC,* 584 B.R. 783 (2018)

CASE NUMBER and DOCKET NUMBER: Consolidated Misc. Adversary No. 13-00007

DATE DECIDED: April 19, 2018

NOTEWORTHY ISSUE: Whether the appeal of the bankruptcy court's decision should be directly appealed to the 10th Circuit without going first to the BAP or district court.

HOLDING: The case was certified by the bankruptcy court for direct appeal to the 10th Circuit. The court found that the liability decision should be certified because the judgment involved questions of law for which there was no controlling decision and, alternatively, the issues were maters of public importance. The court found that the fact that immediate certification would further resolution of other pending cases was not a basis for certification. The court found that certification was required to be made if any of the three bases were met, and here it was two of them. The court noted that the 10th Circuit had to agree to take the case.

FACTS: About 100 plaintiffs had sued the debtor hospital for medical malpractice, forcing the hospital to file Chapter 11. Most of the cases were removed to bankruptcy court. A plan had been confirmed and the cases were partially settled, but most remained pending against one of the defendants. The court had entered a significant liability finding in about 100 cases that had been consolidated for liability determination. After that determination was made, the court heard damages trials for four of the plaintiffs, and those rulings became final judgments. The defendant sought certification of an appeal directly to the 10th Circuit.

SUMMARY NUMBER: 5
TDW

KEY CODE SECTION(S): Rule 8022
KEY TOPIC(S): Appellate rules and procedure

COURT and JUDGE: District Court for the District of New Mexico; J. Johnson

CASE NAME and CITE: *Lankford v. Wagner (In re The Vaughan Company Realtors)*, 2018 WL 1183363 (D.N.M., 2018)

CASE NUMBER: No. 10-10759-J11; Adv. Proc. 12-1139-J; Appeal No. 1:18-cv-00037 WJ/KRS

DATE DECIDED: March 6, 2018

NOTEWORTHY ISSUE: Does Rule 60(b) apply to an effort to set aside an order of the District Court acting as a court of appeals from a Bankruptcy Court ruling?

HOLDING: No. "Fed. R. Bank. P. 8022 is the exclusive vehicle for seeking rehearing when a district court considers a bankruptcy appeal." Bankruptcy Rule 8022 "provides the sole mechanism for filing a motion for rehearing."

FACTS: Lankfords appealed a decision by the bankruptcy court. The notice of appeal was filed late. The district court issued a notice to show cause and later dismissed the appeal as untimely. Lankfords filed a motion to vacate the district court order and later filed a notice of appeal to the Tenth Circuit. The Tenth Circuit Court abated the appeal pending resolution of the post-judgment motions.

The motion to vacate was filed pursuant to Rule 60(b)(4) and (c). However, the Federal Rules of Civil Procedure do not apply in bankruptcy appeals. Bankruptcy Rule 8001 provides that "these Part VIII rules govern the procedure in a United States district court and a bankruptcy appellate panel on appeal from a judgment, order, or decree of a bankruptcy court." Rule 60(b) is inapplicable. The "only way to seek review of an order entered by a district court in its bankruptcy appellate capacity is by motion for rehearing under Bankruptcy Rule 8022 and or appeal." "The Rule 60(b) motion was a nullity when filed in district court sitting as bankruptcy appellate court."

The Court analyzed what would happen if it were to construe Lankfords' Rule 60 motion as a motion for rehearing pursuant to Fed. R. Bank. P. 8022, and concluded that there are no grounds for rehearing. The court looked at Fed. R. App. P. 40 for the standard for ruling on a petition for rehearing pursuant to Fed. R. Bank. P. 8022. Appellate Rule 40 provides in part: "The petition must state with particularity each point of law or fact that the petitioner believes the court has overlooked or misapprehended...." Here, the sole issue is whether the Notice of Appeal was timely filed in bankruptcy court. Lankfords offered the same argument they had made in response to the order to show cause, and did not provide any additional facts or reasons why the Notice of Appeal was in fact timely.

SUMMARY NUMBER: 6
JAA

KEY CODE SECTION(S): Bankr. Rule 8007(e)(1)
KEY TOPIC(S): Appeals

COURT:	USDC-NM
JUDGE:	Gregory J. Fouratt
CASE NAME:	Kearney Stay Lift Appeal No. 2 Kearney v. Abruzzo
CITE:	2018 WL 5112909
CASE NUMBER:	Civ. No. 18-888 JB/GJF
DATE DECIDED:	October 19, 2018

NOTEWORTHY ISSUE: In addition to the traditional standards for a stay pending appeal discussed in the *Kearney Stay Lift Appeal No. 1* case review, the Debtor also asserted that the Bankruptcy Court stay lift orders must be stayed as the appeal divested the Bankruptcy Court of all further jurisdiction in the bankruptcy case, especially with regard to the UCC Plan.

HOLDING: The filing of the appeal of the stay lift orders did not divest the Bankruptcy Court of jurisdiction over the rest of the Ch. 11 case. Thus, the divesture doctrine does not require a stay pending appeal.

FACTS and DISCUSSION: Debtor Kearney is the beneficiary of Trusts established by his late wife. Some of the wife's family members are the contingent remainder beneficiaries of the Trust. The Trust owns shares of stock in Alvarado Realty Co. (ARCO). The ARCO shares paid dividends to the Trust of around $800,000 per year, all of which was paid out to the Debtor. The Debtor believed he was being cheated and that $800,000 a year was an insufficient distribution. He commenced state court litigation against the Trustees of the Trust and others. Counterclaims were filed. The State Court found that it was the Debtor who had breached his fiduciary duties and that good cause existed to modify the Trust. Before a final judgment was entered or any modifications could be made, Debtor filed a Ch. 11 bankruptcy. The Unsecured Creditors Committee filed a plan. The UCC plan requires modification of the trust in three ways:

1. ARCO will pay $12,571,799 to Debtor's Trust in exchange for all ARCO stock held by the Trusts.
2. The Trustees deliver a $3 million trust payment to Debtor, which would be delivered to creditors, thus funding the plan.
3. Kearney's $350,890.55 priority tax debt will be paid from net income that would otherwise be distributable to Debtor from the trusts.

Confirmation of the UCC Plan is contingent upon State Court approval of these items. Judge Thuma entered two different stay lift orders so that the State Court could rule on these issues.

Judge Thuma denied a stay pending appeal and the Debtor sought a stay from the U.S. District Court.

The District Court, through U.S. Magistrate Judge Fouratt, held that "[t]he filing of a notice of appeal is an event of jurisdictional significance.' (citations omitted) '[I]t confers jurisdiction on the court of appeals and divests the district court of its control over those aspects of the case involved in the appeal.' A notice of appeal does not stay the Bankruptcy Court from all further action, however. In accordance with Bankruptcy Rule 8007(e)(1), all 'other proceedings in the [bankruptcy] case' may continue unless and until the Bankruptcy Court suspends them."

A stay motion is a discrete contested matter. Plan confirmation is a discrete contested matter. Judge Fouratt said that "[t]he viability of a plan often depends on the allowance and liquidation of a creditor's claim under 11 U.S.C. § 503 and/or whether a tax debt has priority under 11 U.S.C. § 507. If appealing such matters automatically divested the Bankruptcy Court of jurisdiction over plan confirmation, obtaining a stay pending appeal would be unnecessary in most cases. Accordingly, the Court concludes that the appeal did not divest the Bankruptcy Court of jurisdiction over the remand or confirmation proceedings."

Judge Fouratt also considered the traditional four factor test and determined that no stay pending appeal would issue.

SUMMARY NUMBER: 7
PMF

KEY CODE SECTION(S): §§101(31); 1129(a)(8)
KEY TOPIC(S): Confirmation of Ch.11 Plan, Appeals

COURT and JUDGE: Supreme Court of the United States, Justice Kagan

CASE NAME and CITE: *U.S. Bank National Association v. The Village at Lakeridge LLC.* 138 S.Ct. 960, 65 BCD 91 (2018)

CASE NUMBER and DOCKET NUMBER: 15-1509

DATE DECIDED: March 5, 2018

NOTEWORTHY ISSUE: What is the standard of review of a determination of non-statutory insider status – clear error or *de novo*?

HOLDING: The Supreme Court ruled that the standard of review of non-statutory insider status is to be clear error. Because the ruling of the bankruptcy court passed muster with that standard, the plan confirmation was affirmed. The court did not grant cert on and did not rule on (but commented on in footnotes) whether the purchaser of a claim from an insider becomes an insider and whether the purchase of the claim in this case in good faith.

FACTS: Debtor sought to confirm its plan. It had two classes of creditors, its secured lender and another in which the class member was a creditor who controlled the debtor. The secured lender objected. The creditor in the other class sold the $2.76 million claim for $5,000 to an individual with whom the controlling person was "romantically involved." The bankruptcy court ruled that the purchaser was not an insider so there was an accepting non-insider class for plan confirmation purposes. The footnotes made it clear that the court was skeptical of the entire situation, but it felt limited by the basis on which it had granted cert.

SUMMARY NUMBER: 8
JAA

KEY CODE SECTION(S): 28 U.S.C. Sec. 158(c)(1), Bankr. Rule 8005(a)

KEY TOPIC(S): Appeals

COURT:	USDC-NM
JUDGE:	Judith C. Herrera
CASE NAME:	Moya Michael Alonzo Agency v. State of New Mexico, the United States, and the United States Trustee
CITE:	2018 WL 1384472
CASE NUMBER:	CIV 18-0177 JCH/KBM
DATE DECIDED:	March 16, 2018

NOTEWORTHY ISSUE: What happens when a *pro se* Appellant fails to use the official Notice of Appeal and Statement of Election (B 417A), in attempting to elect to have the appeal heard by the U.S. District Court?

HOLDING: In this case, the Bankruptcy Court Clerk sent the questionable Notice of Appeal (which did not indicate which order was being appealed, but did say "Waiver of the Bankruptcy Appellate Panel") to both the BAP Clerk and District Court Clerk, resulting in there being two appeals pending. The District court Judge dismissed the District Court appeal, leaving it to the BAP to determine if a valid election to be heard by the District Court was made.

FACTS and DISCUSSION: Even *pro se* Appellants have to use the right official form, or could lose their chance to be heard by the District Court.

In response to the confusion created when the Bankruptcy Court Clerk sent the Notice of Appeal to both clerks, the Bankruptcy Court Clerk will now send a Notice of Appeal to only the BAP if the appellant does not use the official form. The BAP will decide in the first instance if a valid election to be heard by the District Court was made.

SUMMARY NUMBER:	9
KEY CODE SECTION(S):	n/a
KEY TOPIC(S):	Appeals
COURT and JUDGE:	Tenth Circuit Court of Appeals (Hartz, Lucero & McHugh)
CASE NAME and CITE:	Duwaik v. JPMorgan Chase Bank (In re Duwaik) 730 Fed.Appx. 715 (unpublished in federal reporter)
CASE NUMBER:	D.C. No. 1:17-CV-00142-MSK (D. Colorado)
DATE DECIDED:	July 12, 2018
NOTEWORTHY ISSUE:	Is the appeal moot because the bankruptcy was dismissed?
HOLDING:	Yes. Setting aside stay relief would not change the status quo, because the stay terminates anyway upon dismissal. As the appeal of the District Court's order can have no real world consequences, the issue is moot and we lack jurisdiction to address the matter.

FACTS:

JPMorgan Chase is the mortgagee on several parcels of real estate owned by Onar Duwaik. Duwaik filed a Chapter 11 case and confirmed a plan; he defaulted on the payments required by the plan. Chase then sought and obtained stay relief to foreclose. Duwaik appealed to the US District Court, who affirmed the grant of stay relief and denied his requested injunction against foreclosure. Duwaik appealed again to the Tenth Circuit.

Duwaik subsequently filed a Chapter 13 case, and argues the appeal is not moot as he now has another stay. This argument is unavailing; whether to lift the stay in his new Chapter 13 case is a distinct matter.

SUMMARY NUMBER: 10
JAA

KEY CODE SECTION(S): Bankr. Rule 8002(a)
KEY TOPIC(S): Appeals

COURT:	USDC-NM
JUDGE:	Gregory J. Fouratt
CASE NAME:	Moya v. FNU LNU
CITE:	2018 WL 2411600 and Doc. 10.
CASE NUMBER:	Civ. No. 17-978 JB/GJF
DATE DECIDED:	May 29, 2018 and September 21, 2018.

NOTEWORTHY ISSUE: When is an appeal untimely?

HOLDING: An appeal must be filed with fourteen days after entry of the order or judgment being appealed, even for *pro se* appellants.

FACTS and DISCUSSION: This Debtor filed her Ch. 7 case *pro se* as "Cynthia Moya, Estate, a Non-individual Entity." She paid no filing fee. At her Creditor Meeting, the Debtor falsely claimed to be an attorney, representing her "estate." Her estate is apparently a thing called "Cynthia Moya, a natural woman, The Beneficial Owner of the Equitable Cestui Que Trust." The Ch. 7 Trustee filed a motion to dismiss and the case was dismissed. An appeal was filed more than 14 days after the order was entered. In the appeal, the Debtor filed a motion asking that the filing fee be paid by the Social Security Administration on her behalf. The request was denied.

The matter was referred by Judge Browning to U.S. Magistrate Judge Fouratt. Judge Fouratt issued his Proposed Findings and Recommended Disposition, dismissing the appeal as untimely. The Debtor did not object. Normally, with no objection, the District Court Judge would enter an order adopting the U.S. Magistrate's recommendation.

Judge Browning, though, pondered his role. In light of there being no objection from the appellant, should he simply approve what the U.S. Magistrate Judge decided, or should he make an independent review? If so what standard should he use? In a thoughtful 11 page opinion, Judge Browning determined that when no objection to the Magistrate Judge's proposed disposition is made, he should review it under a "clearly erroneous" standard. Judge Browning agreed the appeal must be dismissed.

SUMMARY NUMBER: 11
JAA

KEY CODE SECTION(S): Bankr. Rule 8002(a)
KEY TOPIC(S): Appeals

COURT:	USCA 10th Cir.
JUDGE:	Joel M. Carson, III
CASE NAME:	Lankford v. Wagner (In re: Vaughn Company Realtors)
CITE:	742 Fed. Appx. 391
CASE NUMBER:	No. 18-2030
DATE DECIDED:	November 6, 2018

NOTEWORTHY ISSUE: When is an appeal untimely?

HOLDING: An appeal of a bankruptcy court order or judgment must be filed within 14 days of its entry, or the appeal is untimely. Failure to timely file a notice of appeal is a jurisdictional defect barring appellate review.

FACTS and DISCUSSION: In the VCR bankruptcy case, the Trustee filed numerous avoidance actions. One set of defendants was unhappy with being sued. They twice sought bankruptcy court permission to file counterclaims against the Trustee and her counsel for extortion, incompetence and fraud. Permission was denied. Later, a summary judgment was entered against the defendants for return of their net winnings. The Lankfords did not appeal the bankruptcy court's refusal to permit them to sue the Trustee or the entry of summary judgment. Instead that have filed numerous lawsuits against the Trustee, her counsel and the Department of Justice. They have repeatedly sought relief from the original judgment under Rule 60(b). This case involved another such attempt. Judge Jacobvitz denied the motion. The Lankfords appealed yet again, but this time waited until 23 days after the order denying their motion was entered. The U.S. District Court dismissed the appeal as untimely and the Lankfords appealed to the Tenth Circuit. The Tenth Circuit agreed and dismissed the appeal.

SUMMARY NUMBER: 12 KEY CODE SECTION(S): §327(a), §330
KEY TOPIC(S): Attorney Fees

COURT and JUDGE: NM Bankruptcy Court; David T. Thuma
CASE NAME and CITE: Hungry Horse, LLC
CASE NUMBER: 11-16-11222 TA; Docket No. 586
DATE DECIDED: July 31, 2018

NOTEWORTHY ISSUE:

Can Debtor's attorney recover costs and fees incurred paying undisclosed contract attorneys whose employment was not approved by the Court through fee application?

HOLDING: No.

1. §327 requires debtor's attorneys to disclose compensation paid or agreed to be paid.
2. §330 allows reasonable compensation to estate professionals.
3. Rule 2014 requires an employment application for estate professionals, and a verified disclosure of any connections with the Debtor.
4. Rule 2016 requires a detailed application for compensation for estate professionals.
5. These requirements exist to contain bankruptcy estate expenses and allow the Court to review the competence, integrity and experience of proposed estate professionals.
6. §504 prohibits fee sharing. It is an open question whether hiring contract attorneys is a form of fee sharing; the real issue is disclosure, not fee sharing.

The contract attorneys are attorneys, not paralegals, and are professional persons. They are licensed to practice law in New Mexico. They performed attorney work, not paralegal work (water rights and Uniform Commercial Code security interests respectively). The rates they charged to not reflect paralegal status. They did not comply with §327; the firm cannot be reimbursed from the estate for what they paid these contract attorneys.

FACTS:

Debtor is a limited liability company engaged in oilfield services in eastern New Mexico. It filed Chapter 11 on May 17, 2016. It filed a first day motion to employ counsel, alleging no arrangements had been made to share compensation with anyone outside the firm (ie, not a member or an associate of the firm). Disclosures under Rules 2014 (disinterestedness) & 2016 (prior compensation) did not mention any professionals not employed by the firm. Employment of the firm was approved June 15, 2016. The firm's first fee application was approved for $162,000 on August 23, 2017.

The firm filed a second fee application April 12, 2018 which sought approval of $103,000, including a $2,400 line item for fees paid to a sole practitioner and a member of another law firm. These two attorneys were not employed under §327 and made no disclosures under Rules 2014 or 2016. The Unsecured Creditors Committee objected to this expense; the firm argued the attorneys functioned as paralegals and not attorneys.

SUMMARY NUMBER: 13
JAA

KEY CODE SECTION(S): Sec. 547(b)
KEY TOPIC(S): Preference, Attorney Charging Lien, Rooker-Feldman Doctrine

COURT:	USBC-NM
JUDGE:	David T. Thuma
CASE NAME:	Siebel No. 1 Gonzales v. Geer, Wissel, Levy & Hartwell, P.A. (In re: Shari Siebel)
CITE:	Doc. No. 29
CASE NUMBER:	Adv. Proc. No. 17-01054; Bankr. No. 17-10827-j7
DATE DECIDED:	April 23, 2018

NOTEWORTHY ISSUE: What restriction does the Rooker-Feldman doctrine place on a Bankruptcy Judge's review of a state court decision? What are the elements of a properly perfected attorney charging lien? Can a claimed charging lien be set aside as a preference?

HOLDING: The Rooker-Feldman doctrine holds that lower federal courts lack jurisdiction over a case if the result would be the reversal or modification of a state court judgment. Only the U. S. Supreme Court may review a state court judgment. In this case, the state court did not rule on the validity of the charging lien. Thus, the bankruptcy court could.

Judge Thuma found that in New Mexico, a charging lien requires the four following elements: "[f]irst, there must be a valid contract between the attorney and the client, although the contract need not be express. Second, there must be a judgment, or 'fund,' that resulted from the attorney's services. Third, the attorney must have given clear and unequivocal notice that he intends to assert a lien, and notice must be given to the 'appropriate parties.' Finally, the lien must be timely—notice of the lien must be given 'before the proceeds [from] the judgment have been distributed.'" In this case, the second element was not met. No "fund" resulted from the attorney services. Thus there was no lien, and payments received on account on the lien could be preferences.

FACTS and DISCUSSION: Debtor's state court divorce attorneys recorded liens against the Debtor's community property interest in the family home. The home was sold and the attorney fees were paid. The bankruptcy was filed shortly thereafter. The Trustee sought recovery of the payment as a preference. Since there was no valid lien, the payments could be a preference. The defendant law firm asserted the Rooker-Feldman doctrine in defense of the lien, but the state court had not actually ruled on the validity of the lien. Rooker-Feldman is to be narrowly construed. Judge Thuma held that in any event, "...the Trustee was not a party to the state court action, and is not bound by any ruling on the validity of the charging liens. For Chapter 5 claims like this preference action, a trustee does not 'stand in the shoes of' the debtor.'"

In the end, while the Trustee proved the lien was not valid, she did not yet get a judgment for preference recovery. The Judge found there was a fact issue as to solvency and whether the defendant received more than it would have received in a distribution under Ch. 7. This is a rare case where a preference defendant rebutted the presumption of insolvency in the 90 days sufficiently to create a fact issue.

SUMMARY NUMBER: 14
TDW

KEY CODE SECTION(S):
KEY TOPIC(S): Barton Doctrine; Quasi-judicial immunity

COURT and JUDGE: USBC DNM (Thuma)

CASE NAME and CITE: *Coll v. Carla Franco, et al. (In re Manuela Q. Franco)* 586 B.R. 489 (Bankr.D.N.M., 2018)

CASE NUMBER: Adv. No. 17-1001 t

DATE DECIDED: February 28, 2018

NOTEWORTHY ISSUES: Would claims for damages brought against a chapter 7 trustee, without prior court approval, and not alleging breach of fiduciary duty, for actions trustee took in discharge of his official duties, be dismissed?

HOLDING: Yes. The "Barton Doctrine" precludes suit against a bankruptcy trustee for claims based on alleged misconduct in the discharge of a trustee's official duties absent approval from the appointing bankruptcy court. In addition, the doctrine of quasi-judicial immunity protects trustees from personal liability for acts taken pursuant to their court-appointed function and authority that are not breaches of fiduciary duty.

FACTS:
Debtor and husband conveyed 122 acres of land to their son, Hipolito, as his sole and separate property (the "Property"). Debtor's husband died. Debtor filed a chapter 7 case in 2003, and a second chapter 7 case in 2013. She received a discharge in each case. No mineral rights were listed in the bankruptcy schedules in either case. Hipolito sued Debtor in state court to assert his interest in the mineral rights associated with the Property. Hipolito died. Hipolito's widow, Carla, continued the lawsuit.

Debtor's bankruptcy cases were reopened to administer the mineral rights, which debtor claimed were hers. Chapter 7 trustee filed adversary complaint against to determine the estate's interest in the mineral rights. Defendants were Carla and her lawyer (who had taken an interest in whatever mineral rights Carla has) who, in turn, filed counterclaims against the trustee for quiet title, "disparagement" or slander of title, civil conspiracy to disparage title, and constructive trust, seeking compensatory and other damages for actions taken by trustee in his official capacity. Defendants did not seek or obtain approval from the Court before bringing their claims against the Trustee. Defendants do not allege that the Trustee breached his fiduciary duties. Trustee moved to dismiss counterclaims under Rule 12(b)(1) (lack of subject matter jurisdiction) and 12(b)(6).

The Trustee sought dismissal of the counterclaims under the "Barton doctrine," which "precludes suit against a bankruptcy trustee for claims based on alleged misconduct in the discharge of a trustee's official duties absent approval from the appointing bankruptcy court." Here, the defendants sought compensatory and other damages from the Trustee for actions he

took, and continued to take, in his capacity as the chapter 7 trustee. Rule 12(b)(1) applies to Barton doctrine issues.

The Trustee also asserts that the counterclaims are barred under the doctrine of quasi-judicial immunity. A trustee's immunity has roots in the immunity granted to judges, who are "absolutely immune from civil liability for judicial acts, unless committed in the clear absence of all jurisdiction." Judicial immunity "has been extended to non-judicial officers where their duties have an integral relationship with the judicial process." Quasi–judicial immunity applies to bankruptcy trustees in the Tenth Circuit for all claims except those alleging breach of fiduciary duty, if the trustee acted within the scope of the trustee's authority. Essentially, except for breach of duty claims, so long as trustees act pursuant to their court-appointed function and authority, they are immune from personal liability. Motions to dismiss based on quasi-judicial immunity are typically evaluated under Rule 12(b)(6).

The court construed first count of the counterclaim, quiet title, to be against the estate and not the trustee personally, so it was not covered by the doctrines asserted by the trustee and was not dismissed. Count two, disparagement of title, sought money damages from the Trustee personally. Defendants did not request the Court's approval before bringing the claim. Count Two violates the Barton doctrine, so the Court lacks subject matter jurisdiction over the claim, and the Trustee is protected against the claim by quasi-judicial immunity. Clearly, it is not a breach of duty for the Trustee to assert that his bankruptcy estate owns a valuable asset. Count Two was dismissed.

The court granted the trustee's motion to dismiss count three for the same reasons as count two. As to count four, constructive trust, the court agreed with the trustee that imposing a constructive trust is a remedy, not an independent cause of action, and dismissed it as improperly pled. Also, to the extent the claim is asserted against the Trustee personally, it must be dismissed for the same reasons as Count Two.

SUMMARY NUMBER: 15
TDW

KEY CODE SECTION(S):
KEY TOPIC(S): Claims; Counsel

COURT and JUDGE: USBC DNM (Thuma)

CASE NAME and CITE: *In re Railyard Company, LLC*, 2018 WL 4381515 (Bankr.D.N.M., 2018)

CASE NUMBER: Case No. 15-12386 t11

DATE DECIDED: September 12, 2018

NOTEWORTHY ISSUES: Would claim objection response filed by members of claimant LLC, instead of by counsel, be stricken? And would claim objection be sustained by default?

HOLDINGS: Yes, and Yes. Further, the court analyzed the claim on the merits, found it to be wildly inflated and inadequately documented, and subject to disallowance in any event.

FACTS: Railyard Company, LLC ("Debtor") owned a building in Santa Fe. Prepetition, Debtor entered into a lease with Railyard Brewing Company, LLC ("RBC"). A chapter 11 trustee was appointed in Debtor's case. Trustee moved to reject the lease and after trial the court entered an order rejecting the lease with RBC. RBC filed a proof of claim for $6,771,000. Trustee objected to the Claim. RBC did not retain counsel to respond to the objection. Instead, its members filed a pro se response. LLC's must have counsel in contested matters, so the response was stricken, and the claim objection was sustained by default.

Only RBC has standing to assert and defend the claim. The members of RBC inserted themselves as if they were parties to the lease, but the facts and law did not support that position. RBC was the only person or entity with a direct pecuniary interest in the Lease. The Members had no direct interest in the Claim, so lacked standing to defend it.

Limited liability companies must be represented by counsel. That is the law in the Tenth Circuit, and is the rule locally. D.N.M.LR-Civ. 83.7; NM LBR 1074-1. RBC had notice of this requirement, both in this bankruptcy case and in other actions to which RBC is or was a party. *See, Jaramillo v. Frewing*, 2018 WL 3549822, at *3 (D.N.M.), and 2018 WL 4092075 (D.N.M.). The court held that the appropriate remedy for the filing of improper pro se pleadings is to strike them. Further, since RBC failed to respond to the claim objection, it was sustained by default.

The Claim would be disallowed in any event. Bankruptcy Rule 3001.F. requires supporting documentation to be filed with the claim if the claim is based on writings. RBC asserts that the basis of the claim is "Investment in Real Estate, JV agreement, equipment, furnishings, fixtures, bowling equipment, improvements." The attachments to the Claim do not support these asserted bases and do not comply with Bankruptcy Rule 3001. RBC did not attach any documents that might evidence an investment of real estate. The Court does not know what "JV Agreement" RBC is referring to but, RBC did not attach a "joint venture agreement" or

anything similar. To the extent RBC's claim is for funds invested, the evidence in the case was that Debtor, rather than RBC, paid for and owned the personal property and the leasehold improvements. The attached financing statement and balance sheet demonstrate nothing about the asserted claim. Even on the merits, therefore, the Claim should be disallowed.

SUMMARY NUMBER: 16
JAA

KEY CODE SECTION(S): Sec. 502(b)(1)
KEY TOPIC(S): Claims Objections

COURT:	USBC-NM
JUDGE:	Robert H. Jacobvitz
CASE NAME:	In re: WM Distribution, Inc.
CITE:	591 B.R. 52
CASE NUMBER:	No. 17-10535-j11
DATE DECIDED:	June 29, 2018

NOTEWORTHY ISSUE: When does a liquidated damages clause become an unenforceable penalty?

HOLDING: Under New Mexico law, liquidated damages are unenforceable when they are so extravagant or disproportionate that they arise to fraud, mistake or oppression.

FACTS and DISCUSSION: In this case, liquidated damages of $600,000 were an unenforceable penalty. The Debtor had an obligation to pay $1,300,000 under a prepetition settlement agreement. Liquidated damages of an additional $600,000 would be due if either the Debtor or its affiliate field a bankruptcy, among other things. This amount was so extravagant or disproportionate that it constituted an unenforceable penalty, under state law. When liquidated damages become punishment rather than compensation they can be disallowed.

SUMMARY NUMBER: 17
TDW

KEY CODE SECTION(S):
KEY TOPIC(S): Claims

COURT and JUDGE: USBC DNM (Thuma)

CASE NAME and CITE: *In re: Manuela Q. Franco*, 2018 WL 4859517 (Bankr.D.N.M., 2018)

CASE NUMBER: Case No. 03-13492 tr7; Case No. 13-12941 tr7

DATE DECIDED: October 5, 2018

NOTEWORTHY ISSUES: Would claim filed in bankruptcy case be allowed where part of the claim is for damages for "disparagement" of claimant's title to certain mineral rights ($30,620), and the balance of the claim is for the value of ownership of those mineral rights ($637,000)?

HOLDINGS: No. Damages for disparagement of title could not be an allowed claim because the state court dismissed the disparagement of title action and, after the case was removed to bankruptcy court, the claimant's effort to amend the lawsuit and vacate the state court dismissal failed based on "undue delay, futility, and prejudice." Because of the Court's ruling, claimant could not assert a claim for damages against the Debtor or her bankruptcy estate based on alleged slander of title. The claim for ownership of the Disputed Mineral Rights is not a bankruptcy "claim," which is defined as a "right to payment." Code § 101(5). Asserted property interests are not claims.

FACTS:

Debtor and husband acquired 240 acres of land in 1969 in Eddy County, including a half interest in mineral rights. In 1996, they conveyed 122 acres of the land to their son, Hipolito, as his sole and separate property (the "Property"). Husband died. Hipolito died. Hipolito's widow, Carla, and debtor dispute who owns the mineral rights associated with the Property, each relying on different documents and events to support their claims.

Debtor filed a chapter 7 case in 2003, and a second chapter 7 case in 2013. She received a discharge in each case. The latter case was closed on December 30, 2013. No mineral rights were listed in the bankruptcy schedules in either case.

In 2014, Hipolito and Carla filed a state court lawsuit to quiet title to the Disputed Mineral Rights; for damages for disparagement of title; and for injunctive relief. On motion and after a hearing, in April 2015, the state court dismissed the disparagement of title count. Under New Mexico law, slander of title occurs when one willfully and maliciously records or publishes matter which is untrue and disparaging to another's property rights in land. In her original complaint filed in state court, Carla did not allege malice, which is an essential element of a slander of title claim.

More than a year later, in May 2016, Carla filed a Motion for Leave to Amend Pleadings and Motion to Vacate Order of Dismissal (as amended, the "Motion to Amend and Vacate"). Defendants responded. Plaintiff did not reply.

The bankruptcy cases were reopened in June 2016. A notice of bankruptcy and automatic stay was filed in the state court action in August 2016. Carla filed a proof of claim in the bankruptcy case in October 2016, asserting a claim of $667,620 (the "Claim") secured by the Disputed Mineral Rights. In December 2016, Carla removed the State Court Action to the bankruptcy court.

In February 2017, Carla filed a motion for *nunc pro tunc* relief from the automatic stay, or for a ruling that the stay did not apply, to the state court's entry of a quiet title judgment in the State Court Action. In July 2017, the court denied the stay relief motion and ruled that the ownership of the Disputed Mineral Rights was a matter of bona fide dispute.

In May 2018, the Trustee objected to Carla's Claim and in June 2018, trustee moved for summary judgment. In October 2018, the Court denied the Motion to Amend and Vacate. The ruling, which is denoted a final order pursuant to Rule 54(b), foreclosed Carla's right to assert a slander of title claim against the Debtor or her estate.

SUMMARY NUMBER: 18 KEY CODE SECTION(S): §§ 1122, 1129(a)

PMF KEY TOPIC(S): Confirmation of Ch. 11 Plan

COURT and JUDGE: United States Bankruptcy Appellate Panel, Tenth Circuit, Judge Mosier

CASE NAME and CITE: *In re: Novinda Corp.; Minerals Technologies v. Novinda Corp,.* 585 B.R. 145 (2018)

CASE NUMBER and DOCKET NUMBER: No. 16-13083

DATE DECIDED: May 16, 2018

NOTEWORTHY ISSUE: Whether classification of certain unsecured creditors who were also minority stockholders and potential targets for litigation into a separate class from other unsecured creditors was improper gerrymandering or otherwise unfair and discriminatory.

HOLDING: The BAP analyzed the requirements of §1122 for proper classification and noted that § 1129(b) which prohibited discrimination was limited to claims within a class rather than treatment among classes. The fact that the debtor had a priority class of non-insiders (employees holding wage and vacation claims) which it was confident would accept the plan defeated the argument that the classes were gerrymandered (although the 10th Circuit has not ruled on whether classifying creditors to obtain a consenting class was improper). The plan was feasible despite providing a fund for litigation against the creditors opposing confirmation, the plan had sufficient funds provided to pay the priority classes and investigate the claims. It was not dependent on a successful result in the litigation. The fact that only 9 creditors were in the administrative convenience class was found proper because the plan administrator sought it as part of his negotiations to accept the position and because the debtor expected the employee priority class would accept the plan so they didn't need to gerrymander. The plan confirmation was affirmed.

FACTS: Debtor high tech company sought plan confirmation of a liquidation plan that would provide for litigation against minority stockholders who were also unsecured creditors. The minority stockholders had entered into contracts to manufacture the product of the debtor, and disputes arose regarding the manufacturing. The debtor had been financed by several investment firms (the "Funds"). The assets of the debtor had been auctioned off to the Funds as the only bidders. The Funds also agreed to provide financing to pay priority claims and provide $25,000 to investigate claims against the manufacturing firm. The plan provided that the minority stockholders would be in a separate class, although sharing pro rata with other allowed unsecured creditors.

SUMMARY NUMBER: 19 KEY CODE SECTION(S): 11 U.S.C. § 523(a)(8)
PMF KEY TOPIC(S): Discharge

COURT and JUDGE: United States District Court, D. New Mexico, Judge Jacobvitz

CASE NAME and CITE: *In re: Murphy, Murphy v. U.S.A.; N.M. Educational Assistance Foundation aka New Mexico Student Loans*, 2018 WL 2670455

CASE NUMBER and DOCKET NUMBER: Adversary No. 15-1051-j

DATE DECIDED: June 1, 2018

NOTEWORTHY ISSUE: Whether the debtor showed undue hardship to her and her dependents and could get a discharge of her student loans.

HOLDING: "In general, it is quite difficult for a debtor to discharge student loans based on undue hardship." In this case, the court concluded that the debtor met that burden. The factors to be considered are:

1. The debtor cannot maintain based on current income and expenses a "minimal" standard of living for herself and her dependents if forced to repay the loans.
2. Additional circumstances exist indicating the state of affairs is likely to persist for a significant portion of the repayment period.
3. The debtor has made good faith efforts to repay the loans.

FACTS: Debtor was 58 years old. She was divorced, and had four children. Her former husband, 76 years old, suffered a stroke, and the debtor became his primary caregiver. Her oldest son attempted suicide a number of times and had medication for mental illness. The debtor frequently had to leave work to care for him. He will remain a dependent for the foreseeable future. Her second son lives with the debtor, and he pays rent. Some of the student loans were for this son's college education. Son number three is a minor and the debtor is covered by the debtor's insurance and other costs. There was no evidence regarding the fourth son.

The debtor had worked as a waitress and then was terminated when she went to Chile to care for her grandmother who was ill. She cashed in her 401(k) to pay for the trip. The debtor was trained as a surgical assistant, but she cannot find work because of her caregiver commitments. The debtor made some minimal payments on the student loans. The debtor worked with the US-DOE and NM Student Loans on different repayment options, and she was placed in the income based repayment ("IBR") plans. That plan concluded she could pay nothing.

SUMMARY NUMBER: 20 KEY CODE SECTION(S): §§ 523(a)(3)(B); 727(d)(1)

PMF KEY TOPIC(S): Discharge, Dischargeability

COURT and JUDGE: United States Court of Appeals, Tenth Circuit, Judge Phillips

CASE NAME and CITE: *In re: McNally; Carns v. McNally.* 731 Fed.Appx. 814 (2018)

CASE NUMBER and DOCKET NUMBER: No. 17-1367

DATE DECIDED: June 13, 2018

NOTEWORTHY ISSUE: Whether the creditor had adequate notice of the bankruptcy. Whether the omissions of assets and transfers by the debtor were material and/or indicated fraudulent intent sufficient to deny discharge

HOLDING: The findings of the bankruptcy court were upheld. The creditor was sent notice through his attorney who had been attempting to collect the debt. That was adequate even if the attorney was no longer actively working on the matter. The omissions of some failed business ventures, including several books that did not sell, were of inconsequential value and did not indicate fraudulent intent.

FACTS: Creditor obtained a default judgment for $700,000 arising from a failed investment. Debtor attempted several business ventures, including writing several books, an auto leasing attempt and currency trading account. All failed. The bankruptcy schedules listed the creditor's attorney for notice, but the attorney had not been actively representing the creditor for some time. The court found that notice adequate. The omission of the books was found to be immaterial, and transfers were found to have actually been made by the business partner of the debtor. The creditor simply failed to prove any intent to defraud or failure to list any material asset.

SUMMARY NUMBER: 21
JAA

KEY CODE SECTION(S): Sec. 524
KEY TOPIC(S): Discharge Injunction, Redemption

COURT:	10th Cir. BAP
JUDGE:	Judge Karlin
CASE NAME:	Sprague v. Williams (In re: Van Winkle)
CITE:	583 B.R. 759
CASE NUMBER:	BAP No. NM-17-031, 032, 033;
DATE DECIDED:	April 3, 2018

NOTEWORTHY ISSUE: Does the post-discharge foreclosure of nonexempt property, and the re-recording of a deficiency judgment after redemption by the Debtor, violate the discharge injunction? If a creditor violates a court order setting the amount of its lien on otherwise exempt property, can it be held in contempt?

HOLDING: Under New Mexico law, re-recording the lien on non-exempt property does not violate the discharge injunction. Violating a court order can lead to contempt of court.

FACTS: A Debtor filed a motion to avoid a lien on his homestead, as it impaired his exemption. Before a ruling was made, the Debtor died. His personal representative entered into a Stipulated Order which preserved the exemption and capped the judgment lien at a set amount. The judgment creditors later sought to foreclose their remaining judgment lien on the homestead. The judgment creditors also sought to enforce their lien on nonexempt property. They foreclosed on the nonexempt property and the debtor redeemed, but the judgment creditors also filed a new judgment lien for the deficiency, which again attached to the nonexempt property. High-jinx and litigation in bankruptcy court ensued.

As to the nonexempt property, the Tenth Circuit ultimately held "that redeemed real property *once again* becomes part of the mortgagor's real estate subject to prior judgment liens. In New Mexico, judgment liens attach to real property acquired by a judgment debtor after the date a transcript of judgment is filed, including property lost at foreclosure but reacquired through redemption. However, nothing in the New Mexico Supreme Court's interpretation of the law indicates property redeemed is newly acquired property—rather, the property 'again becomes part of [a debtor's] real estate.' While this statutory scheme, which allows repeated foreclosures, appears to conflict with New Mexico's stated public policy behind redemptions, it is nonetheless the law of New Mexico." Thus, the creditor did not violate the discharge injunction by the action, as the "...the filing of the postredemption foreclosure action was not in violation of § 524(a)(2) because, under New Mexico law, a deficiency judgment may become a postredemption lien on the real property once properly transcribed."

As to the Stipulated Order and homestead property, the Stipulated Order provided that the judgment lien was "partially avoided and attache[d] only to the extent of any value over and

above the stipulated value of the [Condo] ($100,000) less the payoff of the First Mortgage, less the Debtor's allowed Homestead Exemption ($60,000)." In the foreclosure case, however, the judgment creditors asked that the proceeds of the sale be paid out first to the mortgage, second to the $60,000 homestead exemption and third to the *balance* of the judgment lien, without any limitation. This was a violation of the Stipulated Order as the judgment creditors asked for the full balance instead of limiting the amount due on the mortgage and lien to a total of $40,000, as the Stipulated Order provided. This led to the contempt of court sanctions order by the bankruptcy court, with actual and punitive damages of $50,000.00.

The Tenth Circuit remanded for a recalculation of the punitive damages but noted "[w]e agree that the record is replete with examples where positions taken by the [creditor] appeared to be an unnecessarily relentless pursuit to collect the Judgment Lien, often without regard to the law or the practicalities of litigation."

SUMMARY NUMBER: 22 KEY CODE SECTION(S): §523(a)(6)
KEY TOPIC(S): Dischargeability

COURT and JUDGE: NM Bankruptcy Court; David T. Thuma

CASE NAME and CITE: WLC Enterprises, Inc. v. Rylant (In re Rylant)
CASE NUMBER: 17-12354 t7; Adv. No. 17-1090 t
DATE DECIDED: December 7, 2018

NOTEWORTHY ISSUE: Is the Plaintiff's claim non-dischargeable?

HOLDING: Yes. Plaintiff's $30,000 judgment survives discharge.

1. There is a split of authority; this Court sees nothing in the Code to prevent intentional breaches of contract from surviving discharge under §523(a)(6).
2. Judge Huling's finding that Crawley failed to prove punitive damages does not prevent Judge Thuma from excepting the debt from discharge under the doctrine of issue preclusion or collateral estoppel. Judge Huling focused on the larger debt from Loop LLC, and New Mexico punitive damage standards are not identical to §523(a)(6) standards.

FACTS:

William Crawley owns WLC Enterprises, Inc., the company that owned Murphy's Mule Barn, a restaurant in Albuquerque. He had known Rylant for many years since Rylant helped Crawley get his first loan. Rylant was a banker in California for 18 years until he pled guilty to fraud and embezzlement charges and served several years in jail. After his release he returned to New Mexico.

Rylant purchased Murphy's Mule Barn in September of 2015 for $350,000; at the time Rylant had $220,000 in a Swiss bank account but did not use those funds for the purchase. Rylant's company Loop DL, LLC agreed to pay $30,000 at closing, $20,000 15 days later and sign a note for the remaining $300,000 at 4% interest. At closing Rylant borrowed $15,000 from Crawley, and borrowed an additional $15,000 from Crawley in December of 2015. He never made a payment on the note, and did not pay the $20,000 second installment. Crawley sued in state district court and got a judgment for $347,194.27 against Loop DL, and $30,000 against Rylant. Judge Valerie Huling found Crawley did not prove a culpable mental state sufficient to support punitive damages. Post judgment Rylant sold all the restaurant assets and kept the sales proceeds. Crawley, age 74, is now driving a truck to support himself.

One wonders why Plaintiff didn't allege §523(a)(2) in the alternative. Judge Thuma discusses factors leading to his decision including Crawley's lack of representation, lack of sophistication, the long friendship between the parties, Crawley's eagerness to sell the restaurant, the one sided terms of the note, Rylant's failure to ever pay even a penny on the note, the loans from Crawley to Rylant personally, failure to use existing cash assets to pay, last minute repossession and sale of restaurant equipment and Rylant's lack of credibility at trial; these all sound like the badges of fraud a Court would consider in a fraud adversary. Plaintiff's counsel is not a bankruptcy regular.

SUMMARY NUMBER: 23 KEY CODE SECTION(S): §523(a)(8)
MKD KEY TOPIC(S): Dischargeability

COURT and JUDGE: NM Bankruptcy Court; Robert H. Jacobvitz
CASE NAME and CITE: Regan v. US Dept. Education (In re Regan); 590 B.R. 567
CASE NUMBER: Case No. 7-17-11208 JA; Adv. No. 17-1046 j
DATE DECIDED: September 6, 2018

NOTEWORTHY ISSUE:

Can Debtor discharge her student loans as an undue hardship under §523(a)(8)?

HOLDING:

No, she has not satisfied the first prong of the ***Brunner*** test, which requires:

1. Debtor cannot maintain a minimal standard of living for herself and any dependents if forced to repay the loans.
2. Additional circumstances exist indicating this state of affairs is likely to persist for a significant portion of the repayment period of the student loans.
3. The debtor has made good faith efforts to repay the loans.

Debtor's Schedule I left off her second job and summer job income, and would exceed the state median were that included. Her IBRP payments would be $219/mo. If she stays in the PSLFP her loans will be forgiven when she is 72 years old. She is healthy, without dependents and has steady employment in the field in which she obtained her degree. She can maintain a minimal standard of living given the existence of IBRP and PSLFP.

FACTS:

Debtor got an associate's degree, then a bachelor's degree at University of Massachusetts. She obtained student loans from 1982 – 1994. She worked for BIA in Gallup in hopes of discharging her student loans, but later learned that would not be possible. She paid on her student loans for a time. She moved to Albuquerque in 2006 and obtained a full time teaching job. She took a large number of deferments and forbearances, and participated in an income contingent repayment plan; she was unable to keep up those payments. She consolidated her student loans in 2008. She defaulted in 2016; her balance is currently $51,000.

Debtor is 62 with no dependents. She teaches summer programs and has a second job at a JC Penny call center to increase her income. She would like to retire, but feels repayment of the student loan debt would be a huge burden for her in the future. She is enrolled in the Public Service Loan Forgiveness Program whereby after 120 consecutive timely payments her loans will be forgiven. If she leaves her job she may qualify under an income contingent repayment plan, of which there are many. Under these plans 240 or 300 qualifying payments are necessary to discharge the student loans.

These are hard cases for debtors to win.

SUMMARY NUMBER: 24
JAA

KEY CODE SECTION(S): Sec. 523(a)(2)(A)

KEY TOPIC(S): Dischargeability, Claim Preclusion

COURT:	USBC-NM
JUDGE:	Robert H. Jacobvitz
CASE NAME:	Maljamar Fuel Stop v. Sherman (In re: Sherman)
CITE:	2018 WL 3617660
CASE NUMBER:	Adv. Proc. No. 17-1039-j; Bankr. No. 17-10241-j7
DATE DECIDED:	July 26, 2018

NOTEWORTHY ISSUE: Can a contractor's misrepresentation that he has a contractor's license be the basis of a non-dischargeability claim under 11 U.S.C. § 523(a)(2)(A)?

HOLDING: It can, but in this case, the creditor's damages would be limited to the amount awarded in the prepetition state court case.

FACTS and DISCUSSION: The contractor clearly lied about having a valid contractor's license. The project failed, and in a state court case the contractor was found liable to the creditor for $155,693.26, plus interest and attorney fees. The dischargeability complaint sought a higher amount of damages. Claim preclusion prevents the bankruptcy court from increasing the damages awarded by the state court, even though the state court judgment was entered by default.

SUMMARY NUMBER: 25 KEY CODE SECTION(S): §523(a)(2) & (6)
MKD KEY TOPIC(S): Dischargeability

COURT and JUDGE: U.S.B.C.; David T. Thuma
CASE NAME and CITE: Nelson v. Bolles (In re Bolles);
CASE NUMBER: Case No. 7-17-11788 TA; Adv. No. 17-01077 t; Docket No. 52
DATE DECIDED: November 27, 2018

NOTEWORTHY ISSUE:

1. Should the Plaintiff's claims survive Debtor's discharge under §523(a)(2)?
2. Should the Plaintiff's claims survive Debtor's discharge under §523(a)(6)?
3. What damages should Plaintiff recover?

HOLDING:

1. No. The Defendant made a false statement, which he knew to be false, with the intent to deceive the Plaintiff into having sex with him, she justifiably relied on his false statement and she was damaged by her reliance on the false statement. His fraud escapes the reach of §523(a)(2) because he used it to obtain sex, rather than money.
2. Yes. The Defendant did not intend to give Plaintiff herpes, but knew she was substantially certain to contract it from unprotected sex with him. His conduct was therefore willful; without analysis the Court also found the conduct malicious.
3. Plaintiff should recover $49,192 in compensatory medical damages, pain and suffering of triple that amount ($147,756) and punitive damages of $50,000 for a total award of $246,768.

FACTS:

The parties met through Tinder and commenced a romantic relationship. Debtor had contracted herpes in 2004, been treated for it in 2014, but did not warn Plaintiff he had it before having unprotected sex with her. Plaintiff was later diagnosed with herpes; even then Defendant said he must have unwittingly contracted the disease from his former spouse. Eventually he confessed.

Nelson sued Bolles in state district court, Bolles filed bankruptcy, Nelson filed an adversary to except her claims from discharge. After an unsuccessful summary judgment motion by Plaintiff, the parties proceeded to trial.

Hard cases often make bad law. The finding that "he did not intent to give her herpes" sounds like a defense decision under §523(a)(6).

SUMMARY NUMBER: 26 KEY CODE SECTION(S): §523(a)(6)
MKD KEY TOPIC(S): Dischargeability

COURT and JUDGE: NM Bankruptcy Court; David T. Thuma
CASE NAME and CITE: Estate of Coleman v. Mladek;
CASE NUMBER: Case No. 7-17-10948 TR; Adv. No. 17-01047 t; Docket No. 39
DATE DECIDED: August 16, 2018

NOTEWORTHY ISSUE:

Should the Court grant summary judgment to Defendant?

HOLDING:

No. There are genuine issues of material fact (willfulness and malice).

The Court provides a good summary of §523(a)(6) cases. Willful requires a deliberate or intentional injury, not an intentional act that leads to injury. The Tenth Circuit uses a subjective standard to measure the Debtor's intent for malice. Malicious intent may be demonstrated by evidence the Debtor knew of creditor's rights and acted in violation of them. New Mexico's slander of title cause of action has malice as an element.

FACTS:

Mladek (through an entity named "The Hand of God" or "THOG") filed a "lien" against property owned by the Coleman Estate in Alamogordo purportedly based upon purchasing Otero County tax liens. In a quiet title lawsuit the state court ruled in favor of Coleman, including a finding that Mladek's entity had not purchased any liens. Before the ruling could be memorialized in a written order, Mladek filed bankruptcy. Coleman Estate filed an adversary proceeding to except its claim from discharge under §523(a)(2) and (a)(6). Plaintiff concedes the §523(a)(2) claim is not well taken; summary judgment is granted on that.

In last year's review we covered Mladek's challenge to Bankruptcy Court jurisdiction and motion to dismiss under F.R.Civ.P. 12(b)(6). This year we cover her motion for summary judgment.

Judge Thuma points out in a footnote the parties did a poor job of presenting evidence in support of their positions; instead of summarily denying the motion the Court provides the opinion to inform the parties of the issues requiring resolution at trial.

SUMMARY NUMBER: 27 KEY CODE SECTION(S): § 727(a)(6)(A), Rule 37
TDW KEY TOPIC(S): Denial of Discharge

COURT and JUDGE: 10th Cir. Court of Appeals (J. Lucero, Kelly, And Phillips)
CASE NAME and CITE: *Layng v. Rael (In re: Rael)*, 2018 WL 6437559 (10th Cir., 2018)
CASE NUMBER: No. 18-8026
DATE DECIDED: December 7, 2018

NOTEWORTHY ISSUES: (1) What is the standard to deny discharge under Code § 727(a)(6)(A) for refusal "to obey any lawful order of the court?" (2) What must a party show to support an "advice of counsel" defense? (3) May a party be sanctioned for failure to respond to discovery when the court finds that the non-disclosure was "substantially justified?" [The opinion includes several other issues.]

HOLDINGS: In a dense, fact-intensive decision covering many topics, (1) the court described the standard for denial of discharge under Code § 727(a)(6)(A) for refusal to obey any lawful order of the court as, "the debtor received the order in question and failed to comply with its terms" and that the debtor's non-compliance was willful;" (2) described the elements to support an "advice of counsel" defense; and, (3) held that it was error to sanction a party for failure to respond to discovery when at the same time the court found that the non-disclosure was "substantially justified."

FACTS: Debtors filed bankruptcy and confirmed a Chapter 11 Plan. The Plan required debtors to pay Wells Fargo by property and making monthly payments. Debtors defaulted on the monthly payments, and Wells Fargo got state court judgments against them. Debtors reopened the Chapter 11 case and, among other things, asked that Wells Fargo be held in contempt for filing the state court proceedings. In the meantime, debtors found a buyer for the property and the court entered a "Sale Order" that required in part that the proceeds be paid to Wells Fargo. Wells Fargo was not held in contempt for obtaining the state court judgment. Debtors did not give the sale proceeds to Wells Fargo and, instead, used the proceeds to pay legal fees and the IRS. Then they converted the case from Chapter 11 to Chapter 7 and filed a motion for discharge. US Trustee objected to discharge. The bankruptcy court granted a discharge, among several other orders in debtors' favor. The district court essentially reversed all the relief granted by the bankruptcy court, including the discharge, finding that the bankruptcy court's determination that debtors' violation of the Sale Order was not willful was clearly erroneous. The district court also reversed the order awarding attorney fees against the Trustee as a discovery sanction. Debtors appealed to the 10th Circuit court of appeals, which affirmed the district court.

Discharge Issue: Debtors argued that the district court erred by reversing the bankruptcy court order granting them a discharge. Under Code § 727(a)(6)(A), a court will deny a discharge if "the debtor has refused ... to obey any lawful order of the court, other than an order to respond to a material question or to testify." The party objecting to discharge under § 727(a)(6) must demonstrate that "the debtor received the order in question and failed to comply with its terms" and that the debtor's non-compliance was "willful." A party acts willfully when he fails to comply with a court order even if he subjectively believes the order

was invalid. If a party "to whom a court directs an order believes that order is incorrect the remedy is to appeal, but, absent a stay, he must comply promptly with the order pending appeal. Here, the Debtors violated Sale Order by failing to give the sale proceeds to Wells Fargo. The court of appeals affirmed the district court, denying debtors a discharge.

Advice of Counsel: Debtors argued that their failure to comply with the Sale Order was not willful because they acted in reliance on the advice of their counsel. To prove an "advice of counsel" defense, debtors had to show that (1) they requested counsel's advice about what to do and communicated all relevant facts to counsel; (2) counsel advised them not to comply and that it was legal not to comply; and (3) they relied in good faith on counsel's advice. Here, debtors inexplicably failed to comply with the court order for over 10 months before they got the advice from counsel upon which they claimed to rely. The bankruptcy court clearly erred in finding that debtors non-compliance was not willful because it was based on the advice of counsel and, therefore, the bankruptcy court erred in granting debtors' request for discharge.

Discovery sanctions: The court of appeals reversed the award of attorney's fees against the Trustee as a discovery sanction. The issue was whether the Trustee's lack-of-knowledge objections to debtors' discovery requests were substantially justified. Rule 37 provides that, if a motion to compel discovery is granted, the court must award movant's reasonable expenses, including attorney fees, unless the nondisclosure was substantially justified, which means "justified to a degree that could satisfy a reasonable person."

The bankruptcy court found that the Trustee's lack-of-knowledge objection was "reasonably justified," because the requests for admissions sought information outside the Trustee's control and a party is not required to obtain responsive information from third parties to satisfy the reasonable-inquiry requirement. Still, the bankruptcy court ordered the Trustee to pay a portion of the debtors' attorney's fees as a sanction for not providing an adequate reasonable inquiry explanation. The district court reversed the sanctions award, concluding that the bankruptcy court abused its discretion by ordering the Trustee to pay the attorney's fees "when [it] simultaneously found the Trustee's response was justified."

SUMMARY NUMBER: 28 KEY CODE SECTION(S): §§ 727(a)(2)(A) and (a)(3
TDW KEY TOPIC(S): Objection to discharge

COURT and JUDGE: 10th Cir. BAP (J. Karlin)

CASE NAME and CITE: *Lee v. Peeples*, 2018 WL 3424680 (10th Cir. BAP, 2018) (Unpublished)

CASE NUMBER: Bankr. Case No. 14-23970; Adv. No. 14-2236; BAP No. UT-18-003

DATE DECIDED: July 16, 2018

NOTEWORTHY ISSUE: What are the standards to deny discharge under Code §§ 727(a)(2)(A) and (a)(3)?

HOLDING: In a very fact specific decision, the BAP sets forth standards for proof of objections to discharge under Code §§ 727(a)(2)(A) and (a)(3).

FACTS: Aggressive former landlord obtained judgments against tenants. Tenants filed chapter 7 in April 2014. Landlord pursued objections to discharge (1) due to lack of records made or retained by one debtor for a business he operated in 2011 and 2012, and (2) alleged concealment of assets within one year of bankruptcy evidenced by debtors' alleged failure to disclose in their bankruptcy schedules the purported business inventory from the business last operated in early 2012, a Barbie doll collection, and personal goods such as DVDs, a laptop computer, and household furnishings. The bankruptcy court ruled against landlord and the BAP agreed.

Code §727(a)(3):

- An objection to discharge under Code § 727(a)(3) requires the objecting party to show that the "debtor failed to maintain and preserve adequate records and that the failure made it impossible to ascertain his [or her] financial condition and material business transactions."
- Section 727(a)(3) is intended to allow creditors to reasonably ascertain a debtor's present financial condition and to follow his business transactions for a reasonable period in the past.
- The bankruptcy court has "reasonably wide discretion" in determining whether the books of account or records in a given case are sufficient to meet the requirements of the statute.
- In consumer cases, debtors have a much-diminished obligation to keep books.

Code §727(a)(2)(A):

- Code § 727(a)(2)(A) requires the objecting party to show by a preponderance of the evidence that (1) the Debtors transferred, removed, concealed, destroyed, or mutilated, (2) property of the estate, (3) within a year prior to the bankruptcy filing, and (4) did

so with actual intent to hinder, delay, or defraud the party. In the present case, the plaintiff argued only concealment.

- Concealment includes "attempts [by debtors] to keep the property out of reach of creditors or the estate by secreting or refusing to reveal the location of the property."
- The Plaintiff must show that the Debtors had assets of value to conceal, and were motivated to hide the assets, so that they could not be executed upon.
- The burden is on the Plaintiff to establish that the debtors owned and concealed valuable property.
- Debtors' failure to attend prepetition, state court collection hearings was in itself insufficient to show actual intent to hinder or delay the Plaintiff's collection actions or to defraud him.
- Avoiding prepetition collection attempts, under some case law, is relevant when coupled with evidence that debtors had in fact transferred or concealed valuable property.

Here, there was "abundant evidence" that the Debtors had no valuable assets to conceal.

SUMMARY NUMBER: 29
PMF

KEY CODE SECTION(S): BR 2004
KEY TOPIC(S): Discovery

COURT and JUDGE: U.S. Bankruptcy Court, D. New Mexico. Judge Thuma

CASE NAME and CITE: *In Re: Victor P. Kearney, Debtor*

CASE NUMBER and DOCKET NUMBER: 17-12274-t11, Doc. 429

DATE DECIDED: September 14, 2018

NOTEWORTHY ISSUE: What are the limits on Rule 2004 pre-litigation discovery?

HOLDING: Given the nature of the purposes of the discovery, the history of discovery abuse, the scope of the discovery sought, and the nature of the claims sought to be investigated, limited discovery would be permitted.

Rule 2004 should not be used to harass or used as a device for a wholesale investigation of a non-debtor's private affairs. It can be used as a pre-litigation devise to determine whether a claim of the estate has merit. The court has discretion to tailor a Rule 2004 discovery request. Whether the request is burdensome is an issue. The fact that this discovery was for derivative claims was significant and weakened the motion. Other issues such as the conflicts from an attempted derivative action and confidentiality were to be considered.

The court ruled that because there were significant "red flags" he would proceed cautiously. The court allowed the new lawyers to get the documents previously produced in the state court pre-bankruptcy litigation under a new confidentiality order.

FACTS: The debtor was the beneficiary of a spendthrift trust. He sought pre-litigation discovery from the corporation whose stock was in the trust. The debtor and his trustees (officers in the corporation) were parties to significant litigation prior to the bankruptcy filing. During that litigation, the debtor had received significant confidential information of the corporation under a confidentiality order and violated that order by disseminating the information to certain people and entities who then circulated the material to at least 28 other people. In the bankruptcy, the debtor retained counsel to investigate whether there were claims against the corporation.

The theory under which the discovery was sought was that claims against the corporation were a major asset of the estate. The claims would be derivative in the sense that the debtor as a beneficiary of the trust would step into the shoes of the trust who had the right to bring a stockholder derivative claim against the corporation.

SUMMARY NUMBER: 30
JAA

KEY CODE SECTION(S): Sec. 707(a) and 109(g)(2)
KEY TOPIC(S): Dismissal, Standing

COURT:	USBC-NM
JUDGE:	Robert H. Jacobvitz
CASE NAME:	In re: Xiong
CITE:	2018 WL 1725572
CASE NUMBER:	17-12681-j7
DATE DECIDED:	April 6, 2018

NOTEWORTHY ISSUE: What constitutes "cause," under Sec. 707(a), for dismissal of an individual Debtor's Ch. 7 case? Do the facts support a 180 day prohibition on refiling under Sec. 109(g)(1)?

HOLDING: The Debtor failed to prosecute her case. The case was dismissed and the 180 restriction on refiling was imposed.

FACTS and DISCUSSION: Basically, this Debtor never appeared at any hearing in the case, despite asking for and receiving extensions of time to respond to motions and continuances of hearings. She also filed 18 appeals of various orders, without paying filing fees.

Judge Jacobvitz found ample evidence to conclude that the Debtor had willfully failed to appear and failed to properly prosecute her case. "Since the filing of the voluntary chapter 7 petition on October 24, 2017, the Court has held five hearings. *See* Docket Nos. 24, 30, 60, 119, and 126. Despite granting two of Ms. Xiong's requests for continuance, Ms. Xiong has not appeared at a single hearing, by telephone or otherwise. *See* Docket No. 26 (continuing hearing on Motion to Avoid Lien and Motion for Relief from Stay to November 6, 2017) and Docket No. 121 (continuing hearing on Motion to Dismiss to March 29, 2018). She filed the Motion to Avoid Lien in response to PODS's Motion for Relief from Stay, but failed to appear at the scheduled final hearing in support of her motion, resulting in the denial of her Motion to Avoid Lien for failure to meet her burden of proof. *See* Docket No. 62".

The Judge further found the Debtor had a consistent pattern of requesting continuances shortly before each hearing. "Given her complete failure to attend any hearing, even by telephone, the Court can only conclude that Ms. Xiong has willfully failed to appear before the Court in proper prosecution of her case."

SUMMARY NUMBER: 31
PMF

KEY CODE SECTION(S):§341
KEY TOPIC(S): Appeal, Dismissal

COURT and JUDGE: United States District Court, D. New Mexico, Judge Brack

CASE NAME and CITE: *Moya v. U.S. Eagle Federal Credit Union and Montoya, Trustee,* 2018 WL 1470554

CASE NUMBER and DOCKET NUMBER: CIV 17-0415 RB/KBM

DATE DECIDED: March 26, 2018

NOTEWORTHY ISSUE: Should the bankruptcy be dismissed if the debtor refuses to properly participate in the § 341 and produce documents.

HOLDING: The bankruptcy by the *pro se* debtor was properly dismissed, affirming the bankruptcy court and adopting the magistrate's findings which were reviewed *de novo*. The debtor asserted that she had been required to "swear" rather than "affirm" her statements at the § 341 were true, but provided no evidence of that. The argument that the bankruptcy court was unconstitutional was rejected. The magistrate properly made some allowance for the *pro se* pleadings, but the magistrate properly declined to construct arguments or search the record for the *pro se* party.

FACTS: The debtor was on her third bankruptcy. She refused to "swear" her statements at the § 341 meeting would be correct, claiming a religious objection. She did not present evidence to show she was required to "swear" rather than to "affirm." She argued the bankruptcy court was unconstitutional and that the bankruptcy court was not part of the judicial branch. There is no mention of why she filed for bankruptcy with that court three times.

SUMMARY NUMBER: 32
JAA

KEY CODE SECTION(S): Sec. 349
KEY TOPIC(S): Dismissal

COURT:	USBC-NM
JUDGE:	Robert H. Jacobvitz
CASE NAME:	Viper Services, LLC v. Fora Financial Business Loans, LLC (In re: Viper Services, LLC)
CITE:	2018 WL 1801208
CASE NUMBER:	Adv. Proc. No. 17-1010-j; Bankr. No. 15-11259-j11
DATE DECIDED:	April 13, 2018

NOTEWORTHY ISSUE: After dismissal of a Ch. 11 case, what constitutes "cause" to not also dismiss a pending preference action that would normally be dismissed under Sec. 349?

HOLDING: Judge Jacobvitz held that "[t]he general idea behind § 349 is that the dismissal of a bankruptcy case should re-establish the rights of the parties as they existed when the petition was filed." "Here, dismissing this adversary proceeding and precluding Viper from pursuing a preference action—an action that exists only because Viper commenced a bankruptcy case—accomplishes that goal."

FACTS and DISCUSSION: In last year's Year in Review concerning this case, we learned that the Court determined that dismissal of the Chapter 11 case would moot the preference action absent a finding of "cause" under 11 U.S.C. § 349. The parties to the adversary filed motions to either find such "cause" or to dismiss the proceeding.

Debtor complained that it would be inequitable to bind it to the plan after case dismissal while depriving it of the ability to pursue a $37,000 preferential transfer claim to help fund the plan. (By "fund the plan," the Debtor meant have money to pay its attorneys' administrative claim.) Judge Jacobvitz noted that the Ch. 11 case was dismissed for failure to file operating reports and pay the US Trustee fees. The Plan relieved the Debtor of the obligation to pay $530,000 to holders of about $590,000 in unsecured claims, and took advantage of other Bankruptcy Code protections. Rather than file the post-confirmation quarterly reports and pay U.S. Trustee fees, Viper allowed its case to be dismissed. Under these circumstances, there is no "cause" to allow the preference action to proceed.

Annual Bankruptcy Case Review Part 2

SUMMARY NUMBER: 33 KEY CODE SECTION(S): §523(a)(8)
KEY TOPIC(S): Rule 12(b)(6)

COURT and JUDGE: NM Bankruptcy Court; Robert H. Jacobvitz

CASE NAME and CITE: Gimbel v. ECMC (in re Gimbel) 2018 WL 1229718

CASE NUMBER: 11-12802 j7; Adv. No. 17-01048 j (Docket No. 25)

DATE DECIDED: March 8, 2018

NOTEWORTHY ISSUE: Should the Debtor's hardship discharge complaint be dismissed for failure to state a claim under F.R.Civ.P. 12(b)(6)?

HOLDING: No.

1. Plaintiff must allege facts sufficient to state a claim that is plausible on its face. ***Ashcroft v. Iqbal***, 556 U.S. 662, 697 (2009); Mr. Gimbel has done so.
2. Laches (the six year delay between bankruptcy petition and adversary complaint) is an affirmative defense ECMC may assert and attempt to prove; it is not a basis for dismissal at the beginning of a lawsuit for failure to state a claim.
3. There is no time limit in the Bankruptcy Code for filing a complaint under §523(a)(8).

There is an odd allegation in ECMC's motion that the increased student loan balance between the petition date and the complaint filing date shows that the Debtor must have incurred additional student loans post bankruptcy, which would not be dischargeable whatever the hardship. Judge Jacobvitz doesn't spend much time on this, but it would seem logical that is merely additional interest on the pre-petition student loans.

FACTS:

Jonathan Gimbel is 63 years old, and lives in Santa Fe. In 2011 he filed a Chapter 7 bankruptcy proceeding; he owed student loan debt to US Dept. of Education and Sallie Me totaling $76,987; the balance is currently $110,497.20. His income was $1,433.13 (2011), $7,639 (2012), $525 (2013), $4,382 (2014), $9,154 (2015) and $8,125 (2016). He owns no real estate and drives a 2010 Honda CR-V on which he pays $326 per month. On May 16, 2017 the Court granted his motion to reopen the case; a month later he filed this adversary proceeding seeking to discharge student loans under 11 U.S.C. §523(a)(8).

SUMMARY NUMBER: 34
PMF

KEY CODE SECTION(S): §§101(14A), 1322(a)
KEY TOPIC(S): Domestic Support Obligation

COURT and JUDGE: United States Court of Appeals, Tenth Circuit, Judge Bacharach

CASE NAME and CITE: *In re: Chamberlain;. Chamberlain v. Chamberlain.* 721 Fed.Appx. 826 (2018)

CASE NUMBER and DOCKET NUMBER: No. 17-1121

DATE DECIDED: February 20, 2018

NOTEWORTHY ISSUE: Whether an obligation to pay college expenses is a domestic support obligation.

HOLDING: Yes. The obligation to pay for a child's college education is a domestic support obligation. The obligation must meet four requirements. (1) It must be owed to or recoverable by a spouse or child or governmental unit.(2) It must be in the nature of alimony, maintenance, or support. (3) It must arise from a separation agreement, divorce decree, or property settlement agreement entered by a court of record or a lawful determination of a governmental unit. (4) It has not been assigned to a nongovernmental entity unless for collection purposes. The obligation to pay for the college education of the child met all the tests.

FACTS: Couple was divorced, and the obligation to pay for the college education was part of the marital settlement agreement.

SUMMARY NUMBER: 35 KEY CODE SECTION(S): §326(a), §330
KEY TOPIC(S): Employment of Professionals

COURT and JUDGE:	Tenth Circuit BAP; Nugent authors for Michael & Somers
CASE NAME and CITE:	In re Morreale; 2019 WL 287079
CASE NUMBER:	Case No. 13-27310; BAP Case No. CO-18-063
DATE DECIDED:	January 22, 2019

NOTEWORTHY ISSUE: Can a Trustee get commission income based on disbursements in a Chapter 7 case and also in the Chapter 11 case for the LLC owned by the Debtor?

HOLDING: No; the Bankruptcy Court is affirmed.

1. Trustees compensation is excluded from §330(a)(1); compensation is subject to §326.
2. §330(a)(7) states compensation to trustees is treated as a commission under §326.
3. Nothing in these statutes authorizes courts to award more than §326(a)'s maximum compensation to Chapter 7 trustees.
4. The phrase "in the case" in §326(a) is the key dispute.
5. Connolly was appointed in the Chapter 7 case, but not the Chapter 11 case. Therefore he cannot receive commission compensation for services in that case.
6. Connolly served as manager of the LLC, not Trustee, in the Chapter 11 case. That service did not bring LLC assets into the individual bankruptcy case. Absent employment as a professional or trustee, he is a volunteer.

FACTS:

Samuel Morreale organized, owned and managed a single member LLC, Morreale Hotels, LLC, which operated two properties in Denver. LLC filed a Chapter 11 petition in December of 2012. Morreale filed an individual Chapter 11 case that was converted to Chapter 7 in 2014. Tom Connolly was appointed trustee in the individual case; Morreale's ownership interest in the LLC was an estate asset of his individual bankruptcy estate. Connolly had himself appointed LLC manager, and proposed a plan of liquidation (rejecting the plan of reorganization the LLC had proposed) in the LLC Chapter 11 bankruptcy case. He sold the two LLC properties and disbursed sales proceeds to LLC creditors; surplus sales proceeds were paid into the Morreale estate. None of the pleadings addressed whether Connolly would be compensated for the LLC sales, he did not seek appointment as a professional or trustee in the Chapter 11 case. He filed an application in the Morreale case seeking commissions based upon disbursements from both cases; Morreale objected. Morreale's individual bankruptcy estate was a surplus estate, so Morreale had standing to object. The bankruptcy court limited Connolly's commission to the Chapter 7 disbursements; Connolly appealed.

SUMMARY NUMBER: 36
PMF

KEY CODE SECTION(S): §§ 327, 105
KEY TOPIC(S): Employment of Professionals

COURT and JUDGE: U.S. Bankruptcy Court, D. New Mexico. Judge Thuma

CASE NAME and CITE: *In Re: Victor P. Kearney, Debtor*

CASE NUMBER and DOCKET NUMBER: 17-12274-t11

DATE DECIDED: February 15, 2018

NOTEWORTHY ISSUE: When and under what circumstances will the employment of a professional relate back either to the date the application for employment is filed or before that date?

HOLDING: The employment of professionals will relate back to the date the application to be employed is filed. That is required because typically significant events occur prior to the notice period running and the opportunity for the hearing on the application. It would be prejudicial to the system if the debtor was without representation during that period.

The real issue in the dispute was whether the application will relate back prior to the date of the filing of the application to be employed. The court ruled it would relate back only under extraordinary circumstances, and such extraordinary circumstances were not present in this case. The employment only dated back to the date the application was filed.

Whether extraordinary circumstances exist will be determined considering the following four factors set out in *In re Arkansas Co., Inc.*, 798 F. 2d 1280 (5th Cir. 1983) together with two factors from *In re Twinton Properties Properties*, 27 B.R. 817 (Bk. M.D. Tenn. 1983):

1. Was the professional responsible for filing the application?
2. Was the professional under time pressure to begin service without approval?
3. How much delay was there after the professional learned that the application had not been filed?
4. Would granting *nunc pro tunc* relief prejudice third parties?
5. Does the party for whom the work was preformed approves the *nunc pro tunc* order?
6. Does the applicant exhibit any pattern of inattention or negligence in soliciting judicial approval for the employment of professionals?

The court added a requirement that the application would have been granted if timely filed.

The court rejected the other factors in *Twinton.*

FACTS: Lawyer filed an application for employment eight days after he had started working on the case. The application was actually to be employed taking direction from a chief

restructuring officer. The proposed CRO also filed an application to be employed. The application of the CRO was withdrawn after objections were filed, and the lawyer then sought to be employed directly by the debtor. The court noted that the application, as filed, would not have been granted. The court analyzed the factors by writing that it would more likely give leeway to a professional not familiar with bankruptcy than the applicant, there was some time pressure, but nothing extraordinary. The applicant was a large law firm. There was no inadvertence or ignorance that delayed the filing. The prejudice would be to the unsecured creditors if the applicant was paid for work at the direction of the CRO who was not retained. The client did not object. The court is not aware of a practice of inattention, even though perhaps in Texas where the applicant was from it may have been the practice to permit these applications. The applicant should have confirmed that such are unusual in the 10th Circuit.

SUMMARY NUMBER: 37

PMF

KEY CODE SECTION(S): §327(a), BR 2014(a)

KEY TOPIC(S): Employment of Professionals

COURT and JUDGE: U.S. Bankruptcy Court, D. New Mexico. Judge Thuma

CASE NAME and CITE: *In Re: Victor P. Kearney, Debtor*

CASE NUMBER and DOCKET NUMBER: 17-12274-t11, Doc. 628

DATE DECIDED: December 7, 2018

NOTEWORTHY ISSUE: Does the court have discretion to refuse to employ a lawyer if there is no conflict? What is the standard, if any, to be applied if there is discretion?

HOLDING: The court ruled that although it was unusual to deny retention of an attorney by the debtor, it had discretion to consider whether to approve the employment of a professional even if there was no conflict of interest. The employment must be in the best interests of the estate. The discretion must be exercised in a way that best serves the objectives of the bankruptcy system. The court denied the application to employ the professional because the lawsuit he was to be hired to pursue was without merit.

FACTS: The UCC proposed a plan of reorganization that provided that the trustees of the spendthrift trust in which the debtor was the income beneficiaries would take certain actions. The trustees of the debtor's spendthrift trust were to seek instruction from the state district court that had jurisdiction over the trust for a ruling on whether performing those actions would be a breach of fiduciary duty. The stay was lifted to allow the trustees to seek that ruling.

The day before the hearing in state court, the debtor made a flurry of filings, including removal from the state court and a suit in Nevada against the trustees. The bankruptcy was in New Mexico because the Schedules asserted he lived in New Mexico, and all filings had shown his New Mexico address. The suit asserted that the trustees violated their fiduciary duties by even thinking about taking the actions called for in the UCC Plan.

Prior to the ruling on the engagement of the lawyer, the state court ruled that the trustees were acting in accordance with their fiduciary duties in performing the actions called for in the UCC Plan.

The court noted that the debtor already had employed a number of lawyers and financial advisers. The suit was frivolous both because it was based on diversity (which J. Herrera had ruled was a frivolous claim) and on breach of fiduciary duty (which the state court had rejected).

SUMMARY NUMBER: 30
TDW

KEY CODE SECTION(S): §105; §362
KEY TOPIC(S): Equitable Powers; Automatic Stay

COURT and JUDGE: USBC DNM (J. Jacobvitz)

CASE NAME and CITE: *In re: Cheryl Lynne Maes*, 2018 WL 3655381 (B. Ct. D.N.M., 2018)
CASE NUMBER: Case No. 04-14871-j7 jointly administered with Case No. 12-13033-t7

DATE DECIDED: July 31, 2018

NOTEWORTHY ISSUE: Does the court have the authority under § 105(a) to reimpose the automatic stay after it terminates by operation of law?

HOLDING: No. No provision in the Code provides for or contemplates reimposing the stay after it is terminated. Section 105(a) does not allow a bankruptcy court to contravene explicit provisions of the Code. *Law v. Siegel*, 571 U.S. 415, 421 (2014) ("[W]hatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code.") "Reimposing the automatic stay upon reopening the bankruptcy cases would contravene the provisions of the Code governing the termination of the automatic stay and the protection afforded by the discharge injunction that replaces the automatic stay and therefore is not within the Court's authority under § 105(a)."

FACTS: Debtor was discharged in her first case in 2004 and was discharged in her second case in 2013. Debtor's Chapter 7 bankruptcy cases were reopened. Upon creditor's request, the cases were jointly administered. Debtor moved to re-impose the automatic stay under §105 to stay prosecution of a foreclosure action on appeal in state court and to stay an action to enforce a HOP (Homeownership Opportunities Program) Agreement pending in federal district court.

When the debtor is granted a discharge, the automatic stay terminates with respect to any act to collect a debt from the debtor other than from property of the estate. Code § 362(c)(2). When a Chapter 7 case is closed after the debtor is granted a discharge, the automatic stay also terminates with respect to acts to collect a debt from the debtor against property of the estate that is abandoned to the debtor upon the closing of the case. See Code §§ 362(c)(1) and 554(c).

In addition, when the debtor is granted a discharge, a discharge injunction goes into effect. Code § 524(a)(2). The discharge injunction replaces the automatic stay. The discharge injunction does not prevent a creditor with a lien against the debtor's property from taking action to enforce remedies against the property subject to the lien.

When a bankruptcy case is reopened, it does not vacate the discharge granted to the debtor or the discharge injunction. See Code §§ 350 and 727(d)-(e). The discharge injunction, instead of the automatic stay, continues to protect the debtor with respect to the debtor's personal liability for discharged debts. Code § 524.

SUMMARY NUMBER: 39 KEY CODE SECTION(S): n/a
KEY TOPIC(S): Exemptions

COURT and JUDGE: Tenth Circuit BAP (Nugent, Cornish, Mosier)

CASE NAME and CITE: Parr v. Rodriguez (in re Parr) 2018 WL 564572
CASE NUMBER: 15-14201; BAP No. CO-17-021
DATE DECIDED: February 26, 2018

NOTEWORTHY ISSUE: Should the Debtor's exemption be recognized?

HOLDING: Yes.

1. Colorado law recognizes an ownership interest in a self-settling trustee like Parr.
2. Colorado law provides that revocable trust assets are subject to the settlor's creditor claims.
3. Colorado law allows equitable interests in real estate absent legal title to support the claim of a homestead exemption.

Reversed and Remanded; the bankruptcy court can determine whether Parr occupied the property on the petition filing date, and whether or not he is elderly so as to get the increased exemption amount.

FACTS:

Larry Parr listed 2710 W. Union in Englewood Colorado (an unencumbered property) as his address; he did not hold legal title as he had transferred the property to a revocable living trust in 2001. He filed a bankruptcy, the Chapter 7 Trustee revoked the trust, and Parr claimed the property exempt as his homestead. The Trustee objected to the exemption, the Bankruptcy Court sustained the objection on grounds that under Colorado law, only individual owners and not trusts can occupy a homestead. Parr timely appealed.

The Trustee evicted Parr from the property in state court and moved for authority to sell the property in the bankruptcy court. He had a $1.4 million offer; Parr's exemption under Colorado law if allowed would have been $60,000, or if he was elderly, $90,000.

The record is incomplete; a transcript is missing; the BAP nonetheless proceeded.

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SUMMARY NUMBER: PMF

KEY CODE SECTION(S): NMSA §§35-12-7, 35-12-8

KEY TOPIC(S): Exemptions

COURT and JUDGE: United States Bankruptcy Court, D. New Mexico, Judge Jacobvitz

CASE NAME and CITE: *In re: Don Edward Johnson and Keiko Johnson, Debtors,* 593 B.R. 331 (2018)

CASE NUMBER and DOCKET NUMBER: No. 17-13247-j7

DATE DECIDED: October 17, 2018

NOTEWORTHY ISSUE: Whether the proceeds of wages which were not subject to garnishment are still exempt after receipt by the employee.

HOLDING: Once wages are deposited into the judgment debtor's bank account, they are protected only by the general exemption statutes rather than the wage garnishment exemption. To the extent they are not protected under the general exemption statute, they are property of the trustee.

FACTS: Debtor claimed cash in his bank account as exempt because the cash came from wages that were exempt from garnishment. The trustee objected to the exemption on that basis.

SUMMARY NUMBER: 41 KEY CODE SECTION(S): §522(b)(3)(B)
MKD KEY TOPIC(S): Exemptions

COURT and JUDGE: 10th Circuit; J. Eid authors for Kelly & O'Brien
CASE NAME and CITE: Jennings v. Royal (In re Royal); 739 Fed.Appx. 505
CASE NUMBER: 10th Cir. Case No. 17-8095
DATE DECIDED: September 14, 2018

NOTEWORTHY ISSUE:

Can Debtor claim his equity in land held as a tenant by the entireties exempt?

HOLDING:

Only to the extent his entireties interest exceeds the joint debt of he and his spouse.

1. §522(b)(3)(B) allows the exemption of entireties interests if they are exempt under nonbankruptcy law.
2. Entireties property is not exempt from claims against both spouses under Wyoming law; it is exempt from claims against only one spouse.
3. The IRS debt and credit card debt are joint debts; Wyoming law prevents the exemption against the claims of joint creditors.

The opinion is poorly written; there is no clear discussion of the pragmatic details of the liquidation. The Court ruled the Trustee can sell the house, pay the mortgage, pay closing costs, pay the claims of joint creditors, and any surplus goes to the Debtor (either because it is exempt or because it is a surplus).

FACTS:

Jennings filed Chapter 7 in December of 2010. He owned residential real property in Casper, Wyoming with his non-filing spouse as tenants by the entireties. He valued his entireties interest at $150,000; (half the property value), subject to a lien of $130,000. He scheduled joint debts owed by him and his spouse as $116,000 to the IRS and $13,000 in credit cards. He claimed the entireties property exempt. His Trustee objected and sought to sell the property and determine proceeds in an adversary proceeding.

Bankruptcy Court ruled that Austin Jennings may claim an exemption in his entireties interest in Wyoming real estate, but only to the extent that his joint entireties interest exceeds the joint indebtedness of Jennings and his nonfiling spouse. Jennings appealed, the BAP affirmed.

Luckily we don't see a lot of entireties questions here in New Mexico.

SUMMARY NUMBER: 42 KEY CODE SECTION(S): §546(e)
MKD KEY TOPIC(S): Fraudulent Transfer

COURT and JUDGE: US Supreme Court; J. Sotomayor authored a unanimous Court
CASE NAME and CITE: Merit Mgt. v. FTI Consulting; 138 S.Ct. 883
CASE NUMBER: 200 L.Ed.2d 183, 86 USLW 4088, 65 Bankr.Ct.Dec.92
DATE DECIDED: February 27, 2018

NOTEWORTHY ISSUE:

Does the securities safe harbor contained in §546(e) require courts to look to the specific transfer to be avoided or to any component parts of the overarching transfer?

HOLDING:

Only the specific transfer the Trustee seeks to avoid. Possible transfers to examine:
1. Credit Suisse to Citizens's Bank, $16.5 million into escrow.
2. Citizen's Bank to Merit (2 installments totaling $16.5 million).
3. Valley View to Merit transfer (stock for $16.5 million).

The securities safe harbor was enacted after a bankruptcy trustee avoided $12 million in margin payments made by a bankrupt commodity broker to a clearing association as constructively fraudulent. Congress has expanded the safe harbor over the years to include financial institutions, stockbrokers and security clearing agencies.

We ignore the financial institution transfers; Merit sold stock to Valley View, and that is the transfer the Trustee seeks to set aside. That transfer was not made by, to or for the benefit of a financial institution; the securities safe harbor provision has no application.

FACTS:

During 2003 two companies (Valley View and Bedford Downs) competed for the last harness racing license in Pennsylvania. With the license they hoped to open a "racino". Both applications were denied, the parties settled whereby Valley View would buy Bedford's stock after acquiring the license. Credit Suisse financed the $55 million purchase; funds were escrowed at Citizen's Bank. One of Bedford's shareholders was the debtor, Merit Management Group, LP. Merit got $16.5 million for its Bedford stock.

Valley View failed to get a gaming license and filed Chapter 11; a plan was confirmed appointing FTI Consulting as trustee of the Centaur litigation trust. FTI sued Merit to avoid the stock purchase as constructively fraudulent. Merit defended with the securities safe harbor because the transaction was a settlement payment made by or to a covered financial institution (Credit Suisse & Citizen's Bank). Merit prevailed, the US District Court affirmed, the Seventh Circuit reversed (ruling the financial institutions were mere conduits) and the Supremes granted certiorari to resolve a circuit conflict.

SUMMARY NUMBER: 43
JAA

KEY CODE SECTION(S): Sec. 548(a)(1)(B)
KEY TOPIC(S): Fraudulent Transfer

COURT:	USBC-NM
JUDGE:	David T. Thuma
CASE NAME:	Montoya v. Lieberman (In re: Santa Fe Medical Group, LLC)
CITE:	Doc. No. 75
CASE NUMBER:	Adv. Proc. No. 16-01051-t; Bankr. No. 15-11247-t
DATE DECIDED:	January 4, 2018

NOTEWORTHY ISSUE: In a constructively fraudulent transfer case, did the Debtor receive reasonably equivalent value? Was the Debtor insolvent at the time of the transfers, or rendered insolvent by the transfers?

HOLDING: The Debtor did not receive value for the transfers it made and was also insolvent during most of the relevant time period.

FACTS and DISCUSSION: Prepetition, the Debtor's principal and defendant settled a dispute over the defendant's employment with the Debtor. Under the settlement, Debtor would pay the defendant $25,000 per month for 60 months. The problem is that none of the consideration given by defendant for the payments went to the Debtor. It went instead to Debtor's principal. What the defendant gave the principal was a right to receive future profits and his interest in the Debtor. Had these things gone to the Debtor instead, there could have been a finding of reasonably equivalent value.

In this case, the Trustee hired an expert witness, who testified to the Debtor's insolvency. The Defendant had no expert. To find insolvency, the Judge had to resolve several close fact issues. The result could possibly have been different had the defendant had his own expert.

SUMMARY NUMBER: 44
TDW

KEY CODE SECTION(S): §548
KEY TOPIC(S): Fraudulent transfers

COURT and JUDGE: USBC DNM (Jacobvitz)

CASE NAME and CITE: *Gonzales v. Sexton (In re Esquibel)*, 2018 WL 3570592 (Bankr.D.N.M., 2018)

CASE NUMBER: Case No. 17-10498-j7; Adversary Pro. No. 17-1042-j

DATE DECIDED: July 23, 2018

NOTEWORTHY ISSUES:
(1) When is real property transferred for purposes of a fraudulent transfer action? When the deed is signed and notarized or, when the deed was recorded in the county clerk's office?
(2) Does the promise of a defendant in a fraudulent transfer action, to maintain property, allow debtor to live rent-free, and to care for the Debtor, constitute value under § 548?

HOLDINGS:
(1) For purpose of a fraudulent transfer action under Code § 548, property was transferred when the deed was recorded in the county clerk's office.
(2) No, the promise to care for the debtor does not constitute value. "The Code defines value in the context of fraudulent transfers as property, or satisfaction or securing of a present or antecedent debt of the debtor, but does not include an unperformed promise to furnish support to the debtor or to a relative of the debtor." Code § 548(d)(2). The promise to allow debtor to live rent free may have value, particularly if such an oral "lease" is enforceable under the statute of frauds. But, evidence of value of such an agreement was not presented at this summary judgment stage.

FACTS:

Debtor owned real property free of liens in Santa Rosa, New Mexico. On May 19, 2014, debtor executed a quitclaim deed, which was notarized, deeding the property to the defendant, debtor's brother. In exchange for the property, defendant promised debtor: to maintain the property; to provide debtor with a rent-free place to live for so long as she is able to live independently; and, to care for debtor in defendant's home should debtor become unable to care for herself.

Almost 28 months later, on September 7, 2016, 177 days before debtor filed bankruptcy, defendant recorded the quitclaim deed. Debtor filed Chapter 7 on March 3, 2017. Debtor liabilities exceeded her assets according to her schedules. Trustee filed Adversary Proceeding against defendant to avoid the transfer of the property as a fraudulent transfer. Trustee filed a motion for summary judgment, which the court granted in part and denied in part.

SUMMARY NUMBER: 45 KEY CODE SECTION(S): §523(a)(2)(C)
KEY TOPIC(S): Judicial Estoppel

COURT and JUDGE: NM Bankruptcy Court; Robert H. Jacobvitz
CASE NAME and CITE: Kirtland FCU v. Shaw (in re Shaw); 2018 WL 1614156
CASE NUMBER: 17-11646 j7; Adv. No. 17-1072 j
DATE DECIDED: March 30, 2018

NOTEWORTHY ISSUE: Should the Debtor's affirmative defenses be stricken?

HOLDING: No.

1. Rule 12(f) allows the striking of affirmative defenses, but only if the motion to strike is filed within 21 days of service of the pleading. KFCU's motion to strike was filed late.
2. A defense may be stricken if it is insufficient as a matter of law.
3. Debtor offers facts that could rebut the presumption of nondischargeability under §523(a)(2)(C). If the car dealer rather than Debtor filled out the credit application, if the Debtor could have afforded the payment he was quoted but not the ultimate payment the loan required, there may be no fraudulent intent.
4. Judicial estoppel would prevent Debtor from suing the dealer without disclosing the cause of action, but would not prevent Debtor from asserting these affirmative defenses which go to his state of mind in purchasing the vehicle.

FACTS:

Dylan Shaw purchased a car shortly before filing bankruptcy. He did not schedule the vehicle loan on Schedule D or a cause of action for fraud against the car dealer who allegedly pressured him into buying the car on Schedule B. He later attempted to amend his schedules to list the creditor and the cause of action but the Court refused to reopen the case for that purpose.

Kirtland FCU filed an adversary seeking to prevent Shaw from discharging the debt pursuant to §523(a)(2)(C) (which targets luxury goods or services incurred within 90 days of the bankruptcy petition filing date as presumptively nondischargeable). Shaw answered, and asserted he was the victim of high pressure sales tactics (salesman misstated the car payment amount and kept Shaw's car away from him). KFCU filed a motion to strike the answer or disallow affirmative defenses on grounds Shaw hadn't disclosed any claims against the car dealer on his Schedule B.

SUMMARY NUMBER: 46
TDW

KEY CODE SECTION(S):
KEY TOPIC(S): Unclaimed Funds; Jurisdiction; Structured Settlements

COURT and JUDGE:

CASE NAME and CITE: In re: Dee's Foodservice Abq Inc., 2018 WL 3025284 (Bankr. D.N.M., 2018)

CASE NUMBER: Case No. 16–11560

DATE DECIDED: June 15, 2018

NOTEWORTHY ISSUE: Where a chapter 11 case ends in a "structured dismissal" does the court have jurisdiction over claims to unclaimed funds?

HOLDING: No. Claims to unclaimed funds following a structured dismissal of a chapter 11 case do not arise under title 11, or in a case under title 11, are non-core, and are not subject to bankruptcy court jurisdiction after dismissal of the chapter 11 case where no plan is confirmed.

FACTS: Debtors' chapter 11 bankruptcy case ended in a "structured dismissal" following sale of debtors' assets under Code §363 and subsequent approval of debtors' motion for order determining claims against the debtors, authorizing disbursement of funds to creditors, and dismissing the debtors' cases. The United States Trustee objected to the motion to the extent it did not seek to provide for the deposit of unclaimed funds in the Court's unclaimed funds registry after dismissal. The Court overruled the objection because the Court did not have jurisdiction over claims to unclaimed funds where the claim arises after dismissal of the chapter 11 case in which no plan has been confirmed.

The court's determination that it did not have jurisdiction over claims to unclaimed funds after dismissal turned on the fact that such claims are "noncore." After a bankruptcy case is dismissed, the Court retains jurisdiction over certain core proceedings. Core proceedings are matters "arising under title 11, or arising in a case under title 11." See 28 U.S.C. § 157(b)(1). "Core proceedings are proceedings which have no existence outside of bankruptcy."

Non-core proceedings are those that "do not depend on the bankruptcy laws for their existence and which could proceed in another court ..." *Gardner v. United States (In re Gardner)*, 913 F.2d 1515, 1518 (10th Cir. 1990) (per curiam) (citation omitted).

"In a structured dismissal where a plan is not confirmed, claims to unclaimed funds only arise after the case is dismissed and are not governed by any provision of the Bankruptcy Code." As such, claims to unclaimed funds do not arise in a case under Title 11 or arise under Title 11 and are therefore noncore.

A bankruptcy court can retain jurisdiction following dismissal of the underlying bankruptcy

case over noncore, related proceedings commenced before bankruptcy case dismissal, although ordinarily noncore, related proceedings are also dismissed upon dismissal of the bankruptcy case. *In re Johnson*, 575 F.3d 1079, 1083 (10th Cir. 2009). A bankruptcy court does not have jurisdiction over noncore proceedings first commenced after dismissal of the underlying bankruptcy case.

Unsuccessful distributions of funds to creditors result in "unclaimed funds." In a structured dismissal, distributions to creditors occur after the case is dismissed. Therefore, claims to unclaimed funds necessarily arise after dismissal, and do not arise in a case under Title 11.

Further, in a chapter 11 case in which no plan is confirmed Title 11 does not govern claims to unclaimed funds. The Code sections that govern unclaimed funds (§§ 347(b) and 1143) in connection with a chapter 11 case apply only if a plan is confirmed. Those sections do not apply to claims for unclaimed funds following a structured dismissal of a chapter 11 case.

SUMMARY NUMBER: 47

PMF

KEY CODE SECTION(S): 28 U.S.C. § 1334; 28 U.S.C. § 1367

KEY TOPIC(S): Jurisdiction, Summary Judgement

COURT and JUDGE: United States Bankruptcy Court, D. New Mexico, Judge Thuma

CASE NAME and CITE: *In re: Marvis Wynn, Debtor, Marvis Wynn and Cobb Wynn, v. Innovations Credit Union.*

CASE NUMBER and DOCKET NUMBER: Adversary No. 17-01089-t, Doc. 33

DATE DECIDED: October 15, 2018

NOTEWORTHY ISSUE: Whether the bankruptcy court had subject matter jurisdiction over non-debtor claims or should exercise supplemental jurisdiction, and whether summary judgment would be granted to the defendant when the plaintiff failed to present contrary evidence.

HOLDING: The court independently considered its subject matter jurisdiction and concluded it did not have jurisdiction over a claim by the non-filing spouse against the lender. It further declined to exercise its discretion to exercise supplemental jurisdiction. It concluded that since it would dismiss the claim of the debtor by granting summary judgment (no response having been filed opposing summary judgment), it would not exercise supplemental jurisdiction over the remaining claim.

FACTS:

Marvis Wynn filed bankruptcy, but Cobb Wynn did not. They jointly filed an adversary proceeding to assert claims against a lender. The lender moved for summary judgment asserting facts in support. Marvis Wynn did not respond or controvert the facts presented, so the court entered summary judgment against him. Because Cobb Wynn was not a debtor, the court concluded it did not have subject matter jurisdiction over her claims and because it was dismissing Marvis' claims on summary judgment, it should decline to exercise supplemental jurisdiction over her claims.

SUMMARY NUMBER: 48
JAA

KEY CODE SECTION(S): Sec. 522(f)(2)(A)
KEY TOPIC(S): Lien Avoidance, Statutory Interpretation

COURT:	USCA 10th Cir.
JUDGE:	Carlos F. Lucero
CASE NAME:	Sandoval Irrevocable Trust v. Taylor (In re: Taylor)
CITE:	899 F.3d 1126
CASE NUMBER:	No. 17-1241
DATE DECIDED:	August 14, 2018

NOTEWORTHY ISSUE and HOLDING: A debtor may avoid judicial liens that impair the homestead exemption. Sec. 522(f) has a formula to determine the extent to which an exemption is impaired. The issue is how the formula applies to a homestead exemption when a home is jointly owned with a non-debtor. Based on the plain language of § 522(f) the Tenth Circuit concluded that the impairment calculation must use the value of other liens on the home corresponding to the debtor's percentage of ownership, rather than the full amount of the liens.

FACTS and DISCUSSION: A Colorado Debtor owned 50% of his home and his non-debtor ex-wife owned the other 50%.

The Debtor scheduled the value of the home at $560,000, with his interest at $280,000. The defendant had recorded judgment liens of $461,472.86. It had an appraisal valuing the home at $962,000. Debtor was entitled to a homestead exemption of $37,500 under Colorado law. The home also had other consensual liens and tax liens.

In applying the lien-impairment formula to determine the extent to which judicial liens impair a homestead exemption, bankruptcy courts must interpret the statutory term "all other liens on the property" as referring to all other liens on Debtor's one-half interest in property, and to extent that a lien encumbered property as whole, to include only one-half of amount of that lien when calculating extent of exemption impairment.

The focus of the statute is the on the Debtor's interest. "Thus, only that part of a lien which actually interferes with the debtor's homestead exemption may be avoided." If we read the term "property" in § 522(f)(2)(A)(ii) to refer to the debtor's interest, rather than the undivided whole parcel, Congressional intent is effectuated."

The Tenth Circuit overruled two earlier Colorado cases in reaching this result.: *In re Cozad*, 208 B.R. 495 and *In re Biesterveld*, 2008 WL 5157700.

SUMMARY NUMBER: 49
TDW

KEY CODE SECTION(S): 523(a)(2)
KEY TOPIC(S): Non-dischargeability

COURT and JUDGE: Supreme Court of the United States, J. Sotomayor (Justices Thomas, Alito, and Gorsuch joined in part)

CASE NAME and CITE: *Lamar, Archer & Cofrin, LLP v. Appling*, 138 S.Ct. 1752 (2018)

CASE NUMBER: No. 16–1215

DATE DECIDED: June 4, 2018

NOTEWORTHY ISSUE: Was debtor's oral statement to his lawyers that he was expecting a tax refund of approximately $100,000, which was enough to cover his owed and future legal fees, a "statement respecting the debtor's . . . financial condition" for purposes of non-dischargeability analysis under § 523(a)(2)(B)?

HOLDING: Yes. The Court held that a statement regarding a specific asset can be a "statement respecting the debtor's . . . financial condition" under § 523(a)(2)(B). The Court explained that the use of the word "respecting" in the legal context generally has a broadening effect. The Court also stated that the statute's legislative history supported its reading.

ANALYSIS: Code §523(a)(2) prohibits debtors from discharging debts for money, property, services, or credit obtained by "false pretenses, a false representation, or actual fraud," 11 U.S.C. § 523(a)(2)(A), or, if made in writing, by a materially false "statement ... respecting the debtor's ... financial condition," § 523(a)(2)(B).

The Supreme Court said "This case is about what constitutes a "statement respecting the debtor's financial condition." Does a statement about a single asset qualify, or must the statement be about the debtor's overall financial status?" The false statements at issue in this case "concerned a single asset and were made orally. So, if the single-asset statements here qualify as 'respecting the debtor's financial condition,'" § 523(a)(2)(B) does not prevent discharge because they were not made in writing. "If, however, the statements fall into the more general category of 'false pretenses, ... false representation, or actual fraud,' § 523(a)(2)(A), for which there is no writing requirement, the associated debt will be deemed nondischargeable."

The statutory language makes plain that a statement about a single asset can be a "statement respecting the debtor's financial condition." If that statement is not in writing, then, the associated debt may be discharged, even if the statement was false.

FACTS: Debtor hired the Lamar law firm to represent him against the former owners of his business. Debtor incurred significant legal fees, and verbally told Lamar that he would be able to pay them after he received a sizeable tax refund that he was expecting. In reliance upon this statement, the firm continued to represent him through the conclusion of the litigation. Debtor received a tax refund, though it was smaller than what he had told Lamar he was anticipating,

and he put it into his business rather than paying Lamar. Lamar obtained a judgment against Debtor, and Debtor subsequently filed for bankruptcy. Lamar initiated an adversary proceeding to collect the debt, and the bankruptcy court ruled that the amount was not dischargeable pursuant to 11 U.S.C. § 523(a)(2)(A) because Lamar had justifiably relied upon Debtor's fraudulent statements. The district court affirmed.

The 11th Circuit reversed and remanded. Noting a circuit split on how to construe the statute at issue, the court explained that because Debtor's fraudulent statements about his tax refund were not in writing and qualified as statements "respecting [his] . . . financial condition" under § 523(a)(2)(B), the debt could be discharged.

SUMMARY NUMBER: 50 KEY CODE SECTION(S): §523(a)(2)
MKD KEY TOPIC(S): Nondischargeability

COURT and JUDGE: NM Bankruptcy Court; David T. Thuma
CASE NAME and CITE: O'Brien v. Montoya;
CASE NUMBER: Case No. 7-17-11823 TA; Adv. No. 17-1080 t; Docket No. 22.
DATE DECIDED: May 4, 2018

NOTEWORTHY ISSUE:

1. Has Plaintiff stated a claim sufficient to survive a Rule 12(b)(6) motion; specifically must money obtained by fraud come from the creditor?

HOLDING:

1. Plaintiff states a claim; motion denied. Rule 12(b)(6) tests the sufficiency of a complaint. It must state a claim for relief that is plausible on its face. The Court must assume the truth of the facts in the pleading, take them in the light most favorable to Plaintiff, and assess whether they give rise to a reasonable inference that the Defendant is liable under applicable law. Since the Supreme Court in ***Cohen v. de la Cruz*** 523 U.S. 213 (1998) decoupled the amount of the debt surviving discharge from the amount of money arising from the fraud (all damages survive discharge even if they don't arise directly from the fraud), the Code does not require that the money obtained by fraud come from the creditor.

FACTS:

Debtor (a suspended attorney) filed a police brutality suit in US District Court on behalf of a client. By mislabeling defendants, failing to serve defendants and eliciting false testimony Debtor got his client a large default judgment against O'Brien, a former Santa Fe County sheriff who had shot his client in an armed confrontation. Years later O'Brien learned of the judgment, got it set aside and the County settled with the estate of Montoya's now deceased client. O'Brien sued for malicious process, won a six figure summary judgment which Montoya appealed and was remanded to review Montoya's statute of limitations defense. After remand Montoya filed bankruptcy on the eve of trial in state court. O'Brien filed an adversary proceeding to except his claims from Montoya's discharge under §523(a)(2) and §523(a)(6). Montoya moved to dismiss the §523(a)(2) fraud claim.

Last year we reviewed Judge Thuma's ruling that to state a claim under §523(a)(2), a plaintiff must allege that the defendant received a benefit from the plaintiff (problematic under these facts). This opinion retreats from that ruling and agrees with ***In re Thompson***555 B.R. 10, 12 (10th Cir. BAP 2016) that "...there is no requirement that the debt be for something the debtor obtains from the creditor."

A pretty technical ruling, but it may come in handy to those defending adversaries.

SUMMARY NUMBER: 51
JAA

KEY CODE SECTION(S): Sec. 547(e)
KEY TOPIC(S): Preference

COURT:	10th Cir. BAP
JUDGE:	Robert H. Jacobvitz
CASE NAME:	Walters v. Cates (In re: Diann Marie Cates)
CITE:	588 B.R. 916
CASE NUMBER:	BAP No. CO-17-047; Bankr. No. 15-18969; Adv. No. 16-1202;
DATE DECIDED:	August 24, 2018

NOTEWORTHY ISSUE: When does a "transfer" occur for purposes of a preference?

HOLDING: Under Colorado law, a transfer occurs and is perfected on the date the deed of trust is recorded, regardless of whether debtor, as opposed to her revocable self-settled family trust, held any rights in the underlying property.

FACTS and DISCUSSION: The facts are convoluted. Three years before filing bankruptcy, the Debtor gave a note for $135,000 and a deed of trust to a creditor. The deed of trust was not recorded at the time. A little later, on January 24, 2013, the Debtor created a revocable trust under which she was the settlor, trustee, and sole beneficiary. She deeded the property in question to the trust on February 4, 2013. The creditors finally recorded the deed of trust on March 4, 2013. Shortly before filing her petition in August of 2015, the Debtor made the trust deed the property back to herself. The bankruptcy trustee argued that the deed of trust first attached to the property just before bankruptcy was filed, when the Debtor regained title to the property, and thus the "transfer" occurred then. The creditor argued that the "transfer" occurred when they recorded their deed of trust, even though the Debtor did not own the property that day.

Under Colorado law, the Debtor's transfer under the deed of trust was perfected, for preference purposes, on date the deed of trust was recorded. This is so regardless of whether debtor or her revocable trust held rights in the property. The transfer did not occur on later recording date of quitclaim deed when the Debtor got the property back from the trust. The Debtor owned property when she granted deed of trust. The executed but unrecorded deed of trust created lien against property which attached on date that deed of trust was executed. On the date that deed of trust was recorded, a bona fide purchaser of the property from Debtor could not acquire an interest that was superior to transferees' interest, as the existence of the quitclaim deed from Debtor to the trust was in the chain of title and was an "irregularity," providing bona fide purchaser constructive notice of deed of trust.

SUMMARY NUMBER: 52 KEY CODE SECTION(S): §507(a)(8)(E)
MKD KEY TOPIC(S): Priority Tax Debt

COURT and JUDGE: NM Bankruptcy Court; Robert H. Jacobvitz
CASE NAME and CITE: Sandia Tobacco Manufacturers, Inc.; 2018 WL 4964295
CASE NUMBER: Case. No. 11-16-12335 JA; Docket No. 385.
DATE DECIDED: October 12, 2018

NOTEWORTHY ISSUE:

Is USDA's claim entitled to priority status under §507(a)(8)(E)?

HOLDING:

Yes. FETRA assessments are excise taxes entitled to priority. The Code doesn't define excise taxes; the 10th Circuit uses the ***Chateaugay/Lorber*** test to determine whether something is the functional equivalent of a tax entitled to priority. Elements:

1. An involuntary pecuniary burden laid upon individuals or property;
2. Imposed by or under the authority of the legislature;
3. For public purposes, including defraying expenses of government or authorized undertakings;
4. Under the police or taxing power of the state;

Petition date is 9/16/16; priority status is limited to FETRA assessments within 3 years of the petition filing date. Quarterly FETRA assessments are based on the date the product is removed from inventory, not the date of the USDA invoice or the invoice's due date. The only priority invoices are those dated December 2013 to December 2014.

The assessments are involuntary, imposed by Congress, for public purposes, and imposed by Congress under its taxing power.

The public purpose prong is the most litigated prong of the test. Every statute should serve some public purpose. Taxes are distinguished from penalties, however; tax provides for the support of government, whereas a penalty is an exaction imposed by statute as punishment for an unlawful act. Look to the principal purpose of the legislature even if there are other incidental purposes. If purpose is to pay for a benefit provided to a private party payer or enforce a private obligation, then no priority. 10th Circuit ruled 10% exaction on premature withdrawal of pension funds is a penalty, did not compensate for pecuniary loss. Pension Benefit Guaranty Corporation claims for unpaid minimum contributions to pensions is not a tax, it funds a private obligation not a public purpose (really?). Coal Act pension contributions, however, were public purpose taxes entitled to priority. Those two cases conflict!

FETRA assessments do benefit private parties (tobacco farmers), but in compensation for loss of the quotas and price supports they previously received. FETRA is not a penalty, and not

imposed to penalize unlawful acts. The assessments aren't payment for a service that benefitted manufacturers. The principal purpose of FETRA is public.

FACTS:

Debtor is a corporation founded in 2003. The company manufactured tobacco products, rendering it subject to the Fair and Equitable Tobacco Reform Act of 2004 (FETRA). FETRA makes the company subject to assessments starting in 2004 to fund USDA payments to tobacco farmers intended to stabilize the tobacco industry. FETRA was enacted to end Depression era tobacco subsidies and quotas, transition tobacco farmers to the free market and recoup the cost of the program by levying assessments on manufacturers and importers. Decreased tobacco use made the existing quota system economically unsustainable for tobacco farmers. Without a transition, however, production could skyrocket and prices thereby plummet. The assessments on manufacturers were based on market share, and required manufacturers to report sales volume to USDA.

Debtor made payments on assessments through 2008, partial payments until 2009, and thereafter paid nothing. Assessments continued through December of 2014.

The company filed a Chapter 11 bankruptcy in September of 2016. USDA filed a priority claim of $4.7 million for FETRA assessments and interest.

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SUMMARY NUMBER: KEY CODE SECTION(S): §363(j), §541 & §726(c)(2)
KEY TOPIC(S): Property of the Estate

COURT and JUDGE: NM Bankruptcy Court; Robert H. Jacobvitz

CASE NAME and CITE: In re Jackson; 2018 WL 3763249

CASE NUMBER: 16-12666 j7; Docket No. 104

DATE DECIDED: August 7, 2018

NOTEWORTHY ISSUE: Is the Debtor's non-filing spouse a creditor?

HOLDING: No. Her claim is disallowed.

1. Opal Jackson's claim is actually a claim by a co-owner to sales proceeds, not a true pre-petition proof of claim. Co-owner claims are covered under §363(j).
2. The bankruptcy estate includes all community property under §541(a)(2); Ms. Jackson is therefore *not* a co-owner under §363(j) as the estate owns her interest in the Nevada Condo.
3. She may apply for proceeds if there is a surplus in the estate after all community claims are paid in full, as set forth in §726(c)(2). After payment of administrative expenses and community claims the non-filing spouse may be entitled to the remaining proceeds of community property [unlikely with a $695,000 claim].

FACTS:

David Jackson filed a Chapter 7 bankruptcy October 28, 2016. He married Opal Jackson (his non-filing spouse) in 1967. They are separated but still married. Ms. Jackson worked for Walmart from 1985 until 2018, accruing a retirement account in the process. The parties jointly purchased real property known as the Nevada Condo in 2015. Opal Jackson filed a $40,000 proof of claim on March 29, 2018 as Claim No. 8, seeking to recover $40,000 she contributed to the acquisition of the Nevada Condo, which David Jackson's Trustee in Bankruptcy sold for $125,000. All funds contributed by Ms. Jackson to the purchase of the Nevada Condo came from her Walmart retirement accounts.

The original claims bar date was July 3, 2017; this was extended to April 30, 2018. TRD filed a $695,000 claim arising out of the operation of a business. The Trustee objected to Ms. Jackson's claim as untimely, because the Nevada Condo was community property that became bankruptcy estate property without the need to pay a co-owner, and because the documents attached to the claim fail to demonstrate those funds were used to improve the Condo.

SUMMARY NUMBER: 54 KEY CODE SECTION(S): 11 USC §541
KEY TOPIC(S): Property of the Estate

COURT and JUDGE: Tenth Circuit Court of Appeals (McHugh, Briscoe & Murphy)

CASE NAME and CITE: Cohen v. Chernushin (In re Chernushin), 911 F.3d 1265

CASE NUMBER: Tenth Circuit Case No. 18-1068

DATE DECIDED: December 21, 2018

NOTEWORTHY ISSUE: Is the second home bankruptcy estate property?

HOLDING: No. The bankruptcy estate had no more interest in the home than Mr. Chernushin had; since Mr. Chernushin's interest in the home extinguished when he died, the bankruptcy estate has no interest in the home and cannot sell it. Property interests are defined by state law.

FACTS:

Mr. Chernushin filed a Chapter 13 case on August 17, 2015 without his wife. He listed two real properties; a primary residence not at issue in this appeal and a second home. Both were owned in joint tenancy with right of survivorship. Mr. Chernushin exempted the primary residence but not the second home. A month later he converted to Chapter 7; Mr. Cohen was appointed Chapter 7 Trustee.

Mr. Chernushin committed suicide June 9, 2016. Mr. Cohen sued Ms. Chernushin, seeking authorization to sell the second home. The Bankruptcy Court granted summary judgment to the non-filing spouse, the U.S. District Court affirmed.

As in New Mexico, under Colorado law a joint tenant's interest in real property continues free of the deceased joint tenant's interest after his death. The sole surviving joint tenant becomes the sole owner of the property upon the death of the other tenant.

SUMMARY NUMBER: 65
TDW

KEY CODE SECTION(S): Rule 15
KEY TOPIC(S): Amendments to pleadings

COURT and JUDGE: USBC DNM (Thuma)

CASE NAME and CITE: *Franco v. Franco (In re Franco)*, Adv. No. 16-1074, Doc. No. 54 (Bankr. D.N.M., 2018) (October 3, 2018)

CASE NUMBER: Adv. No. 16-1074

DATE DECIDED: October 3, 2018

NOTEWORTHY ISSUES: Would amended complaint be permitted to assert slander of title claim where facts supporting amended claim were known or should have been known before the original complaint was filed and where proposed amended claim was time-barred and, therefore, permitting the amendment would be futile?

HOLDINGS: No. Motion to amend and vacate was denied. Essentially, the court treated the motion as one to reconsider the state court's order dismissing the disparagement of title count and to permit filing the same claim with a different name.

FACTS:
Debtor and husband acquired 240 acres of land in 1969 in Eddy County, including a half interest in mineral rights. In 1996, they conveyed 122 acres of the land to their son, Hipolito, as his sole and separate property (the "Property"). Husband died. Hipolito died. Hipolito's widow, Carla, and debtor dispute who owns the mineral rights associated with the Property, each relying on different documents and events to support their claims.

Debtor filed a chapter 7 case in 2003, and a second chapter 7 case in 2013. She received a discharge in each case. The latter case was closed on December 30, 2013. No mineral rights were listed in the bankruptcy schedules in either case.

In 2014, Hipolito and Carla filed a state court lawsuit to quiet title to the Disputed Mineral Rights; for damages for disparagement of title; and for injunctive relief. On motion and after a hearing, in April 2015, the state court dismissed the disparagement of title count. Under New Mexico law, slander of title occurs when one willfully and maliciously records or publishes matter which is untrue and disparaging to another's property rights in land. In her original complaint filed in state court, Carla did not allege malice, which is an essential element of a slander of title claim.

More than a year later, in May 2016, Carla filed a Motion for Leave to Amend Pleadings and Motion to Vacate Order of Dismissal (as amended, the "Motion to Amend and Vacate"). Defendants responded. Plaintiff did not reply. In March 2018, the Court ordered Carla to amend the motion and attach the proposed amended complaint. This Motion to Amend and Vacate is before the court in this opinion.

The bankruptcy cases were reopened in June 2016. A notice of bankruptcy and automatic stay was filed in the state court action in August 2016. Carla filed a proof of claim in the bankruptcy case in October 2016, asserting a claim of $667,620 (the "Claim") secured by the Disputed Mineral Rights. In December 2016, Carla removed the State Court Action to the bankruptcy court.

In February 2017, Carla filed a motion for *nunc pro tunc* relief from the automatic stay, or for a ruling that the stay did not apply, to the state court's entry of a quiet title judgment in the State Court Action. In July 2017, the court denied the stay relief motion and ruled that the ownership of the Disputed Mineral Rights was a matter of bona fide dispute.

The Motion to Amend and Vacate requested that the court reconsider the state court's order dismissing the disparagement of title count. The dismissal order is an interlocutory order which may be reconsidered at any time and modified in the court's discretion. As such, it is not a bar to the motion to amend.

The motion to amend is governed by Rule 15(a). Untimeliness is grounds to deny a motion to amend. Here Carla waited 13 months after dismissal to ask to amend. Courts have denied motions to amend where the party seeking leave to amend knew, or should have known, the facts upon which the proposed amendment was based but failed to plead them. In the proposed amended complaint, Carla alleges acts that allegedly show malice. All of the acts occurred before the original complaint was filed in 2014.

Courts deny motions to amend as futile if the pleading as amended would be subject to dismissal. New Mexico has a four-year statute of limitations on slander of title actions. In actions for injuries to property, "the cause of action shall not be deemed to have accrued until the . . . injury . . . shall have been discovered by the party aggrieved." The court found that Hipolito and Carla had actual notice of a potential slander of title claim beginning in August 1998 and again in January 2001, when Hipolito had notice of information underlying the dispute about the mineral rights.

SUMMARY NUMBER: 56
PMF

KEY CODE SECTION(S): BR 7054(b)
KEY TOPIC(S): Reconsideration

COURT and JUDGE: United States Bankruptcy Court, D. New Mexico, Judge Jacobvitz

CASE NAME and CITE: *In re: Otero County Hospital Association (United Tort Claimants v. Quorum Health Resources, LLC)* 585 B.R. 161 (2018)

CASE NUMBER and DOCKET NUMBER: Adversary No. 13-00007

DATE DECIDED: March 8, 2018

NOTEWORTHY ISSUE: Will the court reconsider an interlocutory order? Should prior payments from insurance proceeds be offset against judgments and, if so, how?

HOLDING: Non-final orders may be reconsidered by the court at any time at the court's discretion. The issue of how much, if any, of prior payments by insurance companies to the plaintiffs on behalf of the defendant requires the participation of the insurance companies as parties. They are not parties to this litigation, so the court believes the issues are properly presented to the litigation in which the insurors are parties.

FACTS: A hospital was sued by over 100 patients for malpractice and filed Chapter 11. The cases were for the most part removed to the bankruptcy court. A settlement in a plan of reorganization provided for the payment of over $11 million to be paid to the plaintiffs from the hospital management company and an insurance company. The settlement permitted the plaintiffs to continue the litigation against the hospital management company, but recovery of any judgment was specifically limited to insurance proceeds.

Litigation with the insurance company who had not settled in full is pending in Tennessee over insurance coverage. That insurance company is not a party to the New Mexico litigation. Final judgments were being entered in the New Mexico litigation on behalf of plaintiffs, and the question was whether and how much the prior payments by insurance companies and the hospital management company would be offset against the judgment. The court determined that the amount, if any, of the offset would be in part affected by whether the payments satisfied the self insured retention ("SIR") of the hospital management company and other coverage questions. The plaintiffs, the hospital management company, and the insurance company were all in litigation in Tennessee over these issues, and the bankruptcy court determined that court should resolve the issues since it had jurisdiction over the necessary party, the insurance company, and the bankruptcy court did not. Also, since execution on the judgments was limited to insurance proceeds, there was no need to stay enforcement of the judgments.

SUMMARY NUMBER: 57
JAA

KEY CODE SECTION(S): F.R.C.P. 54(b)
KEY TOPIC(S): Reconsideration

COURT:	USBC-NM
JUDGE:	David T. Thuma
CASE NAME:	Siebel No. 2 Gonzales v. Geer, Wissel, Levy & Hartwell, P.A. (In re: Shari Siebel)
CITE:	Doc. No. 37
CASE NUMBER:	Adv. Proc. No. 17-01054; Bankr. No. 17-10827-j7
DATE DECIDED:	May 17, 2018

NOTEWORTHY ISSUE: What is the appropriate standard for the Court to use to decide a motion for reconsideration?

HOLDING: The Court originally denied cross-motions for summary judgment and the Defendant's motion to dismiss. The order was therefore interlocutory. As such Rule 54(b) applies, not Rules 59 or 60. They only apply to final orders. Judge Thuma uses a discretionary standard to decide if he should reconsider his order.

FACTS and DISCUSSION: While the Court had denied cross motions for summary judgment and Defendant's motion to dismiss, it did make factual and legal findings, including that Defendant did not have a valid lien. Defendant sought reconsideration.

Rule 54(b) addresses reconsideration of interlocutory orders. An order adjudicating fewer than all claims of all parties "may be revised at any time before the entry of a judgment . . . ."

Judge Thuma "...will not apply any particular test or set of factors in reviewing the motion to reconsider. In general, however, the Court will be skeptical of 'rehash' arguments. The Court may also deny a motion to reconsider in the interests of fairness and finality, if the legal arguments or evidence could have been presented in the original motion but were not. Finally, the movant's facts and arguments in support of reconsideration typically must be strong for the Court to change its ruling."

The Judge went through numerous legal arguments and determined he would not change his ruling.

SUMMARY NUMBER: 58
TDW

KEY CODE SECTION(S): Rule 60(b)
KEY TOPIC(S): Reconsideration; Attorneys fees

COURT and JUDGE: USBC DNM (Thuma)

CASE NAME and CITE: *In re Davide*, 2018 WL 6729665 (Bankr.D.N.M., 2018)

CASE NUMBER: Case No. 16-12689, Doc. No. 254

DATE DECIDED: December 21, 2018

NOTEWORTHY ISSUES: Would court reconsider order granting counsel's fee application upon debtors' motion for reconsideration filed 5 months after the fee application was filed and 2 months after the order awarding fees was entered, where debtors failed to object to the fee application?

HOLDINGS: No. Debtors did not object to counsel's fee application and only sought relief after learning that the order would be enforced as a money judgment. Debtors motion failed to satisfy the requirements of Rule 60(b).

FACTS: Debtors filed chapter 11, employed counsel, and filed a plan of reorganization and a draft disclosure statement, among other things. The disclosure statement was never approved. In the face of an upcoming final hearing on a motion to dismiss or convert the case, the Debtors stipulated to conversion of the case to chapter 7. The day before conversion, debtors' counsel moved to withdraw. Over debtors' objection, the Court granted the motion to withdraw. In April 2018, Counsel filed a final fee application, U.S. Trustee objected, and in July 2018 the court entered an agreed order allowing fees, and resolving the UST's objection. In August 2018, a transcript of judgment was issued relating to the Fee Order, and in early September 2018, counsel sought to domesticate the judgment in state district court, with notice to debtors. Five days later, debtors filed a Request to Reconsider Order Granting Application for Compensation.

The Court treated the motion as a motion seeking relief from a final judgment under Rule 60(b). At the court's request, and after a preliminary hearing, the debtors filed a second motion to reconsider, although the debtors did not address under which parts of Rule 60 debtors were requesting relief. After some analysis, the court examined the motion under Rule 60(b)(6), the catch-all provision, which requires extraordinary circumstances and is used only when necessary to accomplish justice. The court did not find that the circumstances justified relief.

SUMMARY NUMBER: 59
PMF

KEY CODE SECTION(S): 28 U.S.C. § 1334(b)
KEY TOPIC(S): Reference to Bankruptcy Court

COURT and JUDGE: United States District Court, D. New Mexico, Judge Herrera

CASE NAME and CITE: *Abruzzo v. Kearney,*. 2018 WL 485438

CASE NUMBER and DOCKET NUMBER: 18-cv-000922 JCH/SCY

DATE DECIDED: October 5, 2018

NOTEWORTHY ISSUE: Would a case removed to the district court from state court based on both diversity and "related to" bankruptcy jurisdiction be referred to the bankruptcy court automatically?

HOLDING: State court case was removed to the district court asserting diversity of citizenship and that it was "related to" a pending bankruptcy case. The district court noted that the case was asserted to be related to a bankruptcy case, so pursuant to the court's blanket referral order entered in 1984, 84-0324, the case is properly automatically referred to the bankruptcy court. If any party wishes to have the reference withdrawn so the matter will be heard in the district court, a motion for withdrawal of the reference must be filed.

FACTS: The debtor was frantically trying to stop the state court which was all too familiar with him from hearing whether his spendthrift trust trustees could take certain actions specified in a proposed plan of reorganization. The trustees asked for instructions from the state court, and one of the many maneuvers of the debtor was to remove the request for instructions to the district court. Because the bankruptcy court had previously lifted the automatic stay for the state court to consider the request, the debtor did not want the bankruptcy court to hear the removed action. The effort of the debtor failed.

SUMMARY NUMBER: 60
TDW

KEY CODE SECTION(S): §362
KEY TOPIC(S): Stay Relief

COURT and JUDGE: USBC DNM (Thuma)

CASE NAME and CITE: In re Crespin, 581 B.R. 904 (Bankr.D.N.M., 2018)

CASE NUMBER: Case No. 17–11234 ta13

DATE DECIDED: 02/20/2018

NOTEWORTHY ISSUES: Was there cause to lift the stay to permit judgment creditors to go back to state court to determine the total amount of punitive damages, costs, attorney fees, and interest owed by debtors?

HOLDINGS: No. The court applied a list of factors in addition to the often-cited *Curtis* factors, and found that the bankruptcy court could easily and quickly liquidate the buyers' claim, thereby "discharging [the bankruptcy court's] core claims-allowance duty." Thus, there was insufficient "cause" to modify the automatic stay.

FACTS: Debtors sold a mobile home to buyers. Buyers learned later that Greentree had a lien on the home, sued debtors, and got a judgment. Debtors filed chapter 7. Judge Jacobvitz ruled that debtors' debt to buyers was non-dischargeable but left it to the state court to decide punitive damages and other non-compensatory judgment amounts. The state court upheld the actual damages judgment and set a trial to determine punitive damages, costs, attorneys fees and interest. Debtors filed chapter 13 the day before the trial. Buyers filed a motion for stay relief for cause to allow the state court to determine the additional damages.

The court examined the 12 non-exclusive factors identified in *In re Curtis*, 40 B.R. 795, 799–800 (Bankr. D. Utah 1984). The "Curtis factors" are: 1. Whether the relief will result in a partial or complete resolution of the issues; 2. The lack of any connection with or interference with the bankruptcy case; 3. Whether the foreign proceeding involves the debtor as a fiduciary; 4. Whether a specialized tribunal has been established to hear the particular cause of action and that tribunal has the expertise to hear such cases; 5. Whether the debtor's insurance carrier has assumed full financial responsibility for defending the litigation; 6. Whether the action essentially involves third parties, and the debtor functions only as a bailee or conduit for the goods or proceeds in question; 7. Whether litigation in another forum would prejudice the interests of other creditors, the creditors' committee and other interested parties; 8. Whether the judgment claim arising from the foreign action is subject to equitable subordination under Section 510(c); 9. Whether movant's success in the foreign proceeding would result in a judicial lien avoidable by the debtor under Section 522(f); 10. The interest of judicial economy and the expeditious and economical determination of litigation for the parties; 11. Whether the foreign proceedings have progressed to the point where the parties are prepared for trial; 12. The impact of the stay on the parties and the 'balance of hurt.'

The court found that several of the *Curtis* factors (3, 5, 6, 7, and 8) are "often irrelevant" and that several factors not identified in *Curtis* are relevant. The court set forth factors it deems "most relevant" for a modification of the automatic stay to liquidate its claim in another (usually state) court:

i. Specialized Tribunal (divorce; child custody; probate proceedings; government contract claims; social security disability claims; and workers' compensation claims).
ii. Estate Administration. Would granting stay relief hinder or delay administration of the estate?
iii. The Claims Allowance Process. If the matter involves allowance of a claim in bankruptcy, which is a core bankruptcy function, the Court's inclination is to keep the stay in place and liquidate the claim.
iv. Judicial Economy. Would lifting the stay promote judicial economy?
v. Litigation Expense. Would it be cheaper for the parties to litigate in bankruptcy court or the other tribunal?
vi. Prejudice to other Creditors. Would lifting the stay potentially prejudice other creditors for any reason?
vii. Likelihood of Success. How likely is the creditor to prevail on its claim?
viii. Balance of the Hurt. Is there some reason, not taken into account by the above factors, that either the creditor or the estate would be prejudiced by lifting the stay or keeping it in place?

SUMMARY NUMBER: 61
JAA

KEY CODE SECTION(S): Sec. 362
KEY TOPIC(S): Relief from Automatic Stay

COURT:	USBC-NM
JUDGE:	David T. Thuma
CASE NAME:	In re: MBF Inspection Services, Inc.,
CITE:	Doc. No. 148
CASE NUMBER:	No. 18-11579-t11
DATE DECIDED:	December 12, 2018

NOTEWORTHY ISSUE: Should the stay be lifted to allow creditors to complete pending federal court litigation against the Debtor?

HOLDING: Applying the new *Crespin* factors, Judge Thuma did not lift the stay, conditioned on the Debtor agreeing to certain conditions.

FACTS and DISCUSSION: Prepetition, the Debtor was sued in Ohio by a group of its pipeline inspectors under the Fair Labor Standards Act. The dispute centered on whether the inspectors were hourly or salaried employees. The Sixth Circuit, which covers Ohio, had recently ruled in favor of pipeline inspectors in other similar cases. The Debtor wanted to litigate the issue in bankruptcy court through the claims allowance process.

In determining whether to lift the stay to permit litigation to go forward, Judge Thuma has modified the old *Curtis* factors and now uses the *Crespin* factors:

1. Whether the nonbankruptcy court is a specialized tribunal;
2. Whether granting stay relief would hinder or delay estate administration;
3. Whether the facts of the matter require a deviation from the Court's core function of allowing or disallowing claims;
4. Whether lifting the stay would promote judicial economy;
5. Whether it would be less expensive for the parties to litigate in bankruptcy court;
6. Whether lifting the stay would prejudice other creditors;
7. The movant's likelihood of prevailing in the litigation; and
8. Whether the "balance of the hurt" weighs in favor of or against stay relief.

The decision was to keep the stay in place and litigate the claims in bankruptcy court, if the Debtor agreed to certain conditions. Most importantly, Debtor had to concede that Sixth Circuit law would apply.

SUMMARY NUMBER: 62
TDW

KEY CODE SECTION(S): §362
KEY TOPIC(S): Stay Relief

COURT and JUDGE: USBC DNM (Thuma)

CASE NAME and CITE: *In re Kearney*, 2018 WL 4502076 (Bankr.D.N.M., 2018)

CASE NUMBER: Case no. 17-12274-t11

DATE DECIDED: September 18, 2018

NOTEWORTHY ISSUES: Was there cause to lift the automatic stay to permit a state court to consider changes to a testamentary trust that were required to implement one of two competing chapter 11 plans?

HOLDINGS: Yes. The bankruptcy court found that cause existed to lift the stay under the non-exclusive factors identified in *In re Curtis*, 40 B.R. 795, 799–800 (Bankr. D. Utah 1984), and the factors identified by Judge Thuma in *In re Crespin*, 581 B.R. 904, (Bankr. D.N.M. 2018).

FACTS: Debtor's wife died at the age of 31. At the time of her death, she owned about 18.5% of a family company in which debtor had no interest. Under the terms of wife's will, the stock was bequeathed to two testamentary spendthrift trusts, of which debtor is the lifetime, income beneficiary.

Debtor sued members of his wife's family in state court, before Judge Malott, alleging, *inter alia*, that some of them as trustees (the "Trustees") of wife's testamentary trusts, breached fiduciary duties owed to the Debtor. There also were claims that debtor breached his fiduciary duties as a trustee of the trusts. Ultimately, the state court ruled against debtor on several material points resulting in awards of attorneys fees and sanctions against debtor. On the eve of a state court hearing at which a judgment and additional fees and sanctions were likely to be awarded against debtor, debtor filed the chapter 11 case, in which debtor filed several versions of plans and disclosure statements. An unsecured creditor committee was formed, and it filed a competing plan of reorganization. Implementation of the UCC Plan requires, inter alia, state court approval of three proposed transactions involving the trusts in order to fund the UCC Plan.

With limited exceptions, the state court is the proper court to hear and determine state law disputes about testamentary trusts. See N.M.S.A § 46A-2-203 ("The district court has exclusive jurisdiction of all proceedings involving a trust."). Thus, before the UCC plan could become effective, the state court likely would have to decide whether to approve the Proposed Trust Changes.

The Trustees filed a Supplemental Motion for Relief from the Automatic Stay asking for additional stay relief so Judge Malott could hear and rule on the Proposed Trust Changes.

SUMMARY NUMBER: 63
TDW

KEY CODE SECTION(S): Rule 60(b)
KEY TOPIC(S): Relief from Judgment or Order

COURT and JUDGE: 10th Cir. Court of Appeals, Judge O'Brien

CASE NAME and CITE: *Saggiani v. Strong*, 718 Fed.Appx. 706 (Tenth Cir. 2018)

CASE NUMBER: No. 17-4061

DATE DECIDED: January 16, 2018

NOTEWORTHY ISSUE: Would order approving claim settlement be set aside upon Rule 60(b) motion filed 11 months after court entered settlement order?

HOLDING: No. Fact specific ruling held that motion was not filed within a reasonable time, did not meet the test for "excusable neglect" theory, and facts did not warrant application of "catchall" provision of "any other reason that justifies relief."

FACTS: Claim between debtor companies was settled under court-approved Conflict Resolution Procedures (CRPs) that were part of a Trustee's plan of liquidation that was confirmed after notice and opportunity to object. Under the CRP, a Conflicts Referee recommended the settlement, which was later approved by the bankruptcy court. Eleven months later, a party in interest, who had notice of the motion to approve the settlement, sought to set aside the order approving the settlement agreement under Rule 60(b). He argued that the settled claim was time-barred, should have been disallowed, and that he did not discover the defense until many months after the settlement was approved. He argued that Rule 60(b)(1) applied (excusable neglect) because he relied upon the Trustee, and did not conduct an independent investigation of possible defenses to the claim. He also argued that the catchall provision of Rule 60(b)(6) applied to set aside the order approving the settlement ("any other reason that justifies relief").

The bankruptcy court denied the Rule 60(b) motion, because it was untimely, all relevant facts were known to the movant or were easily discoverable at the time the court approved the settlement agreement, and the approved disclosure statement and the confirmed plan constituted an informal proof of the settled claim, so that it would not have been time-barred. The district court affirmed, and the movant appeal.

While very fact specific, the case includes points about Rule 60(b) that are worth noting:

- A Rule 60(b) motion must be made within a reasonable time—and for reasons (1), (2), and (3) no more than a year after the entry of the judgment or order or the date of the proceeding." Fed. R. Civ. P. 60(c)(1).
- A motion is not timely merely because it has been filed within one year of the judgment.
- There must be a "sufficient justification for the delay.

- The court will take into consideration "the interest in finality, the reason for delay, the practical ability of the litigant to learn earlier of the grounds relied upon, and prejudice to other parties."
- Here, the parties have a substantial interest in implementing the settlement agreement; and the movant was served with the settlement motion and did not object.
- The facts supporting the defense were known or should have been known to movant at the time he failed to object to the settlement motion.
- **Rule 60(b)(1).** The failure to object to the settlement was not excusable neglect. Excusable neglect arises where failure to comply with a deadline is attributable to negligence, which here means carelessness or faultless omission.
- Movant knew about the deadline and chose not to object. Rule 60(b)(1) relief is "not available for a party who simply misunderstands the legal consequences of his deliberate acts." All the facts were available to him at the time he elected not to object.

- Movant sought also relief under **Rule 60(b)(6)** contending the bankruptcy court abused its discretion in denying relief because the Trustee was conflicted in resolving the intercompany claims and failed to disclose all the facts and issues underlying the purported time-bar to the claim. He asserts the Trustee violated the CRPs and the court should have remediated the violation by invalidating the settlement agreement under Rule 60(b)(6).
- Rule 60(b)(6) relief is appropriate only when it "offends justice to deny such relief."
- Denial of a 60(b)(6) motion will be reversed "only if we find a complete absence of a reasonable basis and are certain that the decision is wrong."
- Movant claimed that the trustee violated the CRP by failing to disclose the purported time-bar, but all the relevant facts were available to movant when he elected not to investigate or object to the settlement motion.
- "The broad power granted by clause (6) is not for the purpose of relieving a party from free, calculated and deliberate choices he has made. A party remains under a duty to take legal steps to protect his own interests."

SUMMARY NUMBER: 64
JAA

KEY CODE SECTION(S):
28 U.S.C. Secs. 1452(a), (b), 1334(b),(c)

KEY TOPIC(S): Removal, Remand

COURT:	USBC-NM
JUDGE:	David T. Thuma
CASE NAME:	Smith & Marrs, Inc., v. Hoskins (In re: Hoskins Family Enterprises, Inc.)
CITE:	Doc. 48
CASE NUMBER:	Adv. Proc. No. 17-01056; Bankr. No. 17-11175-t11
DATE DECIDED:	January 25, 2018

NOTEWORTHY ISSUE: What factors should the court consider when deciding whether to remand a proceeding removed from state court?

HOLDING: In deciding whether to remand a removed proceeding, the bankruptcy court will consider the same standards that apply to abstention. This proceeding would be remanded to state court.

FACTS and DISCUSSION: In 2015, a lawsuit was filed in state court by Smith & Marrs against the Hoskins Family Enterprises. A trial was set for May 8, 2017. Hoskins filed a Ch. 11 petition on May 9, 2017, stopping the trial. The Debtor then removed the state court case to bankruptcy court.

Judge Thuma found that when considering remand, the Court should consider the standards that apply to abstention. He also found there are two types of abstention: "mandatory" (28 U.S.C. § 1334(c)(2)), and "permissive" (28 U.S.C. § 1334(c)(1)). Since the removed case dealt entirely with state law issues, and was thus non-core, mandatory abstention would be considered. (The plaintiffs sued on a note and mortgage and the Debtor counterclaimed for breach of fiduciary duty and breach of contract.)

Judge Thuma used this test to determine mandatory abstention under 28 U.S.C. Sec. 1334(c)(2):

1) The motion for abstention must be timely filed;
2) The matter must be based on a state law claim or cause of action;
3) The action was commenced in state court;
4) The action can be timely adjudicated in state court;
5) The claim is within the Court's non-core jurisdiction; and
6) There is no independent source of federal jurisdiction that would have permitted the plaintiff to commence the action in federal court in the absence of the bankruptcy case.

The Judge found the elements of mandatory abstention were satisfied and the case was remanded. The court also held that the elements of permissive abstention were met.

SUMMARY NUMBER: 65
JAA

KEY CODE SECTION(S):
28 U.S.C. Secs. 1452(a), (b), 1334(b), (c), and 1334(e)(1)

KEY TOPIC(S): Removal, Remand

COURT:	USBC-NM
JUDGE:	David T. Thuma
CASE NAME:	New Mexico Health Care Assn., Inc., v. Plaza De Retiro, Inc. (In re: Plaza De Retiro, Inc.)
CITE:	Doc. No. 33
CASE NUMBER:	Adv. Proc. No. 18-01043-t; Bankr. No. 09-10974-t11
DATE DECIDED:	October 24, 2018

NOTEWORTHY ISSUE: What factors should the court consider when deciding whether to remand a proceeding removed from state court?

HOLDING: In deciding whether to remand a removed proceeding, the bankruptcy court will consider the same standards that apply to abstention. This proceeding would not be remanded to state court.

FACTS and DISCUSSION: Long after a Ch. 11 plan was confirmed, all the Debtor's property sold and the case closed, the Debtor became eligible for a dividend of $88,798.21 from the NM Worker's Compensation Administration self-insurance group. The dividend was on account of insurance paid for by the Debtor pre-petition. The Debtor's prospect of receiving the dividend was unknown to the Debtor and Ch. 11 Trustee during the bankruptcy case. The New Mexico Health Care Association, Inc., administrator of the self-insurance group, filed suit in state court and named 92 defendants, who were mostly creditors in the bankruptcy case. Debtor's former attorneys, who were named defendants, removed the case to bankruptcy court. The Plaintiff filed a motion to remand.

Since the dividend was "unscheduled property" of the Debtor, it was not abandoned when the case was closed. Therefore, the dividend was property of the estate, and the bankruptcy case would be reopened for administration of the asset. The court found the matter to be within its "arising in" jurisdiction under 28. U.S.C. Sec. 1334(b). The court also found jurisdiction under 28 U.S.C. Sec. 1334(e)(1), which gives the district court jurisdiction over property of the estate. All of this means the Bankruptcy Judge found he had core jurisdiction over the matter.

Judge Thuma found that when considering remand, the Court should consider the standards that apply to abstention. He also found there are two types of abstention: "mandatory" (28 U.S.C. § 1334(c)(2)), and "permissive" (28 U.S.C. § 1334(c)(1)). Since the matter is a core

matter, mandatory abstention does not apply. The factors the Court will consider to determine permissive abstention are as follows:

1. Effect that abstention would have on the efficient administration of the bankruptcy estate;
2. Extent to which state law issues predominate;
3. Difficulty or unsettled nature of applicable state law;
4. Presence of a related proceeding commenced in state court or other nonbankruptcy court;
5. Federal jurisdictional basis of the proceeding;
6. Degree of relatedness of the proceeding to the main bankruptcy case;
7. Substance of the asserted "core" proceeding;
8. Feasibility of severing the state law claims;
9. Burden the proceeding places on the bankruptcy court's docket;
10. Likelihood that commencement of the proceeding in bankruptcy court involves forum shopping by one of parties;
11. Existence of a right to jury trial; and
12. Presence of nondebtor parties in the proceeding.

Judge Thuma weighed the factors and decided he would not remand the case.

SUMMARY NUMBER: 66 KEY CODE SECTION(S): n/a
MKD KEY TOPIC(S): Res Judicata

COURT and JUDGE: U.S.B.C.; David T. Thuma
CASE NAME and CITE: Aquatic Pools, Inc;
CASE NUMBER: Case No. 15-11406 t11; Docket No. 204
DATE DECIDED: June 14, 2018

NOTEWORTHY ISSUE:

1. Should the Court set aside the fee order under Rule 60(b)(4) [void judgment]?
2. Should the Court set aside the fee order under Rule 60(b)(6) [other reason]?
3. Should res judicata preclude Debtor from suing Counsel with respect to the insurance issue in the first case?

HOLDING:

1. No. The narrow grounds for relief under Rule 60(b)(4) were not met.
2. No. The motion was filed two years after the fee order, which is not a reasonable time; there were no extraordinary circumstances justifying relief.
3. Notice was sufficient to preserve the fee order, but not to preclude a future dispute. Unlike Potter v. Pierce, this debtor did not object to the fee application.

Rule 60(b)(4) is an extremely narrow remedy. A judgment is not void because it is erroneous, and 60(b)(4) may not be a substitute for appeal. Only if a court lacks jurisdiction (personal or subject matter) or if it acts in a fashion inconsistent with due process of law is a judgment void. This Court had jurisdiction to rule on the fee application, jurisdiction over Counsel and Debtor, There was notice and opportunity to object, and hence, due process.

Relief under Rule 60(b)(6) cannot be for any reasons listed in 60(b)(1-5), and may only be granted in exceptional circumstances. It must be filed in a reasonable time.

FACTS:

Debtor filed a Chapter 11 case in 2015, which was dismissed for lack of insurance after two months. At the end of the first case, Debtor owed its counsel $18,000. Debtor obtained insurance and filed a second Chapter 11 case a month later. Counsel disclosed the prior balance in its Rule 2014 disclosure. Debtor confirmed a plan, and Counsel filed its only fee application, expressly mentioning the fees due from the first case. The fee application was approved without hearing.

The parties became adverse; in February of 2017 Counsel sought a writ of garnishment; Debtor hired new counsel, and moved to set aside the order approving fee application under Rule 60(b).

Had someone objected to the first case balance due, the Court might not have allowed the prior case fees in the application, and might not even have authorized counsel's employment.

SUMMARY NUMBER: 67
TDW

KEY CODE SECTION(S): 523(a)(7); Rule 56
KEY TOPIC(S): Dischargeability; Summary Judgment; Standing

COURT and JUDGE: Tenth Circuit Court of Appeals, J. Bacharach

CASE NAME and CITE: *Medical Lien Management, Inc., et al. v. Dampier,(In re Dampier)*, 722 Fed.Appx. 855 (10th Cir. 2018)
CASE NUMBER: No. 17-1160
DATE DECIDED: February 14, 2018

NOTEWORTHY ISSUES:
(1) Must statutory standing be raised in summary judgment briefs to be preserved on appeal of order granting summary judgment?
(2) Is restitution imposed as part of a criminal sentence non-dischargeable under 523(a)(7)?

HOLDING:
(1)Yes. Statutory standing argument will be forfeited if not raised in summary judgment briefs.
(2) Yes. Restitution imposed as part of a criminal sentence is non-dischargeable

FACTS: Debtor was convicted in state court of theft for stealing from his employers, and was ordered to pay restitution of approximately $197,000. Debtor filed bankruptcy. Employers filed non-dischargeability action, seeking determination that the restitution obligation was not dischargeable under § 523(a)(7). The bankruptcy court held that the restitution obligation was non-dischargeable and granted the employers' motion for summary judgment. The BAP affirmed. Tenth Circuit reviewed de novo.

Section 523(a)(7) provides, in part: "A discharge under [Chapter 7] does not discharge an individual debtor from any debt ... to the extent such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss."

Debtor argued that employers lack standing under § 523(a)(7) because they are not governmental units. The 10th Circuit held that debtor "forfeited" the statutory standing argument because debtor did not raise it in this summary judgment briefs

On the merits, the Tenth Circuit held that restitution imposed as part of a criminal sentence is non-dischargeable under §523(a)(7) even though the restitution is forwarded to the victim, following *Kelly v. Robinson*, 479 U.S. 36, 107 S.Ct. 353, 93 L.Ed.2d 216 (1986), and *Troff v. Utah (In re Troff)*, 488 F.3d 1237 (10th Cir. 2007). In *Kelly* the Supreme Court explained that even though "restitution is forwarded to the victim," § 523(a)(7) does not "allow[ ] the discharge of a criminal judgment that takes the form of restitution" because "[t]he criminal justice system is not operated primarily for the benefit of victims, but for the benefit of society as a whole."

SUMMARY NUMBER: 68
TDW

KEY CODE SECTION(S): §521(a)
KEY TOPIC(S): Retain and Pay

COURT and JUDGE: USBC DNM (Thuma)

CASE NAME and CITE: In re Templin, 2018 WL 1864928 (Bankr.D.N.M., 2018)

CASE NUMBER: Case No. 17–13196 t7

DATE DECIDED: April 17, 2018

NOTEWORTHY ISSUES: Mortgage company moved for order requiring debtor to comply with § 521(a)(2) and (6) of the Bankruptcy Code, and to delay entry of the bankruptcy discharge until he does.

HOLDINGS: Following Judge Jacobvitz's decision in *In re Williamson*, 540 B.R. 460 (Bankr. D.N.M. 2015), the court denied the creditor's motion. The court found no basis to delay or deny entry of discharge due to debtor's failure to comply with §521(a)(2) and (a)(6).

FACTS: Debtor owns a mobile home financed by creditor. The financing documents do not include an *ipso facto* clause. Debtor filed chapter 7 and filed a statement of intent about the mobile home and creditor's purchase money loan, stating: "[Debtor will] Retain the property and ... will continue making payments to creditor without reaffirming."

Debtor did not sign a reaffirmation agreement with creditor. No objections to discharge were filed and debtor was eligible for discharge. Debtor does not intend to reaffirm with creditor, nor to surrender the mobile home, nor to redeem it. Rather, Debtor intends to "retain and pay." The Court temporarily delayed entry of the discharge, until it ruled on creditor's motion.

Section 521(a)(2)(A) requires a debtor, within 30 days after his petition date, to file a statement of his intention with respect to the retention or surrender of property of the estate and, if applicable, specify that ... the debtor intends to redeem such property, or that the debtor intends to reaffirm debts secured by such property. The court stated that this language is "generally acknowledged to give a debtor three, and only three, options for encumbered property: surrender it, redeem it, or reaffirm the debt."

Section 362(h) makes clear that if a debtor violates § 521(a)(2), the automatic stay will be lifted, and the subject personal property will be abandoned from the bankruptcy estate.

Also, Section 521(d) has the effect of permitting the secured creditor to enforce an *ipso facto* clause to the extent enforceable under applicable nonbankruptcy law. This means that, after the stay has been lifted and the property abandoned from the bankruptcy estate, the creditor can prevent a debtor from successfully opting to "retain and pay" for the collateral by enforcing the *ipso facto* clause. This enforcement mechanism is only available, however, to creditors who have included ipso facto clauses in their security agreements.

The court found no basis in the Code to deny or delay debtor's discharge. Nor did the court have a basis to order the debtor to comply with §521(a)(2). There are many Code-based remedies for failure to comply with specific Code requirements, but none for §521(a)(2). Following Judge Jacobvitz's decision in *Williamson*, which addressed the same complaint by the same creditor as in the present case, the court found no sufficient basis to invoke equitable powers to enforce a specific Code requirement for which Congress chose not to provide a specific remedy, as it did for so many Code violations.

Judge Jacobvitz stated:

> Because the Bankruptcy Code itself provides the remedy with regard to the property as a consequence of the Debtor's noncompliance with duties under § 521(a)(2)(A) and (B), and § 521(a)(6), [creditor] is not entitled to an order compelling Debtors to enter into a reaffirmation agreement, redeem the Manufactured Home, or surrender the property as a result of Debtors' failure to carry out their duties under § 521(a)(2) or § 521(a)(6). Instead, [creditor] must look to applicable non-bankruptcy law to enforce whatever rights it believes it has with regard to the Manufactured Home under the Contract.

Here, because the creditor's financing documents did not include an *ipso facto* clause and debtor was not otherwise in default, creditor had no state court remedy.

SUMMARY NUMBER: 69
TDW

KEY CODE SECTION(S): F.R.C.P. 4(m)
KEY TOPIC(S): Service of Complaint

COURT and JUDGE: USBC DNM (J. Jacobvitz)

CASE NAME and CITE: *Gonzales v. Delgado (In re Quick Cash, Inc.)* 2018 WL 1801211 (Bankr.D.N.M., 2018)

CASE NUMBER: No. 15–11800–j7; Adversary No. 17–1051–j

DATE DECIDED: April 13, 2018

NOTEWORTHY ISSUE: Were trustee's efforts to serve adversary proceeding sufficiently diligent to warrant extending the 90-day service deadline for good cause under Rule 4(m)?

HOLDING: Yes, under the circumstances, for one of the defendants that filed motion to dismiss; the court did not rule as to the other defendant due to insufficient evidence.

FACTS: Debtor filed chapter 11. A creditors' committee was appointed. The committee was filed a fraudulent transfer adversary proceeding against numerous defendants including "RCS" and "Elkhorn." The case was converted to chapter 7 and trustee was appointed. The court set a deadline for the trustee to determine whether to proceed with the adversary proceeding and, if so, serve alias summonses on defendants. Trustee filed an amended complaint. Several alias summonses were issued and trustee attempted service on the defendants by mail, to different addresses, during the weeks following the deadline. Ultimately, both RCS and Elkhorn received the amended complaint and alias summons.

RCS and Elkhorn filed motions to dismiss the adversary proceeding alleging that the Trustee failed to timely serve the summons and complaint as required under Fed. R. Civ. P. 4(m). Service in adversary proceedings is governed by Bankruptcy Rule 7004, which incorporates certain sections of F.R.C.P. 4, including Rule 4(m). Rule 4(m) provides that a defendant must be served within 90 days after the complaint is filed, or the court must dismiss the action without prejudice against that defendant or order that service be made within a specified time. If the plaintiff shows good cause for the failure to serve within the deadline, the court must extend the time for service for an appropriate period. No defendant was served within the 90 day deadline under Rule 4(m).

This case is about whether there was "good cause" to extend the deadline to serve the defendants, and is very fact specific. The Court found good cause to extend the deadline to effect service on RCS through the date the Trustee successfully served RCS and denied the motion to dismiss as to RCS. The court held over the Motion to Dismiss as to Elkhorn to hear additional evidence. (Later in the case the adversary proceeding was dismissed as to Elkhorn by stipulation.)

- If good cause is shown, trustee was entitled to an extension of time.
- Determination of good cause under Rule 4(m) is entrusted to the sound and considerable

discretion of the court.
- "Good cause" is not defined by Rule 4(m).
- A plaintiff may satisfy the "good cause" requirement by showing that plaintiff "has acted diligently in trying to effect service or there are understandable mitigating circumstances."
- The plaintiff who seeks to rely on the good cause provision must show meticulous effort to comply with the rule.
- The Court examined the details of the trustee's efforts to serve RCS at various addresses, to the attention of the registered agent, and found that the Trustee's efforts to serve RCS were sufficiently diligent to demonstrate good cause to extend the service deadline consistent with Rule 4(m).
- The Court did not need to decide whether the Trustee's service of the alias summons and amended complaint on RCS was effective; RCS admitted that it ultimately received the summons.
-Although not an issue in this case, the Court noted that "non-receipt raises due process concerns," citing *Tully v. Haughee (In re Haughee)*, 428 B.R. 828, 830 (Bankr. N.D. Ind. 2010) (observing that "[o]ne might seek to construe Fed. R. Bankr. P. 7004(b)(9) as providing that service of process is complete upon mailing of a copy of a summons and complaint to a defendant/debtor at the address provided for by the Rule, regardless of whether the defendant/debtor ever receives the mailing. That construction of the Rule would be such an obvious violation of any concept of both procedural and substantive due process that the court will spend very little time to address the invalidity of any such contention.").

SUMMARY NUMBER: 70 KEY CODE SECTION(S): n/a
KEY TOPIC(S): Standing

COURT and JUDGE: US Bankruptcy Court, NM (Robert H. Jacobvitz

CASE NAME and CITE: In re Las Cruces Country Club, Inc.; 585 B.R. 239
CASE NUMBER: Case No. 16-12947 j7
DATE DECIDED: April 2, 2018

NOTEWORTHY ISSUE:

1. Who has standing to object to the sale of estate property?
2. Was an auction at the mediation appropriate procedure?

HOLDING:

1. Prestige lacks standing; it is a potential purchaser, not creditor or stockholder
2. Debtor has standing to object, this is a surplus estate.
3. Creditors lack standing if they would be paid in full by the sale, but here they may support the sale over an auction for fear the current buyer would walk.
4. Greater safeguards in a public auction than there were here; Trustee will hold one.

FACTS:

LCCC, a nonprofit corporation, filed a Chapter 7 petition November 29, 2016. Philip J. Montoya is the Trustee. 99% of the scheduled assets was "the amount due on sale of real estate" worth $4.8 million. LCCC conveyed real estate to Park Ridge for a note of $4.8 million prior to the bankruptcy. Park Ridge never paid; the Trustee seeks a reconveyance in an adversary proceeding.

In the main case creditor First Valley sought to convert the case to Chapter 11 and appoint its principal as Chapter 11 Trustee. Mr. Montoya received a $2.1 million offer from Prestige Development Group Inc. to purchase the Park Ridge note; that is enough to pay all creditors in full.

Several parties (CEP, Park Ridge, Prestige) mediate, which mediation turns into a de facto auction of the note; the Trustee then moves to sell the note (actually all estate assets) to CEP or to Park Ridge for $3.3 million, with the surplus donated to NMSU. Prestige objects, it will pay more. LCCC wants a formal auction to maximize estate surplus.

SUMMARY NUMBER: 71
JAA

KEY CODE SECTION(S): None
KEY TOPIC(S): Standing

COURT:	USCA 10th Cir.
JUDGE:	Monroe G. McKay
CASE NAME:	Orr v. Husch Blackwell, LLP
CITE:	718 Fed. Appx. 759
CASE NUMBER:	No. 17-3214
DATE DECIDED:	April 12, 2018

NOTEWORTHY ISSUE: Does an officer and shareholder of a Debtor corporation have standing to sue the counsel who represented the Ch. 11 Trustee?

HOLDING: No. If counsel for a Ch. 11 Trustee commits torts arising out of representation of the Trustee, the causes of action belong to the Debtor corporation or Trustee, not the officers and shareholders.

FACTS and DISCUSSION: Conduct that harms a corporation only confers standing on the corporation, not the shareholders. To have standing, a shareholder must have suffered an injury not dependent on the corporation.

SUMMARY NUMBER: 72
TDW

KEY CODE SECTION(S): None
KEY TOPIC(S): Standing on Appeal

COURT and JUDGE: Tenth Circuit Court of Appeals (J. Baldock)

CASE NAME and CITE: *Parr v. Rodriguez*, 732 Fed.Appx. 714 (10th Cir., 2018)

CASE NUMBER: No. 17-1258

DATE DECIDED: May 22, 2018

NOTEWORTHY ISSUE: Did debtor have standing to appeal an order approving a sale of estate property under code §363 when the Debtor did not object to the motion to sell?

HOLDING: No. Because debtor did not file an objection to the sale motion, debtor was not a "person aggrieved" and therefore lacked standing to appeal.

FACTS: Chapter 7 trustee filed motion to sell estate property. Pro se debtor did not object. The bankruptcy court granted the motion, and debtor appealed. Trustee moved to dismiss appeal. The BAP granted the motion to dismiss and debtor appealed.

"Only a person aggrieved by a bankruptcy court order may seek appellate review of that order." To be a "person aggrieved," the party must show that his "rights or interests are directly and adversely affected pecuniarily by the decree or order of the bankruptcy court." A debtor does not qualify as a "person aggrieved" by a bankruptcy court order "[u]nless the estate is solvent, and excess will eventually go to the debtor, or unless the matter involves rights unique to the debtor," such as an "exemption of property from the estate." Further, a prerequisite for being a person aggrieved are attendance and objection at a bankruptcy court proceeding."

Here, the BAP did not make a determination whether the estate was insolvent. Instead, the BAP ruled that Debtor lacked standing because he had not filed any objection to the Sale Motion, nor requested a hearing. The court of appeals agreed. The Debtor lacked standing to appeal because he did not object to the sale motion, stating "prerequisites for being a person aggrieved are attendance and objection at a bankruptcy court proceeding."

SUMMARY NUMBER: 73
PMF

KEY CODE SECTION(S):§ 362
KEY TOPIC(S): Standing

COURT and JUDGE: United States Court of Appeals, Tenth Circuit, Judge Moritz

CASE NAME and CITE: *In re: Adam Peeples;. Lee v. McCardle.* 880 F.3d 1207 (2018)

CASE NUMBER and DOCKET NUMBER: 17-4046

DATE DECIDED: January 26, 2018

NOTEWORTHY ISSUE: Who is within the "zone of interest" (what is commonly called "who has standing") to bring an action for a violation of the automatic stay.

HOLDING: Although traditionally the analysis has been prudential or statutory standing, the correct analysis is whether the claimant is within the "zone-of-interests" which the particular federal statute was intended to protect. The question should be whether Congress intended to protect the particular plaintiff. There is a stringent zone of interest requirement for anyone seeking a remedy under a federal statute. Even if a creditor is harmed, the issue is whether the creditor has a remedy under the automatic stay provisions. Not every injury is remediable in the federal courts. The automatic stay is for the benefit of the estate.

The landlord creditor was not within the "zone of interest" intended to be protected by the automatic stay, so his suit for violation of the automatic stay was dismissed. Despite the fact that the landlord creditor was going to face damages, Congress did not intend the automatic stay to extend to protecting creditors

FACTS: Landlord sued tenant for past due rent and received a judgment. Landlord then sued in state court the trustee of a trust claiming that the trustee had wrongfully got the grantor of the trust to disinherit the tenant. The landlord claimed that the tenant should have received overdue distributions which he wanted. The landlord lost that suit and the state court was figuring out the amount of attorneys' fees to be ordered paid by the landlord to the trustee when the tenant filed bankruptcy.

The landlord then claimed that the automatic stay in the tenant's bankruptcy stopped the state court from entering judgment against him for the fees. He filed an adversary claiming violation of the stay and seeking damages. Case dismissed.

SUMMARY NUMBER: 74
JAA

KEY CODE SECTION(S): Bankr. Rule 8007
KEY TOPIC(S): Stay Pending Appeal

COURT:	USBC-NM
JUDGE:	David T. Thuma
CASE NAME:	Kearney Stay Lift Appeal No. 1 In re: Victor P. Kearney
CITE:	Document No. 486
CASE NUMBER:	17-12274-t11
DATE DECIDED:	October 1, 2018

NOTEWORTHY ISSUE: What is the standard for issuance of a stay pending appeal of motions to modify or terminate the automatic stay?

HOLDING: Judge Thuma considered the four factor test for stays pending appeal and determined that he would not issue a stay. In the end, it was in fact best for all creditors and the debtor that the Ch. 11 case move forward. That required decisions by the State Court that the stay lift orders would permit.

FACTS and DISCUSSION: Debtor Kearney is the beneficiary of Trusts established by his late wife. Some of the wife's family members are the contingent remainder beneficiaries of the Trust. The Trust owns shares of stock in Alvarado Realty Co. (ARCO). The ARCO shares paid dividends to the Debtor's Trust of around $800,000 per year, all of which was paid out to the Debtor. The Debtor believed he was being cheated and that $800,000 a year was an insufficient distribution. He commenced state court litigation against the Trustees of the Trust and others. Counterclaims were filed. The State Court found that it was the Debtor who had breached his fiduciary duties and that good cause existed to modify the Trust. Before a final judgment was entered or any modifications could be made, Debtor filed a Ch. 11 bankruptcy. The Unsecured Creditors Committee filed a plan. The UCC plan requires modification of the trust in three ways:

1. ARCO will pay $12,571,799 to Debtor's Trust in exchange for all ARCO stock held by the trusts.
2. The Trustees deliver a $3 million trust payment to Debtor, which would be delivered to creditors, thus funding the plan.
3. Debtor's $350,890.55 priority tax debt will be paid from net income that would otherwise be distributable to Debtor from the Trusts.

Confirmation of the UCC Plan is contingent upon State Court approval of these items. Judge Thuma entered two different stay lift orders so that the State Court could rule on these issues. The Debtor appealed the stay lift.

Rule 8007 provides that bankruptcy courts may issue a stay pending appeal. Judge Thuma employs a four factor test: 1) whether the applicant has made a strong showing of likelihood of success on the merits; 2) whether the applicant will be irreparably harmed without a stay; 3) whether issuance of a stay will substantially injure other interested parties; and 4) where the public interest lies. Judge Thuma states that factors one and two are the most critical. The movant has the burden to show the factors weigh in its favor.

Judge Thuma noted that orders granting or denying stay relief are reviewed under an abuse of discretion standard. This means the appellate court has to have a firm and definite conviction that a clear error of judgment was made or the lower court strayed outside of permissible choice in the circumstances. Stated differently, abuse of discretion occurs when the trial court's decision is arbitrary, capricious, whimsical or results in a manifestly unreasonable judgment.

SUMMARY NUMBER: 75 KEY CODE SECTION(S): n/a
MKD KEY TOPIC(S): Summary Judgment

COURT and JUDGE: NM Bankruptcy Court; David T. Thuma
CASE NAME and CITE: Mazel v. Holley (In re Brainard);
CASE NUMBER: Case No. 7-17-11254 TA; Adv. No. 17-1060 t
DATE DECIDED: January 9, 2018

NOTEWORTHY ISSUE:

1. Is either party entitled to summary judgment?
2. Is the agreement an executory contract?

HOLDING:

No, there are genuine issues of material fact. To get summary judgment movant must:

1. Show by pleadings, admissions, affidavits or discovery that there is no genuine issue as to any material fact; and
2. Movant is entitled to judgment as a matter of law.
3. Movant bears the initial responsibility of demonstrating lack of an issue of material fact;
4. If Movant carries this burden, non-Movant must designate specific facts showing a genuine issue for trial.

A note can be an independent contract; on the other hand when signed together with another closely intertwined document, the two documents can be treated as a single contract. Here the two contracts were signed at the same time by the same parties in the same transaction. The note is not negotiable, and the purchase agreement cannot be assigned. The contracts should be construed together as a single instrument.

The Court cannot tell if the contract was executory. If Brainard retained solely a security interest, then it is likely a financing device. If Brainard retained ownership and managerial authority over the businesses, it might be an executory contract. These fact issues prevent SJ.

FACTS:

Brainard sold his Vape business in Taos & Durango to Holly for $111,000 ($20,000 down, the rest through a promissory note) in May of 2017. Holley stopped paying the note, he says because Brainard stopped cooperating. Brainard filed bankruptcy; his Trustee sued Holley to enforce the note. The Trustee did not seek to assume any executory contracts.

Holley defends by arguing unless someone satisfies Brainard's obligations to meaningfully complete the transfer of the business, he has no obligation to pay anything on the note. Mazel argues only the note is relevant to the dispute.

SUMMARY NUMBER: 76
JAA

KEY CODE SECTION(S): Sec. 542, Rule 7012(b)(6)
KEY TOPIC(S): Turnover

COURT:	USBC-NM
JUDGE:	Robert H. Jacobvitz
CASE NAME:	Mazel v. Lovelace (In re: Infinity Home Health Care, LLC)
CITE:	2018 WL 5310659
CASE NUMBER:	Adv. Proc. No. 18-1051-j; Bankr. No. 16-10062-j7
DATE DECIDED:	October 25, 2018

NOTEWORTHY ISSUE: Did the Trustee plausibly plead turnover under Sec. 542?

HOLDING: Not in this case. Sec. 542 only applies to a debt to the estate that is undisputed and presently payable. The Trustee cannot use turnover to liquidate a contract dispute.

FACTS and DISCUSSION: The Trustee essentially alleged that there was an implied contract between the Debtor and Lovelace. Alternatively, in the response to the motion to dismiss, the Trustee alleged unjust enrichment.

Judge Jacobvitz found that "New Mexico law recognizes implied in fact contracts as 'a meeting of minds, which, although not embodied in an express contract, is inferred, as a fact, from conduct of the parties showing, in the light of the surrounding circumstances, their tacit understanding.' To be legally enforceable, implied in fact contracts, like express contracts 'must be factually supported by an offer, an acceptance, consideration, and mutual assent.' The complaint failed to allege facts supporting an implied contract." (citations omitted). The court found that the Trustee did not plead any facts to support an implied contract.

Jacobvitz also said that "[i]n New Mexico, the elements of an unjust enrichment claim are that the opposing party has "[1] been knowingly benefitted at one's expense (2) in a manner such that allowance of the other to retain the benefit would be unjust." The Trustee failed to allege this in the complaint. It was raised only in the response to the motion to dismiss.

In any event, the Trustee's theories cannot be used to liquidate a breach of contract claim in a Sec. 542 turnover complaint.

Discussion from the Bench

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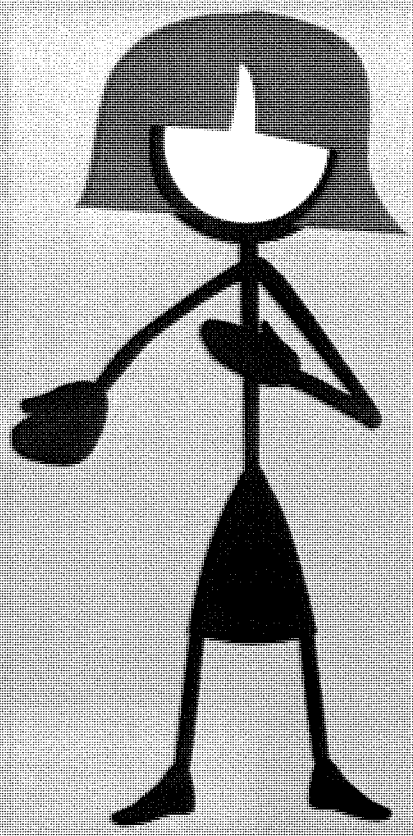
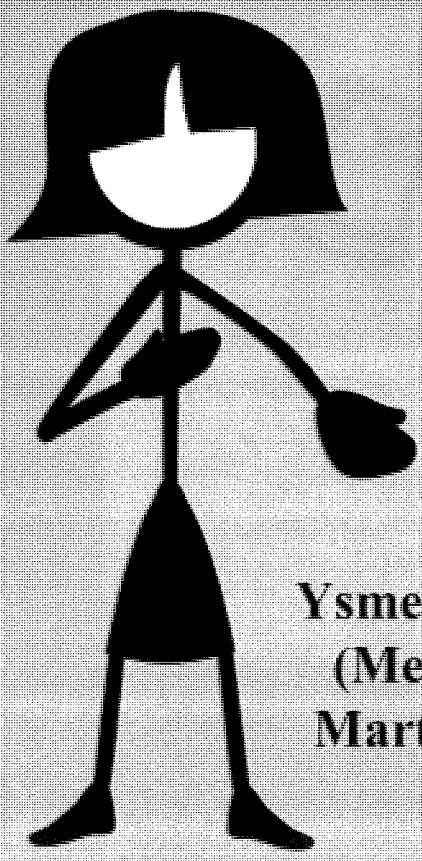
Clerk's Office Report

2019 Bankruptcy Year in Review

Clerk's Office Report



Lana Merewether



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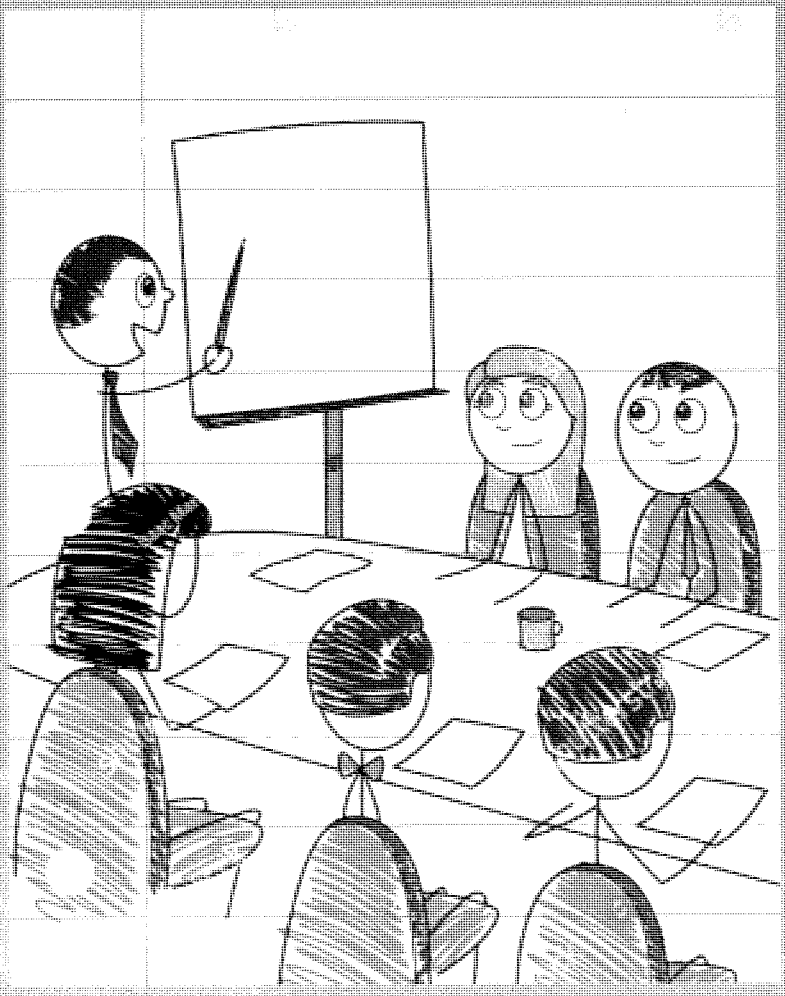
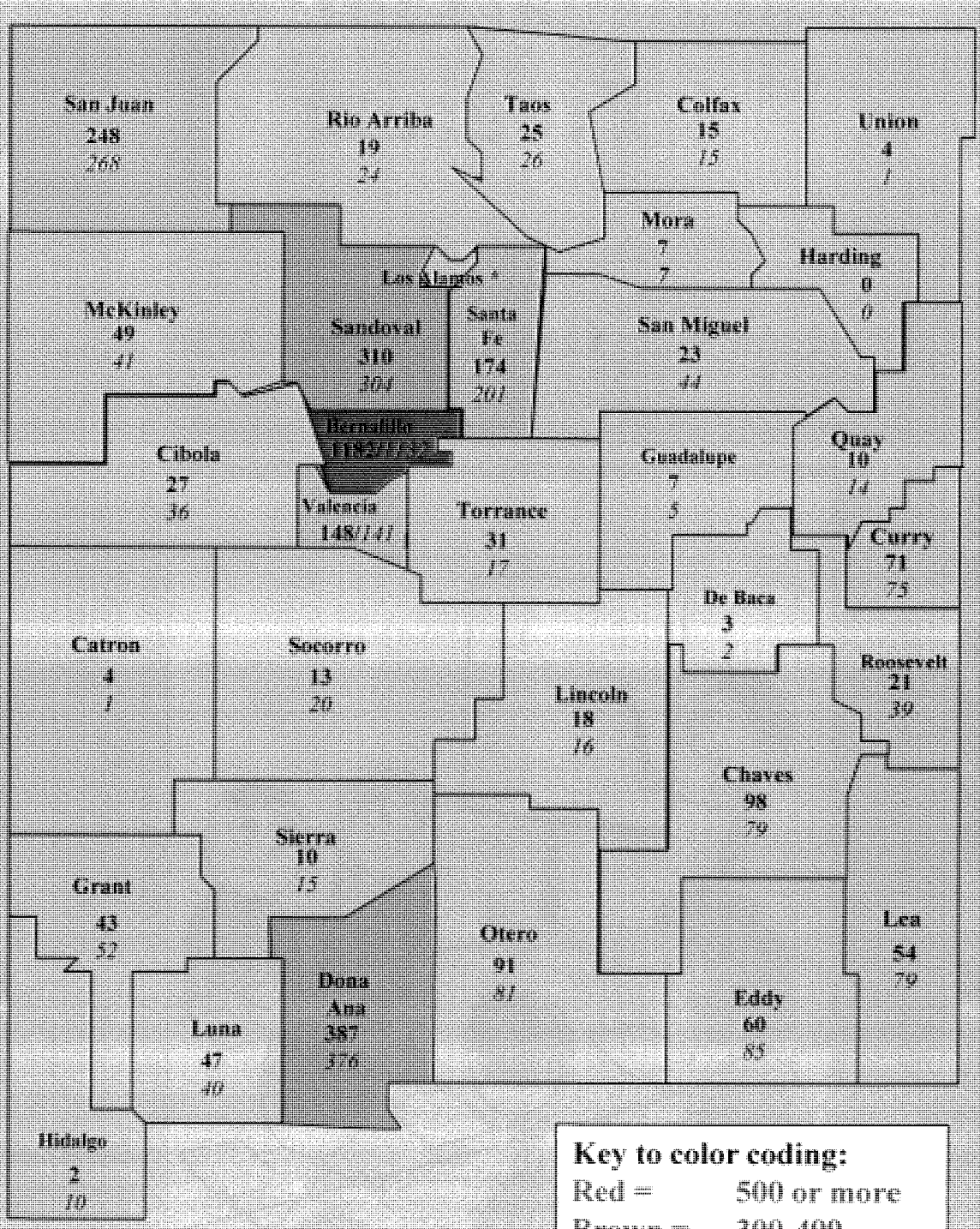


District of New Mexico
Bankruptcy filing totals
for 2018

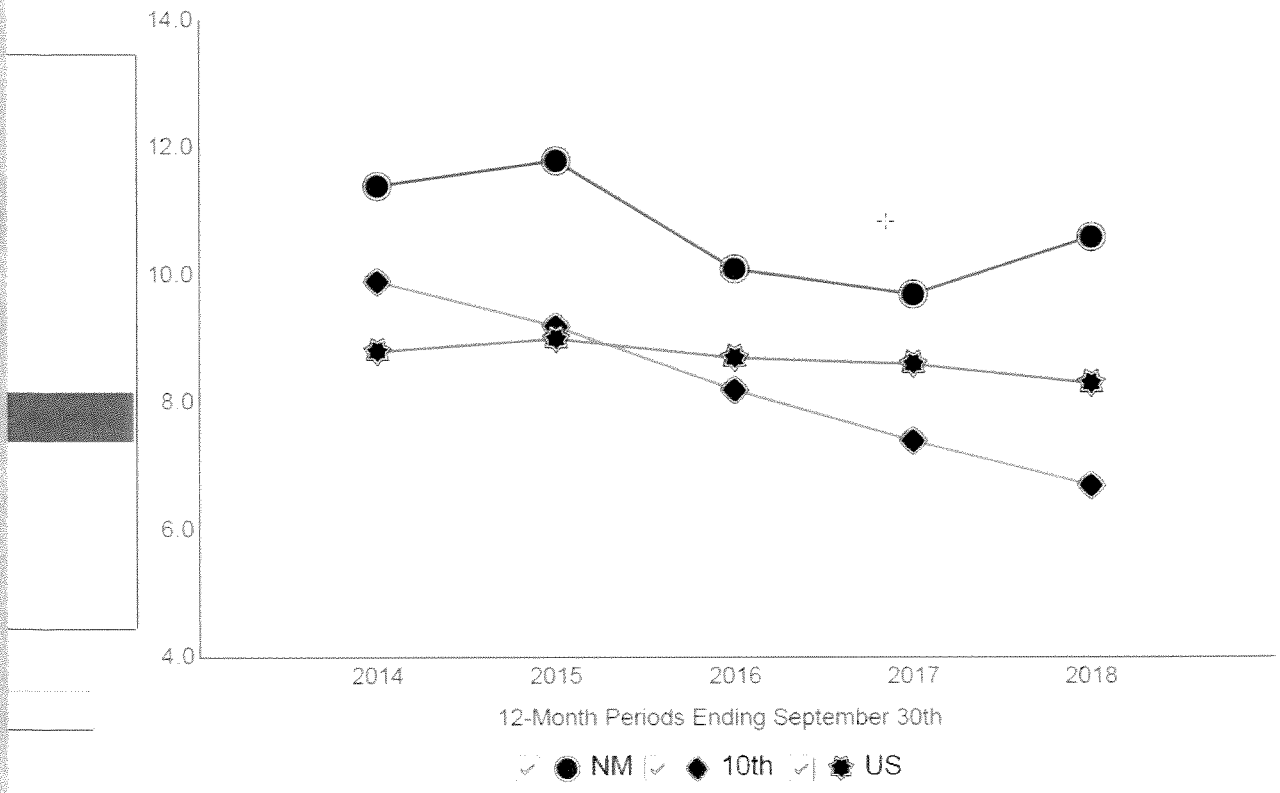
(year 2017 totals are in italics)



Key to color coding:

Red =	500 or more
Brown =	300-499
Green =	100-299
Blue =	Less than 100

Pro Se Filing Rate Over Time



	2014	2015	2016	2017	2018
NM	11.4%	11.8%	10.1%	9.7%	10.6%
10th Circuit	9.9%	9.2%	8.2%	7.4%	6.7%
US	8.8%	9.0%	8.7%	8.6%	8.3%

Office of the United States Trustee Review

34th Annual Bankruptcy Year in Review

Presentation by the Office of the United States Trustee

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The views and opinions expressed are those of the authors' and not the views and opinions of the United States Trustee Program.

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10 Things to Learn from the *In re Wright* Decision

1. Be aware of the requirements of 11 U.S.C. § 528 for debt relief agencies (and yes, if you file consumer cases, you are one).
    a. Written contract
    b. Identifies services to be provided
    c. Sets out the fees for such services

2. Accurate and complete fee disclosure required by § 329 and Rule 2016(b) are mandatory, not permissive.

3. Part 7, Question 16 - of Statement of Financial Affairs should be accurately answered.
    a. This seeks information on payments made for bankruptcy related services provided within one year of the bankruptcy filing.

4. A pure heart with no subjective intent to break the rules is not a defense to inaccurate disclosures.

5. Complete candor with the Court is not optional.
    a. "You never get a second chance to make a first impression."

6. Completely think through whether a bifurcated approach (pre and post filing) to fees is a good thing.

7. Do not blame your mistakes on staff you are supposed to be supervising.

8. Pay attention to Rule 1006(b)(3).
    a. All installments of the filing fee must be paid in full before the debtor or chapter 13 trustee may make further payments to an attorney or any other person who renders service to the debtor in connection with the case.

9. Agreeing to disgorge fees is not an equivalent substitute for a thorough explanation of the facts.

10. It is almost never a good sign when the judge begins a decision with a quote from Shakespeare.

2018 WL 4211570
Only the Westlaw citation is currently available.
United States Bankruptcy Court, N.D. Oklahoma.

IN RE: Roberta Ellarae WRIGHT, Debtor.
In re: Ian Gomes and Stephanie Ann Gomes, Debtors.
In re: Brittany Marie Dirkswager, Debtor.
In re: Ryan Michael Brown, Debtor.
In re: Tommy Lenard Guthrie and Debra Denise Guthrie, Debtors.
In re: Kiley Gene Lawrence, Debtor.
In re: Michael Joe Lawson and Sara Lynne Lawson, Debtors.
In re: Karen Dawn Inman, Debtor.
In re: David Charles Williams, Debtor.
In re: Daphne Leannette Robitaille, Debtor.
In re: Kimberly Leann Sullivan, Debtor.
In re: Brett Wayne Murphy and April Irene Conder, Debtors.
In re: Daniel Bruce Bowers and Janie Mae Bowers, Debtors.
In re: Dale Daniel Burris, Jr. and Sheila Mae Burris, Debtors.
In re: Darin Dwane Miller and Kathy Jo Miller, Debtors.
In re: Kenneth Charles Burton, Debtor.
In re: Kirby Dwayne Smith and Rebecca Leann Smith, Debtors.

Case No. 17-11936-M, Case No. 17-11172-M, Case No. 17-11410-M, Case No. 17-11411-M, Case No. 17-11555-M, Case No. 17-11557-M, Case No. 17-11558-M, Case No. 17-11559-M, Case No. 17-11688-M, Case No. 17-11689-M, Case No. 17-11690-M, Case No. 17-11930-M, Case No. 17-11932-M, Case No. 17-11933-M, Case No. 17-12027-M, Case No. 17-12028-M, Case No. 17-12029-M

Signed September 4, 2018.

Synopsis

Background: United States Trustee filed motion for review of transactions between debtors and attorney who had agreed to represent them and for imposition of possible sanctions against attorney, inter alia, for violating his fee disclosure obligations.

Holdings: The Bankruptcy Court, Terrence L. Michael, Chief Judge, held that:

[1] attorney violated his fee disclosure obligations under bankruptcy statute and rule;

[2] attorney not only violated fee disclosure requirements, but committed a fraud on his clients and on court; and

[3] as sanction, bankruptcy court would require disgorgement of all postpetition fees.

Ordered accordingly.

West Headnotes (19)

[1] **Bankruptcy**
Disclosure requirements

Fee disclosure obligations imposed on debtor's attorney by bankruptcy statute and rule apply regardless of whether the attorney applies for compensation from bankruptcy estate. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[2] **Bankruptcy**
Disclosure requirements

Fee disclosure obligations imposed on debtor's attorney are mandatory, not permissive. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[3] **Bankruptcy**
Disclosure requirements

Fee disclosure obligations imposed on debtor's attorney are designed to prevent bankruptcy attorneys from extracting more

than their fair share from prospective debtors willing to do whatever is necessary to obtain their counsel of choice and avoid unfavorable bankruptcy proceedings. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[4] **Bankruptcy**
Disclosure requirements

Bankruptcy counsel's fee revelations must be direct and comprehensive; coy or incomplete disclosures which leave the court to ferret out pertinent information from other sources are insufficient. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[5] **Bankruptcy**
Disclosure requirements

Absent complete disclosure, bankruptcy court is unable to make an informed judgment regarding the nature and amount of compensation paid or promised by debtor for legal services in contemplation of bankruptcy. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[6] **Bankruptcy**
Disclosure requirements

Consequences of failure on part of debtor's attorney to comply with his or her fee disclosure obligations can be severe, including forfeiture of right to receive any compensation for services rendered to debtor. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[7] **Bankruptcy**
Disclosure requirements

Disgorgement of fees due to inadequate fee disclosure by debtor's counsel is a matter left to sound discretion of bankruptcy court. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[8] **Bankruptcy**
Disclosure requirements

Entry of fee disgorgement order due to attorney's violation of fee disclosure obligations should be commensurate with the egregiousness of the violation and will depend on the particular facts of each case. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[9] **Bankruptcy**
Disclosure requirements

Court may sanction attorney's failure to make proper fee disclosure regardless of actual harm to the estate. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[10] **Bankruptcy**
Disclosure requirements

That debtor's attorney acted with a pure heart, and without any subjective intent to violate his fee disclosure obligations under bankruptcy statute and rule, is no defense to his failure to make the proper disclosures. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[11] **Bankruptcy**
Disclosure requirements

Negligent or inadvertent omissions do not vitiate a failure on part of debtor's attorney to properly disclose his or her fees. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[12] **Bankruptcy**
Disclosure requirements

Debtors' attorney violated his fee disclosure obligations under bankruptcy statute and rule

by sloppily disclosing in inaccurate amounts the fees which he had collected, by treating fees that his clients had agreed to pay as the fees that he had agreed to accept despite fact that, based on attorney's factoring agreement with collection agency that would retain a portion of any fee, he had actually agreed to accept hundreds of dollars less from each client, and by not disclosing this fee sharing arrangement with collection agency. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[13] **Bankruptcy**
Disclosure requirements

Debtors' attorney had duties of competence to his clients that transcended bankruptcy law, and he could not lay the blame for his inaccurate fee disclosures on the loss of his long-time assistant and his difficulties in training a new one. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[14] **Bankruptcy**
Disclosure requirements

Conduct of debtors' attorney in offering to make available upon request the factoring agreement pursuant to which he shared fees with collection agency did not satisfy his obligation pursuant to Bankruptcy Rule to disclose "the particulars of any such sharing or agreement to share." Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[15] **Attorney and Client**
Nature and term of office

Attorney and Client
Candor, and disclosure to opponent or court

Attorney becomes officer of the court upon taking an oath and meeting other requirements imposed by state law, and as officer of court, has duty to show complete candor toward that tribunal. 5 Okla. Stat. Ann. § 2.

Cases that cite this headnote

[16] **Attorney and Client**
Fraud

Bankruptcy
Disclosure requirements

By adopting bifurcated approach to fees, pursuant to which attorney had his clients enter into two separate retainer agreements, one for preparing and filing bare bones petition to which he would allocate whatever portion of agreed fee his clients could afford to pay up front, and a second postpetition agreement for continuing his representation after petition was filed, thereby rendering whatever fees could not be paid up front nondischargeable and collectable by agency that factored attorney's accounts, as well as by his failure to disclose payments that he received from agency pursuant to this factoring arrangement, attorney not only violated fee disclosure requirements, but committed a fraud on his clients and on court. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[17] **Bankruptcy**
Debtor's duties in general

Bankruptcy system is a fragile one, built on the principles of full and candid disclosure.

Cases that cite this headnote

[18] **Bankruptcy**
Disclosure requirements

As sanction for attorney's violation of his fee disclosure obligations in connection with undisclosed factoring arrangement with agency from which he secretly received a large portion of his fees, and whose collection of fees from clients he facilitated by employing a bifurcated retention/billing system that had the effect of rendering, as postpetition fees not dischargeable in bankruptcy, whatever fees

his clients could not afford to pay up front, bankruptcy court would require disgorgement of all such postpetition fees, and would find that postpetition retention agreements were void and unenforceable either by attorney or factoring agency. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

Cases that cite this headnote

[19] **Bankruptcy**
Filing fees
Bankruptcy
Disclosure requirements

While attorney violated Bankruptcy Rule governing the payment of court filing fee in installments, which required debtors who elected to pay the filing fee in installments to complete their installment payments prior to making any further payment for legal services to their bankruptcy counsel or anyone else, by entering into factoring arrangement that he should have realized would result in collection activity by factor and payments to it before filing fees were fully paid, bankruptcy court would not impose any additional sanctions beyond those imposed for attorney's fee disclosure violations, where all required court filing fees were eventually fully paid, either by debtors or attorney, and each of the debtors received their discharge. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 1006, 2016(b).

Cases that cite this headnote

Attorneys and Law Firms

J. Ken Gallon, Law Office of J. Ken Gallon, Miami, OK, for Debtor.

Katherine Vance, U.S. Trustee, Tulsa, OK, for U.S. Trustee.

Memorandum Opinion

TERRENCE L. MICHAEL, CHIEF JUDGE

"..., but at the length truth will out." [1]

*1 It is an oft-stated maxim that attorneys are "officers of the court." What exactly does it mean to be an "officer of the court?" Is it enough for an attorney to obtain a desired result for his or her client, even if they mislead, fail to fully inform, or violate rules of the Court in the process? Is a United States Bankruptcy Court a place where, when it comes to the areas of attorney conduct and non-disclosure, no harm equals no foul? Does ignorance of the law excuse misconduct? All of these questions are raised in the seventeen cases presently before the Court. For each question, the answer is the same: absolutely, unequivocally, no.

Before the Court is the Motion for Review of Debtor's Transactions with J. Ken Gallon, Attorney (the "Motion"), [2] filed in Case No. 17-11936-M, *Roberta Ellarae Wright*, by Katherine Vance, on behalf of the United States Trustee ("UST"), and 17 contested matters initiated *sua sponte* by the Court in each of the above captioned cases (the "Captioned Cases"). [3] Because the matters are based on substantially identical facts and raise identical issues regarding the conduct of J. Ken Gallon ("Gallon"), counsel for debtors in each of these cases, they were consolidated for purposes of resolution. [4] The matters discussed herein were first brought to the Court's attention in the *Wright* case, and the Court will continue to treat it as the lead case. A hearing on the Motion and these contested matters was held on May 10, 2018, at which the Court heard argument and took evidence related to the conduct of Gallon in these cases. The following findings of fact and conclusions of law are made pursuant to Federal Rule of Bankruptcy Procedure 7052, made applicable to this contested matter by Federal Rule of Bankruptcy Procedure 9014. [5]

Jurisdiction

The Court has jurisdiction over these bankruptcy cases pursuant to 28 U.S.C.A. § 1334(b). [6] Reference to the Court of these bankruptcy cases is proper pursuant to 28 U.S.C.A. § 157(a). Matters concerning the administration of the estate are core proceedings as defined by 28 U.S.C.A. § 157(b)(2)(A).

Findings of Fact

1. The BK Billing Model

*2 Gallon is a consumer debtors' attorney based in Miami, Oklahoma. BK Billing, LLC ("BK Billing"), a Utah limited liability company, is a finance company that provides factoring services to bankruptcy counsel in Chapter 7 cases. On May 11, 2017, Gallon executed an Accounts Receivable Assignment Agreement (the "AR Agreement"), in which he established a factoring arrangement with BK Billing.[7] The AR Agreement set up a mechanism where Gallon would sell his accounts receivable for "post-petition services" to Chapter 7 consumer debtors based on client contracts that he uploaded to the BK Billing system. Gallon ultimately factored, or sold, 14 client contracts to BK Billing under the AR Agreement ("the BK Billing Cases"). Under the original AR Agreement, Gallon agreed to transfer each account receivable in exchange for 70% of the total contractual value of the account, which amount was to be received by Gallon with 2-3 business days.[8] An amendment executed on July 5, 2017, increased the total amount paid to Gallon upon the submission of an account to 75% of the value of the contract, but lowered the amount immediately available to Gallon to 60%, and set the other 15% aside in an escrow account to be maintained by BK Billing as security for performance of the transferred accounts.[9] The AR Agreement gives BK Billing the "right to approve of [Gallon's] form engagement agreement prior to accepting any [accounts]."[10] In addition, Gallon is obligated to "cooperate with the collections by BK Billing of the [accounts], including, but not limited to providing evidence reasonably required for any legal action, arbitration, or mediation instituted by BK Billing for collection purposes, and permitting BK Billing to use [Gallon's] name, address, and telephone number for collection purposes."[11]

In addition to the factoring services, BK Billing provided Gallon with various pleadings and templates to effectuate a business model whereby Gallon would enter two separate retention agreements with his clients. The first, executed prior to filing a Chapter 7 bankruptcy case, was for services up to and including filing the petition. The second, executed after the case was filed, was for all remaining services that were rendered to a debtor post-petition.

At a hearing in these matters, Gallon testified that upon meeting with a new client, if he determined that the client was in need of immediate bankruptcy relief but was unable to pay his fee prior to filing the case, Gallon would present them with the "BK Billing Model."[12] Key features of the BK Billing Model include:

A. The debtors entered into a "Contract for Pre-Petition Legal Services in a Chapter 7 Bankruptcy Case" (the "Pre-Petition Agreement")[13] with Gallon.[14]

B. Under the Pre-Petition Agreement, the debtors were to pay Gallon a specified fee[15] for various pre-petition bankruptcy services, including "meeting and consulting with [Gallon] as needed," a "detailed analysis of [ ] client questionnaire," and "preparation and filing of a Chapter 7 Voluntary Petition, Statement About Social Security Numbers[.]"[16] The debtors agreed to pay additional fees for a "Pre-filing Credit Counseling Briefing Certificate" and a credit report.

C. The Pre-Petition Agreement gave the debtors the option to pay the Bankruptcy Court filing fee of $335 in full up front, apply to pay it in installments, or request that Gallon pay the fee and seek reimbursement from the debtors at a later time.

D. The Pre-Petition Agreement stated that Gallon's contractual responsibilities would end "upon completion of the filing of [the] bankruptcy case." It also stated that "the Law Firm will remain professionally obligated to serve as counsel for Client in the case until the Bankruptcy Court allows the Law Firm to formally withdraw."[17]

E. The Pre-Petition Agreement laid out various options regarding the completion of the debtors' bankruptcy case through discharge. The debtors could 1) retain Gallon under a second retainer agreement to be executed post-petition, where Gallon would complete the case for an additional specified fee;[18] 2) seek other counsel to complete the case; or 3) proceed without legal representation, i.e., *pro se*. If the debtors did not choose to retain Gallon for post-petition services within 10 days after filing the

bankruptcy petition, they agreed to consent to Gallon's withdrawal as counsel in the case. The Pre-Petition Agreement also placed the responsibility on the debtors to notify their creditors once the bankruptcy case was filed.

*3 F. After execution of the Pre-Petition Agreement, Gallon filed what is colloquially referred to as a "bare-bones" Chapter 7 petition on behalf of the debtors. That means the documents filed represent the bare minimum necessary to successfully open a bankruptcy case and invoke the automatic stay. In all cases, this consisted of Official Form 101, Voluntary Petition for Individuals Filing for Bankruptcy, required by Rule 1002(a); a Certificate of Counseling, required by Rule 1007(b)(3)(A); a list of creditors, required by Rule 1007(a)(1); and a Verification as to Official Mailing Matrix, required by Rule 1008.[19] In the seven cases filed prior to August 24, 2017, the initial filing also included Official Form 106Sum, Summary of Your Assets and Liabilities and Certain Statistical Information, required by Bankr. N.D. Okla. Local Rule 1007-1(G); Official Form 106D, Schedule D: Creditors Who Have Claims Secured by Property, required by Rule 1007(b)(1)(A); Official Form 106E/F, Schedule E/F: Creditors Who Have Unsecured Claims, required by Rule 1007(b)(1)(A); and Official Form 106Dec, Declaration About an Individual Debtor's Schedules, required by Rule 1008.[20]

G. In eleven of the seventeen Captioned Cases, Gallon filed Bankruptcy Form 103A, Application for Individuals to Pay the Filing Fee in Installments (the "Installment Application"), on behalf of the debtors, requesting that they be allowed to pay the Court filing fee in installments of $83.75 per month for four months, beginning one month from the date the petition was filed. At the time the Installment Application was filed in each case, the Court had no information regarding the financial condition of the debtors, i.e., no schedules of current income or expenditure had been filed.

H. In each of the BK Billing Cases, Gallon and the debtors executed a "Contract for Post-Petition Legal Services in a Chapter 7 Bankruptcy Case" (the "Post-Petition Agreement").[21] In the Post-Petition Agreement, the debtors agreed to retain Gallon to represent them in the post-petition proceedings of their bankruptcy case in exchange for a specified fee,[22] described as a non-refundable flat fee. Gallon agreed to perform the following services for debtors:

1) Preparation and filing of the Statement of Financial Affairs and Schedules;

2) Preparation for and attendance at the Section 341 Meeting of Creditors;

3) Review and attendance (if necessary) to motions for stay relief;

4) Review of any redemption agreements;

5) Review of any reaffirmation agreements;

6) Follow through with case administration and monitoring;

7) File motions to reopen (if necessary)[.][23]

I. The Post-Petition Agreement included the following statements:

I acknowledge and agree that as all of these fees are for post-petition services, they are not dischargeable in my Chapter 7 case. In the event of nonpayment of the agreed-upon fees, the Law Firm may commence legal proceedings for collection.

I understand that the Law Firm may assign my post-petition accounts receivable to BK Billing, LLC. I authorize the Law Firm or BK Billing to communicate with me via e-mail, text, and/or telephone. I explicitly give my consent to the Law Firm to share my client file information with BK Billing, including my contact information and social security number. I acknowledge that my payments to BK Billing will be reported to credit bureaus. I acknowledge that on-time payments can help my credit and late payments can hurt my credit. I have been provided an opportunity to ask the Law Firm questions regarding the Law Firm's accounts receivable assignment agreement with BK Billing. The Law Firm has answered all such questions to my satisfaction.

I agree to submit to the personal jurisdiction of the Oklahoma courts with respect to such action, and Oklahoma law will apply. If such collection

procedures shall become necessary, I agree to pay all reasonable costs of such collection, including reasonable attorney fees.

I understand that I am to notify my creditors of my bankruptcy case once my case is filed. [24]

J. Attached to the Post-Petition Agreement was a "Recurring Payment Authorization and Consent Form" in which the debtors authorized Gallon or BK Billing, LLC, referred to as an "independent billing company," to charge their debit card a specified fee per month until a specified amount was paid in full. [25] That form included the following statement:

***4** I give my consent that the Law Firm may sell or factor the accounts receivable associated with my contract to BK Billing. I acknowledge my payments would then be made directly to BK Billing on behalf of the Law Firm. I authorize the Law Firm or BK Billing to communicate with me via mail, e-mail, text, and/or telephone. I give my consent for the Law Firm to share my client file information, including my Social Security Number, with BK Billing for the purpose of processing and reporting my payments. I acknowledge that my payments may be reported to the Credit Bureaus. I acknowledge that on-time payments may help my credit and late payments may hurt my credit. [26]

K. In all of the Captioned Cases, Gallon filed the remaining schedules and statements required by § 521 and Rule 1007(b) sometime after the petition date.

L. Among the documents filed post-petition in each case was a Disclosure of Compensation of Attorney for Debtor ("Disclosure of Compensation"), which indicated that Gallon had agreed to accept a specified fee [27] "for services rendered or to be rendered on behalf of the debtor(s) in contemplation of or in connection with the bankruptcy case." [28] Gallon stated that he had received a specified fee [29] prior to filing the statement, leaving a specified balance due. [30] In every case, he checked the box next to the statement "I have not agreed to share the above-disclosed compensation with any other person unless they are members and associates of my law firm." Gallon also indicated that "by agreement with the debtor(s), the above-disclosed fee does not include the following service: 1) Lien Avoidance; 2) Adversary Proceeding; 3) Judgment Lien Removal; 4) Re-Affirmation (sic) Agreement; 5) Re-Affirmation (sic) Agreement Recession; 6) Amendment to Peition (sic), Schedules and Statements; 7) Objection to Discharge." [31]

2. The debtors

The facts in each of the Captioned Cases are as follows:

a. BK Billing Cases

Roberta Ellarae Wright, Case No. 17-11936-M

On September 12, 2017, Roberta Ellarae Wright ("Wright") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $200 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report. [32] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,350. Wright's case, Case No. 17-11936-M, was filed on September 28, 2017. On October 5, 2017, Wright executed a Post-Petition Agreement, where she agreed to pay $1,425 as a flat fee for Gallon to represent her in the completion of the case. [33] No receipt was offered to show the amount received by Gallon. What appears to be an internal information sheet was offered to show that Gallon received $200 from Wright. [34] Under the AR Agreement, Gallon received $855 from BK Billing upon submission of the Wright account, with an additional $213.75 placed in escrow. [35] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $75; leaving a balance due of $1,425. [36] Wright's Statement of Financial Affairs ("SOFA") disclosed that she had paid Gallon $125 (date not indicated), and included the description "Prepare petition schedules & Statements, credit counseling, credit report." [37] Gallon filed an Installment Application on behalf of Wright. [38] The final installment of Wright's filing fee was paid on December 6, 2017. BK Billing collected $118.75 from Wright on October 15, 2017, a date before the filing fee was paid in full. [39]

Ian Gomes and Stephanie Ann Gomes, Case No. 17-11172-M

*5 On June 12, 2017, Ian Gomes and Stephanie Ann Gomes (the "Gomeses") retained Gallon under a Pre-Petition Agreement, where they agreed to pay $100 for pre-petition services in a Chapter 7 bankruptcy case.[40] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in post-petition proceedings for $1,400. Their case, Case No. 17-11172-M, was filed on June 13, 2017. On that same date, the Gomeses executed a Post-Petition Agreement, where they agreed to pay $1,400 as a flat fee for Gallon to represent them in the completion of their case.[41] A receipt shows that Gallon received $500 in cash from Ian Gomes on June 12, 2017, which was described as a "Bankruptcy Retainer."[42] Under the original AR Agreement, Gallon received $980 from BK Billing upon submission of the Gomeses' account.[43] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[44] The Gomeses' SOFA disclosed they had paid Gallon $100 on June 12, 2017, and that "[t]he Debtors paid $100 dollars to prepare and to file the Petition, Credit Counseling, Creditors and Verification of Creditors. Debotrs [sic] paid $400 was for [sic] the Filing Fee, Credit Counseling Course, Debtors Education Course and the Credit Report."[45] The filing fee of $335 was paid on the filing date.

Ryan Michael Brown, Case No. 17-11411-M

On July 14, 2017, Ryan Michael Brown ("Brown") retained Gallon under a Pre-Petition Agreement, where he agreed to pay $158 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report.[46] The Pre-Petition Agreement gave him the option of retaining Gallon to complete his case in post-petition proceedings for $1,400. Brown's case, Case No. 17-11411-M, was filed on July 14, 2017. On July 24, 2017, Brown executed a Post-Petition Agreement, where he agreed to pay $1,350 as a flat fee for Gallon to represent him in the completion of the case.[47] A receipt shows that Gallon received $200 in cash from Brown on July 7, 2017, which was described as a "Attorney Fee's [sic] to file Petition; For CC CR."[48] Under the AR Agreement, Gallon received $810 from BK Billing upon submission of the Brown account, with an additional $202.50 placed in escrow.[49] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $150; leaving a balance due of $1,350. Brown's SOFA disclosed that he had paid Gallon $200 on July 11, 2017. Gallon filed an Installment Application on behalf of Brown.[50] The final installment of Brown's filing fee was paid on November 14, 2017. BK Billing collected $112.50 from Brown on September 15, 2017, September 29, 2017, and November 2, 2017, all dates before the filing fee was paid in full.[51]

Brittany Marie Dirkswager, Case No. 17-11410-M

Sometime in June 2017, Brittany Marie Dirkswager ("Dirkswager") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $1,400 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[52] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Dirkswager's case, Case No. 17-11410-M, was filed on July 14, 2017. On July 19, 2017, Dirkswager executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[53] No receipt was offered to show the actual amount received by Gallon. Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Dirkswager account, with an additional $210 placed in escrow.[54] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[55] Dirkswager's SOFA disclosed that she had paid Gallon $150 on June 22, 2017, and that "[t]he Debtor paid $100 dollars to file the Petition, Credit Counseling Course, Creditors, Verification of Creditors. The Debtor paid $50 for the Credit Counseling Course and Credit Report."[56] Gallon filed an Installment Application on behalf of Dirkswager.[57] The final installment of Dirkswager's filing fee was paid on November 28, 2017. BK Billing collected $58.33 from Dirkswager on September 1, 2017, September 26, 2017, October 7, 2017, October 20, 2017, and November 10, 2017, all dates before the filing fee was paid in full.[58]

Tommy Lenard Guthrie and Debra Denise Guthrie, Case No. 17-11555-M

*6 No Pre-Petition Agreement was offered to show when or the terms under which Tommy Lenard Guthrie and

Debra Denise Guthrie (the "Guthries") retained Gallon. Their Chapter 7 bankruptcy case, Case No. 17-11555-M, was filed on August 4, 2017. On August 9, 2017, the Guthries executed a Post-Petition Agreement, where they agreed to pay $1,400 as a flat fee for Gallon to represent them in the completion of their case.[59] A receipt shows that Gallon received $500 by credit card from Debra Guthrie on July 28, 2017, which was described as "for payment of Bankrupte" [sic].[60] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Guthries' account, with an additional $210 placed in escrow.[61] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[62] The Guthries' SOFA disclosed that they had paid Gallon $500 (date not indicated), and included the description "Form 122, prepare petition & creditor matrix, pull credit report and credit counseling."[63] The filing fee of $335 was paid on the filing date.

Karen Dawn Inman, Case No. 17-11559-M

On July 5, 2017, Karen Dawn Inman ("Inman") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $1,400 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[64] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Inman's case, Case No. 17-11559-M, was filed on August 4, 2017. On August 8, 2017, Inman executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[65] A receipt shows that Gallon received $100 from Inman on July 6, 2017, which was described as "CR & CC for BK."[66] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Inman, with an additional $210 placed in escrow.[67] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[68] Inman's SOFA disclosed that she had paid Gallon $150 (date not indicated), and included the description "Credit Report, Credit Couseling [sic] and attorney fees."[69] Gallon filed an Installment Application on behalf of Inman.[70] The final installment of Inman's filing fee was paid on November 22, 2017. BK Billing collected $116 from Inman on September 1, 2017, October 1, 2017, and November 1, 2017, all dates before the filing fee was paid in full.[71]

Kiley Gene Lawrence, Case No. 17-11557-M

On August 1, 2017, Kiley Gene Lawrence ("Lawrence") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $100 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[72] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Lawrence's case, Case No. 17-11557-M, was filed on August 4, 2017. On August 9, 2017, Lawrence executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[73] A receipt shows that Gallon received $153 in cash from Lawrence on August 1, 2017, which was described as "Attorney Fee's [sic] - BK."[74] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Lawrence account, with an additional $210 placed in escrow.[75] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[76] Lawrence's SOFA disclosed that she had paid Gallon $150 (date not indicated), and included the description "payment for credit report, credit counseling & fees."[77] Gallon filed an Installment Application on behalf of Lawrence.[78] The final installment of Lawrence's filing fee was paid on December 4, 2017. BK Billing collected $120 from Lawrence on September 6, 2017, October 6, 2017, and November 6, 2017, all dates before the filing fee was paid in full.[79]

Michael Joe Lawson and Sara Lynne Lawson, Case No. 17-11558-M

*7 On July 27, 2017, Michael Joe Lawson and Sara Lynne Lawson (the "Lawsons") retained Gallon under a Pre-Petition Agreement, where they agreed to pay $40 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[80] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in post-petition proceedings for $1,400. Their Chapter 7 bankruptcy case, Case No. 17-11558-M, was filed on August 4, 2017. On

August 15, 2017, the Lawsons executed a Post-Petition Agreement, where they agreed to pay $1,460 as a flat fee for Gallon to represent them in the completion of their case.[81] A receipt shows that Gallon received $100 in cash from Sara Lawson on July 27, 2017, which was described as "for BK [unreadable]."[82] Under the AR Agreement, Gallon received $876 from BK Billing upon submission of the Lawson account, with an additional $219 placed in escrow.[83] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $40; leaving a balance due of $1,460.[84] The Lawsons' SOFA disclosed that they had paid Gallon $100 (date not indicated), and included the description "prepare petition, e, f, creditor matrix and run credit report and credit counseling."[85] Gallon filed an Installment Application on behalf of the Lawsons.[86] The final installment of the Lawsons' filing fee was paid on November 30, 2017. BK Billing collected $121.66 from the Lawsons on September 1, 2017, October 1, 2017, and November 1, 2017, all dates before the filing fee was paid in full.[87]

Kimberly LeAnn Sullivan, Case No. 17-11690-M

An undated and unexecuted Pre-Petition Agreement was offered as evidence that Kimberly LeAnn Sullivan ("Sullivan") retained Gallon, where she agreed to pay $110 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report.[88] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Sullivan's case, Case No. 17-11690-M, was filed on August 24, 2017. On August 25, 2017, Sullivan executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[89] A receipt shows that Gallon received $500 in cash from Sullivan on August 17, 2017, without further notation.[90] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Sullivan account, with an additional $210 placed in escrow.[91] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[92] Sullivan's SOFA disclosed that she had paid Gallon $500 (date not indicated), and included the description "prepare petition, verify creditors, pull credit report, credit counseling."[93] The filing fee of $335 was paid on the filing date.

David Charles Williams, Case No. 17-11688-M

On August 22, 2017, David Charles Williams ("Williams") retained Gallon under a Pre-Petition Agreement, where he agreed to pay $200 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report.[94] The Pre-Petition Agreement gave him the option of retaining Gallon to complete his case in post-petition proceedings for $1,300. Williams's case, Case No. 17-11688-M, was filed on August 24, 2017. On August 25, 2017, Williams executed a Post-Petition Agreement, where he agreed to pay $1,300 as a flat fee for Gallon to represent him in the completion of the case.[95] A receipt shows that Gallon received $600 in cash from Williams on June 23, 2017, which was described as "Attorney Fee's [sic] BK"[96] The receipt also shows an amount due of $1680, and a balance (due) of $1080. Under the AR Agreement, Gallon received $780 from BK Billing upon submission of the Williams account, with an additional $195 placed in escrow.[97] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $200; leaving a balance due of $1,300. Williams's SOFA disclosed that he had paid Gallon $600 (date not indicated), and included the description "prepare petition, creditor matrix and verification [sic], obtain credit report, filing fee and credit counseling."[98] The filing fee of $335 was paid on the filing date.

Daphne Leannette Robitaille, Case No. 17-11689-M

***8** On August 1, 2017, Daphne Leannette Robitaille ("Robitaille") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $100 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report.[99] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Robitaille's case, Case No. 17-11689-M, was filed on August 24, 2017. On August 25, 2017, Robitaille executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[100] A receipt shows that Gallon received $150 in cash from Robitaille on August 1, 2017, which was described as "50 CC & CR & 100 [unreadable]."[101] Under the AR Agreement, Gallon received $840 from BK

Billing upon submission of the Robitaille account, with an additional $210 placed in escrow.[102] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[103] Robitaille's SOFA disclosed that she had paid Gallon $150 (date not indicated), and included the description "prepare petition, creditor verifcation [sic], credit report & credit counseling."[104] Gallon filed an Installment Application on behalf of Robitaille.[105] The final installment of Robitaille's filing fee was paid on December 18, 2017. BK Billing collected $116.66 from Robitaille on September 11, 2017, October 5, 2017, and November 5, 2017, all dates before the filing fee was paid in full.[106]

Daniel Bruce Bowers and Janie Mae Bowers, Case No. 17-11932-M

On September 22, 2017, Daniel Bruce Bowers and Janie Mae Bowers (the "Bowers") retained Gallon under a Pre-Petition Agreement, where they agreed to pay $500 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[107] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in post-petition proceedings for $1,400. Their Chapter 7 bankruptcy case, Case No. 17-11932-M, was filed on September 28, 2017. On September 29, 2017, the Bowers executed a Post-Petition Agreement, where they agreed to pay $575 as a flat fee for Gallon to represent them in the completion of their case.[108] A receipt shows that Gallon received $1,000 in cash from Bruce Bowers on September 19, 2017, which was described as "Retainer for BK."[109] Under the AR Agreement, Gallon received $345 from BK Billing upon submission of the Bower account, with an additional $86.25 placed in escrow.[110] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $1,000; leaving a balance due of $500.[111] The Bowers' SOFA disclosed that they had paid Gallon $1,000 (date not indicated), and included the description "prepare petition schedules & statements, filing fee, credit counseling."[112] The filing fee of $335 was paid on the filing date.

Dale Daniel Burris, Jr. and Sheila Mae Burris, Case No. 17-11933-M

An undated and unexecuted Pre-Petition Agreement was offered as evidence that Dale Daniel Burris, Jr. and Sheila Mae Burris (the "Burrises") retained Gallon, where they agreed to pay $90 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[113] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in post-petition proceedings for $1,410. Their Chapter 7 bankruptcy case, Case No. 17-11933-M, was filed on September 28, 2017. On September 29, 2017, the Burrises executed a Post-Petition Agreement, where they agreed to pay $1,400 as a flat fee for Gallon to represent them in the completion of their case.[114] No receipt was offered to show the actual amount received by Gallon. Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Burris account, with an additional $210 placed in escrow.[115] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,250; had received $0; leaving a balance due of $1,250.[116] The Burrises' SOFA disclosed that they had paid Gallon $150 (date not indicated), and included the description "Prepare petition, schedules & statements, credit report, credit counseling."[117] Gallon filed an Installment Application on behalf of the Burrises.[118] The final installment of the Burrises' filing fee was paid on November 27, 2017. BK Billing collected $58.34 from the Burrises on October 13, 2017, October 21, 2017, and November 4, 2017, all dates before the filing fee was paid in full.[119]

Brett Wayne Murphy and April Irene Conder, Case No. 17-11930-M

*9 On September 28, 2017, Brett Wayne Murphy ("Murphy") and April Irene Conder ("Conder"), retained Gallon under a Pre-Petition Agreement, where they agreed to pay $100 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[120] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in post-petition proceedings for $1,400. Their Chapter 7 bankruptcy case, Case No. 17-11930-M, was filed on September 28, 2017. On September 29, 2017, Murphy and Conder executed a Post-Petition Agreement, where they agreed to pay $1,400 as a flat fee for Gallon to represent them in the completion of their case.[121] A receipt shows that Gallon received $500 in cash from

Murphy and Conder on September 20, 2017.[122] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Murphy/Conder account, with an additional $210 placed in escrow.[123] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[124] Murphy's and Conder's SOFA disclosed that they had paid Gallon $500 (date not indicated), and included the description "Prepare petition ceritors [sic] & verifcation. [sic] Credit report, credit counseling & filing fee."[125] The filing fee of $335 was paid on the filing date.

b. Non-Factored Cases[126]

Kenneth Charles Burton, Case No. 17-12028-M

On October, 12, 2017, Kenneth Charles Burton ("Burton") filed a petition for relief under Chapter 7 of the Bankruptcy Code, Case No. 17-12028-M. The bare bones petition was filed by Gallon as counsel. A receipt shows that Gallon received $150 in cash from Burton on October 3, 2017."[127] No Pre-Petition Agreement was offered to show the terms under which Burton retained Gallon. According to Gallon, no Post-Petition Agreement was executed with Burton because Gallon had ceased doing business with BK Billing and had agreed to complete the Burton case pending further Court review.[128] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[129] Burton's SOFA disclosed that he had paid Gallon $150 (date not indicated), and included the description "prepare petition, schedules, statements, credit counseling, credit report150"[130] Gallon filed an Installment Application on behalf of Burton.[131]

Darin Dwane Miller and Kathy Jo Miller, Case No. 17-12027-M

On October, 12, 2017, Darin Dwane Miller and Kathy Jo Miller (the "Millers") filed a petition for relief under Chapter 7 of the Bankruptcy Code, Case No. 17-12027-M. The bare bones petition was filed by Gallon as counsel. No receipt was offered to show the amount received by Gallon. No Pre-Petition Agreement was offered to show the terms under which the Millers retained Gallon. According to Gallon, no Post-Petition Agreement was executed with the Millers because Gallon had ceased doing business with BK Billing and had agreed to complete the Miller case pending further Court review.[132] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $130; leaving a balance due of $1,370.[133] The Millers' SOFA disclosed that they had paid Gallon $200 (date not indicated), and included the description "prepare petition schedules & statements, credit counseling, credit report."[134] Gallon filed an Installment Application on behalf of the Millers.[135] Although Gallon had no contract or agreement with the Millers, they voluntarily paid Gallon $1,325 post-petition.[136]

Kirby Dwayne Smith and Rebecca Leann Smith, Case No. 17-12029-M

***10** On October, 12, 2017, Kirby Dwayne Smith and Rebecca Leann Smith (the "Smiths") filed a petition for relief under Chapter 7 of the Bankruptcy Code, Case No. 17-12029-M. The bare bones petition was filed by Gallon as counsel. A receipt shows that Gallon received $200 by check from Kirby Smith on October 9, 2017.[137] No Pre-Petition Agreement was offered to show the terms under which the Smiths retained Gallon. According to Gallon, no Post-Petition Agreement was executed with the Smiths because Gallon had ceased doing business with BK Billing and had agreed to complete the Smith case pending further Court review.[138] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $125; leaving a balance due of $1,375.[139] The Smiths' SOFA disclosed that they had paid Gallon $200 (date not indicated), and included the description "prepare petition schedules & Statements, credit report, credit counseling, Debtor Education."[140] Gallon filed an Installment Application on behalf of the Smiths.[141]

c. Conventional Cases

Between June 13, 2017, the date Gallon filed the first BK Billing Case, and October 17, 2017, the date of the hearing where Gallon first disclosed his relationship with BK Billing to the Court, Gallon filed nineteen cases that did not utilize the services of BK Billing (the "Conventional Cases").[142] Gallon's disclosed attorney fee[143] in the Conventional Cases ranged from $900 to $1,250, and averaged $1,160.53.[144] In each of the

Conventional Cases, the debtor paid the filing fee on the filing date and did not seek to pay it in installments. In each of the Conventional Cases, Gallon attached all required schedules and statements to the petition on the filing date, i.e., none were filed as bare-bones cases. [145]

3. Court proceedings

Completely unaware of the bifurcated contractual relationships Gallon had entered into with his clients, the Court set the Disclosure of Compensation in the *Wright* case for hearing, noting that the Court had previously ruled that some of the excluded services were required to be performed by counsel for debtors in every Chapter 7 case. [146] In addition, the Court noticed an unusual spate of Installment Applications filed by Gallon in the previous few months without sufficient information for Court review, and set the Installment Agreement in the *Wright* case for hearing to inquire about this practice. It was at this hearing (the "October 17 Hearing") that the Court was first informed of Gallon's use of the BK Billing Model and his factoring arrangement with BK Billing. The UST stated that she had only become aware of the arrangement the day before when preparing for the hearing with Gallon. At the hearing, the Court bluntly asked Gallon to explain "Why wouldn't this be disclosed?" His answer:

> *11 MR. GALLON: Well, it might -- the reason I did not disclose it, Your Honor, in my mind, is that once -- I mean, what, what is happening here is there, is a bifurcation process.
>
> So the client hires you to perform, to, to file the petition and the creditors and the verification. Then once that's done, you have a second meeting, which is the bifurcation, where they rehire you to finish the, the schedules, statements, and all that. Then once that's done, that's whenever it is factored. And so it is just my way of receiving, I mean, I could collect it from the debtor instead of BK Billing. And so I didn't, I mean, I just didn't think it was something that I was required to disclose. It's my receivable. It's monies that's owed me. [147]

Two days after the October 17 Hearing, Gallon filed an amended Disclosure of Compensation in the *Wright* case (the "Amended Disclosure"), which added the following statement:

> Counsel may receive financing from a third-party via a financing or factoring facility. Although in undersigned counsel's view such financing or factoring facility should not be considered an agreement to share compensation, the terms of such agreement will include the granting by undersigned counsel of an interest in the undersigned counsel's accounts and the creditor may have rights to receive payment from the client. Any such financing or factoring facility agreement will clearly provide that client must first give consent to the party relationship and under no circumstances will any of the terms of the financing or factoring facility agreement require counsel to disclose any information that is either confidential or may be considered a privileged communication with the client. The actual agreement will be made available upon request by a party-in-interest. [148]

Gallon has since filed the same Amended Disclosure in all of the BK Billing Cases.

The Court continued the hearing to allow the UST to gather more information regarding Gallon's relationship with BK Billing and decide on a course of action. At the continued hearing, the Court heard from the UST and Gallon, and discussed the UST's Motion filed in the *Wright* case. [149] The Motion proposed an agreement between the UST and Gallon, whereby Gallon would: 1) disgorge his fee in the *Wright* case "in part;" 2) continue to represent debtors in any of the open BK Billing Cases; 3) continue representing debtors in the Non-Factored Cases; [150] and 4) cease doing business with BK Billing going forward. A proposed agreed order along those lines was later submitted to (not filed with) the Court that indicated Gallon would disgorge $855 received post-petition (presumably from BK Billing) and cancel any post-petition contract that allowed BK Billing to further collect from Wright. The Court found the

proposed agreement wholly unsatisfactory, and held a telephonic hearing on January 31, 2018, at which it requested more information from Gallon regarding the Captioned Cases. The Court subsequently issued an Order Scheduling Hearing and Directing Counsel for the Debtor to Address Issues of Compensation.[151] The Order outlined the concerns of the Court and advised Gallon of the various types of sanctions or remedies the Court was contemplating in these cases. Among the possible sanctions was disgorgement of all fees paid by debtors in any of the Captioned Cases and the indemnification by Gallon of his clients against any further collection action brought by BK Billing.[152]

*12 On May 10, 2018, the Court held a hearing (the "May 10 Hearing") on these matters. Gallon's arguments and defenses were presented in a pre-hearing brief.[153] His arguments can be summarized as follows:

1. Use of the BK Billing Model made Gallon financially worse off than if he had used a conventional, pre-petition billing method.[154]

2. Gallon relied on BK Billing, based on the vigor and sophistication used to induce him to adopt the BK Billing Model. BK Billing appeared to be a highly professional organization, presented a polished sales pitch, and was a high-level sponsor of the National Association of Consumer Bankruptcy Attorneys annual meeting. Gallon was given the impression that its model was widely and successfully used.[155]

3. Gallon did not disclose the BK Billing Model because 1) he relied on BK Billing to advise him of the need to change his usual procedures; 2) he was not aware that BK Billing provided a specific form of disclosure to be filed with the Court; and 3) "it just did not occur to him that such disclosure was required."[156]

4. Gallon did not understand that participating in the BK Billing program might involve violation of bankruptcy law.[157]

5. A significant motivation for Gallon to offer the BK Billing Model "was to allow clients to obtain relief from their debt problems more quickly."[158]

6. Gallon's long-time bankruptcy legal assistant was distracted and ultimately quit during the period he was utilizing the BK Billing Model. He states that many of the mistakes in the disclosures and statements were due to that distracted assistant, his own inept efforts at learning the software, and finally the learning curve of training a new assistant.[159]

7. Each of the debtors in the Captioned Cases received a discharge without complaint or complication. Gallon suggests that this is a vindication of any charge that his pre-petition investigation and analysis of the debtors' cases, without preparing schedules and statements, was inadequate.[160]

When questioned about the reason for the bifurcation and performance of services post-petition, Gallon admitted that the practice was not for the benefit of debtors, but was done solely to facilitate the BK Billing Model of collection, by making all fees attributed to post-petition work non-dischargeable.[161] Gallon valued his time at $250 per hour, based on the amount he charges in Chapter 13 cases. He acknowledged that he did not accurately account for services provided pre-petition to debtors, and often spent more time working on their cases pre-petition than the debtors paid for before the case was filed. For example, if a debtor paid only $100 prior to the case being filed, Gallon acknowledged that he spent more than 4/10 of an hour preparing the case for filing.[162] Under the BK Billing Model, Gallon then shifted the remainder of his fee to be collected post-petition, even though some of the services being compensated had already been provided pre-petition.

*13 Gallon testified that he immediately stopped using the services of BK Billing as soon as he became aware of the concerns of the Court and the UST. The UST stipulated that Gallon cooperated fully in amending disclosures and providing documents and information during their investigation of these matters.[163] At the May 10 Hearing, Gallon reiterated his understanding that the factoring of his fee to BK Billing did not involve any sharing of fees since they were simply a collection agency and not providing any services to the debtors.[164]

Conclusions of Law

1. Counsel's duty of disclosure pursuant to § 329

Section 329 of the Bankruptcy Code lies at the heart of these cases. Under that section, if a debtor pays or makes an agreement to pay an attorney for services related to a bankruptcy case,[165] that attorney is required to file a statement with the Court that discloses: 1) any compensation paid to the attorney, if the payment was made after one year before the date of the filing of the petition; 2) any compensation agreed to be paid to the attorney, if such agreement was made after one year before the date of the filing of the petition; and 3) the source of such compensation paid or agreed to be paid.[166] For Chapter 7 debtors' counsel, § 329 is implemented by Bankruptcy Rule 2016(b).[167] In addition to the duties specified in § 329, the Rule adds the requirement that counsel disclose "whether the attorney has shared or agreed to share the compensation with any other entity," including "the particulars of any such sharing or agreement to share by the attorney[.]"[168] These disclosures are required to be filed within 14 days after the case is filed, and supplemented within 14 days after any payment or agreement not previously disclosed.[169]

*14 [1] [2] [3] [4] [5] Counsel's duties disclosure apply whether or not the attorney applies for compensation from the estate.[170] The disclosure requirements of § 329 are "mandatory not permissive."[171] The statute is "designed to prevent bankruptcy attorneys from extracting more than their fair share from prospective debtors willing to do whatever is necessary to obtain their counsel of choice and avoid unfavorable bankruptcy proceedings."[172] "Counsel's fee revelations must be direct and comprehensive. Coy or incomplete disclosures which leave the court to ferret out pertinent information from other sources are not sufficient."[173] "Absent complete disclosure, the court is unable to make an informed judgment regarding the nature and amount of compensation paid or promised by the debtor for legal services in contemplation of bankruptcy."[174]

Rule 2017 directs the court to review any payments or transfers, or agreements for either, made directly or indirectly by debtors to an attorney, either before or after the filing of the bankruptcy case, to determine if those payments or transfers are excessive.[175] According to the advisory committee's note appended to the Rule's original publication,

> This rule ... is premised on the need for and appropriateness of judicial scrutiny of arrangements between a debtor and his attorney to protect the creditors of the estate and the debtor against overreaching by an officer of the court who is in a peculiarly advantageous position to impose on both the creditors and his client.[176]

If the payment or agreement is found to exceed the reasonable value of the services provided by the attorney, the Court may cancel the agreement or disgorge any such payment to its source.[177]

*15 [6] [7] [8] [9] [10] [11] The consequences of an attorney's failure to comply with the disclosure requirements of § 329 can be severe, including forfeiting the right to receive *any* compensation for services rendered to the debtor.[178] "Disgorgement of fees as a result of inadequate disclosure by counsel is a matter left to the sound discretion of the bankruptcy court."[179] "The imposition of a disgorgement order should be commensurate with the egregiousness of the conduct and will depend on the particular facts of each case."[180] "The Court may sanction failure to disclose 'regardless of actual harm to the estate.' "[181] This Court has previously adopted a strict position regarding failure of debtors' counsel to disclose compensation arrangements to the Court:

> This Court takes the requirement of full disclosure under § 329 seriously, for to do less is to judicially repeal the statute....Were the Court to require less than full disclosure, the purpose behind § 329(a) would be defeated. Counsel could avoid disclosure of any or all of the fees paid to them by making a covert decision that the undisclosed fee was so unrelated to the bankruptcy case that its disclosure was not required, and eliminating the possibility of Court review in the process. The Court's ability to make a meaningful review of attorney's fees would be

> hindered if not destroyed. Such a result can be neither condoned nor allowed. [182]

Nothing presented to the Court in these matters suggests that any lesser standard should prevail. Nor does the Court find that a "pure heart," without a subjective intent to violate the Code or Rules, provides counsel any defense to the failure to file the proper disclosures under § 329. [183] "Negligent or inadvertent omissions 'do not vitiate the failure to disclose.' " [184]

[12] The Court finds Gallon's original Disclosure of Compensation in each of these cases to be grossly misleading and indicative of a wanton disregard—*to the point of negligence*—for the level of candor required under § 329. Some of Gallon's errors defy comprehension. For example, in the *Wright* case, Gallon disclosed that he had agreed to accept $1,500 for legal services with a balance due of $1,425, when he actually had agreed to receive $855, plus $213.75 paid to escrow, from BK Billing. [185] The statement is flat-out deceptive, whether or not that is what Gallon intended. The disclosure conflates the total amount a debtor agreed to pay for his services with the amount he agreed to accept for his services, even though those amounts differ by several hundred dollars in each of the BK Billing Cases.

[13] Other errors demonstrate the general level of sloppiness evident in much of Gallon's record keeping. For example, in the *Wright* case, Gallon disclosed that "prior to the filing of this statement I have received $75," even though his Pre-Petition Agreement indicated Ms. Wright had agreed to pay $200 plus an additional $42 in fees. An internal office memo indicated that she had actually paid $200. Although Gallon blamed such mistakes on the loss of his long-time assistant and the difficulty in training a new one, Gallon has duties of competence to his clients that transcend bankruptcy law. [186] He should not accept clients if he does not have the basic skills to file their cases in a complete and competent manner. This Court does not accept laying the blame at the foot of an employee as an excuse.

***16** Of equal concern is that Gallon indicated in each Disclosure of Compensation that he had not shared his fee with any other person. Both in his written brief and testimony, Gallon insisted on his understanding that he was not sharing fees because "it was his receivable" that he could dispose of or sell in any way he wanted, and that BK Billing was simply a collection agency. The Court is not particularly concerned here with the legal or ethical violations involved with any possible sharing arrangement. [187] What concerns the Court is Gallon's rather brazen position, with no citation to authority, that collection of a fee from his client that is split between himself and BK Billing does not constitute sufficient "sharing of compensation" that it should—*at a minimum*—be disclosed to the Court. Courts have found that a failure to comply with disclosure requirements is sanctionable even if proper disclosure would have shown no violation of the Code or Rules. [188]

[14] Gallon filed an Amended Disclosure in each of the cases in an effort to remedy the deficiencies in the original. His efforts fell woefully short. His statement that "counsel may receive financing from a third-party" does not adequately disclose that in each of the affected cases he *did in fact* receive such financing, and on what terms. He goes on to state his view that the arrangement does not involve sharing of fees, but gives no particulars of the arrangement. Offering to make the agreement available upon request does not satisfy Rule 2016(b)'s requirement of disclosing "the particulars of any such sharing or agreement to share." [189]

2. Counsel's duty of candor to the tribunal

[15] In addition to the statutory duties provided in the Bankruptcy Code, Gallon has other duties to his clients and the Court based on his role as an officer of the court. An attorney becomes an officer of the court upon taking an oath and meeting other requirements imposed by state law. [190] In Oklahoma, that oath requires counsel to show complete candor toward the tribunal. [191] Oklahoma Rule of Professional Conduct 3.3 reinforces the requirement of candor. [192] Such candor is vital to the integrity of the bankruptcy process itself.

***17** The Court is troubled by Gallon's practice of charging a higher fee to his clients that use the BK Billing Model than to his conventional clients. Gallon charged his average conventional client $1,250 when the fee was fully paid prior to filing a debtor's petition. Under the BK Billing Model, a debtor was charged a total of $1,500 for attorney fees. From the debtor's perspective, that is a $250

premium, or 20% above the fee charged in a conventional case, for the convenience of paying the fee over 12 months. From Gallon's perspective, the math is even worse. For example in the *Wright* case, Gallon invoiced Wright's account to BK Billing for $1,425. He actually received $855 from BK Billing. That means Wright agreed to pay a 66% markup over the amount Gallon actually received for providing her services.[193] Additionally, if Gallon was willing to accept roughly $1,069, or 75% of $1,425, in a typical BK Billing Case, assuming he received the escrowed payments, the Court could rightly conclude that he consistently overcharges his conventional clients for the value of his services. Gallon's only defense of the practice of charging higher fees to BK Billing clients was that it was encouraged by BK Billing as part of their training package.

[16] It is clear to the Court that a prominent feature of the BK Billing Model is the designation of the bulk of services as "post-petition" in order to render them beyond the Chapter 7 discharge and therefore collectable by BK Billing. There are (at least) two problems with this approach. First, by waiting until after the petition is filed to perform most of the actual services, such as filing out schedules and statements, counsel risks overlooking essential information regarding the debtors' financial condition, which may have been missed in the cursory interview conducted pre-petition. Counsel may discover too late that he or she should have chosen a different chapter, or not filed the case at all. Second, the amount of Gallon's fees designated pre- or post-petition was motivated by how much money the debtor was able to pay up front, and not related in any way to when Gallon's services were actually performed. Valuing his time at $250 per hour, Gallon admitted that in several cases he spent much more time pre-petition than he was paid for, but then designated the remaining fee as "post-petition," thus turning an otherwise dischargeable pre-petition claim into a non-discharged claim.[194] Such a scheme works a fraud both on the debtor and the Court.

Of additional concern to the Court is that Gallon indicated that the source of the compensation to be paid to him was the debtor, even though Bankruptcy Form 2030 presented him with another option. Courts have consistently held that payment of funds from a third-party payor to pay a debtor's legal fees does not alter counsel's obligation of proper disclosure.[195] In each of the BK Billing Cases except *Gomes*, Gallon received a direct deposit equal to 60% of the invoiced account value from BK Billing, with an agreement he would be paid an additional 15% if the accounts were sufficiently remitted by the debtors.[196] Clearly, "the "source of such compensation" is directly required to be disclosed under § 329. Gallon tries to deflect responsibility for this failure by stating that he relied on BK Billing to train and advise him on the use of their model. Such reliance on BK Billing in the discharge of his professional duties and judgment is a breach of the Oklahoma Rules of Professional Conduct.[197] Despite not being "trained" or provided a form by BK Billing, Gallon certainly understood that he was only indirectly being compensated by his clients, but that the actual funds he received came directly from BK Billing. He should have known that the information provided to the Court in the Disclosure of Compensation filed in these cases was grossly misleading, if not out right false. His declaration that it simply "did not occur to him that such disclosure was required" is both disheartening and astonishing. This Court has published no less than three opinions directly related to the failure of debtors' counsel to properly disclose all financial dealings with their clients.[198] As an officer of the Court, Gallon is expected to be aware of such rulings.

*18 Gallon tries to rationalize his failures by citing the blind faith he put in BK Billing as a company. He suggests that he was induced to adopt the BK Billing Model based on the company's slick sales pitch and high-profile sponsorship of a leading bankruptcy conference. While the Court does not doubt that BK Billing rolled out a persuasive marketing campaign, the Court believes that any reasonable attorney would have at least questioned the "too good to be true" aspect of the model. Instead, Gallon blindly adopted the BK Billing Model, without conducting even a minimal inquiry into the legal or ethical issues that such a system might raise. The Court finds that such abdication of his professional judgment is unreasonable.

[17] [18] This Court has previously noted the bankruptcy system is a fragile one, built on the principles of full and candid disclosure.[199] Its operation and survival rely on the integrity and professionalism of its practitioners. Only through serendipity were these matters brought to the Court's attention. "This is not an area where the Court will engage in or tolerate a game of

'catch me if you can,' or allow 'I guess I did not know better' to be a palatable excuse."[200] The Court finds Gallon's disclosures regarding the nature and source of his compensation in these cases to be grossly inadequate to the point of being misleading. The Court is aware that it has discretion when determining the degree of sanctions for non-disclosure.[201] The Court finds Gallon's entire fee in each of these cases to be unreasonable. His failures are sufficiently severe and pervasive to warrant disgorgement. The Court would be justified in disgorging all fees received by Gallon or collected by BK Billing, but finds that such an order would be administratively unworkable, since some of the funds paid by the debtors pre-petition were allocated to court fees and other miscellaneous services. The Court will limit disgorgement to the value of fees actually collected by BK Billing from each of the debtors in the Captioned Cases after their petitions were filed.[202] Such funds shall be remitted by Gallon to the debtor that made the payment. The Post-Petition Agreements in each case are found to be void, and neither Gallon nor BK Billing may enforce any claim against the debtors under those contracts.[203] The Court is aware this is a harsh sanction, but anything less would minimize the serious nature of Gallon's conduct.

3. Debtors' violations of Rule 1006

[19] Section 1930 of title 28 of the United States Code sets out the schedule of fees to be collected by the clerk when a bankruptcy case is filed. The statute explicitly allows a debtor in a voluntary case to pay the required fee in installments.[204] Rule 1006 implements this statute, but adds that a debtor that utilizes the installment provision may make no further payments "to an attorney or any other person who renders services to the debtor in connection with the case" until the filing fee is paid in full.[205]

***19** In eleven of the seventeen Captioned Cases, Gallon filed an Installment Application. In each of those cases, the application included a statement executed by both the debtors and Gallon that the debtors understood they must pay their entire filing fee before they make any more payments or transfer any more property to an attorney *or anyone else* for services in connection with their bankruptcy case.[206] In eight of those cases, due to the scheme orchestrated by Gallon, debtors unwittingly made payments to BK Billing toward Gallon's attorney fee before their entire filing fee was paid to the Court, in direct violation of Rule 1006. The remaining three cases were not submitted to BK Billing for factoring, therefore no violation occurred.

Gallon, as an attorney admitted to practice before this Court, is charged with knowing and understanding the Federal Rules of Bankruptcy Procedure, as well as the applicable provisions of the Bankruptcy Code. His signature on the Installment Application was a violation of both his ethical and statutory duties. Rule 9011(b)(3) outlines counsel's ethical duty of candor in signing an application submitted to the Court:

> (b) Representations to the court
>
> By presenting to the court (whether by signing, filing, submitting, or later advocating) a petition, pleading, written motion, or other paper, an attorney or unrepresented party is certifying that to the best of the person's knowledge, information, and belief, formed after an inquiry reasonable under the circumstances,–
>
> * * *
>
> (3) *the allegations and other factual contentions have evidentiary support* or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery[.][207]

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") was enacted "to correct perceived abuses of the bankruptcy system."[208] Among its reforms were §§ 526–528, which target debt relief agencies, "*i.e.*, professionals who provide bankruptcy assistance to consumer debtors."[209] As a debt relief agency, Gallon is bound by duties of candor therein.[210] The relevant subsection of § 526 reads as follows:

> (a) A debt relief agency shall not–
>
> * * *
>
> (2) *make any statement, or counsel or advise any assisted person* or prospective assisted person *to make a statement* in a document filed in a case or proceeding under this title, *that is untrue or misleading*, or that upon the exercise of reasonable care, should have been known by such agency to be untrue or misleading[.][211]

Considering he set these events in motion by factoring his fee to BK Billing, Gallon knew or should have known that BK Billing would begin collection activity prior to the debtors' court fees being paid in full. He is also charged with knowing that such payment to BK Billing was a violation of the debtors' duties under Rule 1006. His signature on the Installment Agreements is a violation of his duty of candor under both Rule 9011(b)(3) and § 526(a)(2). Gallon compounded the violation of § 526(a)(2) by advising his clients to sign the Installment Agreements and causing them to make misleading statements regarding their payment of his fees.

The Court does not take these violations lightly. The bankruptcy system requires complete candor from both debtors and their engaged professionals.[212] Standing alone, the Court would find cause to sanction Gallon under Rule 9011(c) or § 526(c)(5) for filing and endorsing the debtors' misleading statements found in the Installment Agreements. The Court notes that in all eleven cases, all required Court filing fees were eventually fully paid, either by the debtors or Gallon, and each of the debtors received their discharge. Therefore, despite the authority to do so, the Court will not impose additional sanctions.

4. Counsel's duties under BAPCPA

***20** As soon as Gallon became aware of his missteps in these cases, he worked diligently to assist the UST to investigate this matter and cut ties with BK Billing. As such, he offered no defense of the BK Billing Model of bifurcating services into pre- and post-petition categories or its factoring practice, which required debtors to incur debt to pay their attorney's fee. Several courts across the country have faced variations on this theme. Some have offered advice and recommendations in order to craft an acceptable scheme whereby attorneys may offer bifurcated services.[213] Others have noted that various provisions added to the Code by BAPCPA appear to thwart such schemes.[214] This Court has reviewed the cases carefully and believes that BAPCPA presents serious impediments to the legality of this kind of bifurcated services scheme, such as the BK Billing Model.[215] The difficulty here is that no one appears in these cases to defend the model or offer an alternative argument to the Court. That seems like shaky ground to rule or comment on the validity of the model. Because the Court has disposed of these matters under section 329, it is not necessary to review them further on alternative grounds. Therefore the Court will wait until issues of bifurcation of services and fee factoring are before it in an actual case or controversy before it weighs in on §§ 526 and 528. The Court raises these issues in the hope that counsel considering use of a similar scheme will carefully review the legal and ethical provisions of BAPCPA and state ethics rules *before* they file a petition in this district.

Conclusion

***21** Gallon must disgorge the value of all fees actually collected by BK Billing from the debtors after their petitions were filed in each of the Captioned Cases. Such funds shall be remitted by Gallon to the debtor that made the payment. The Post-Petition Agreements in each case are found to be void, and neither Gallon nor BK Billing may enforce any claim against the debtors under those contracts. A separate order consistent with this Memorandum Opinion is entered concurrently herewith in each of the Captioned Cases.

All Citations

--- B.R. ----, 2018 WL 4211570

Footnotes

1 William Shakespeare, *The Merchant of Venice* act 2, sc. 2.

2 Case No. 17-11936-M, *at Docket No. 38.*

3 Although not all of the Captioned Cases were originally assigned to the undersigned Judge, they were transferred to him after the facts described herein came to light, so that counsel's conduct could be reviewed by the Court in a comprehensive manner.

4 *See* Order Scheduling Hearing and Directing Counsel for the Debtor to Address Issues of Compensation, Case No. 17-11936-M, *at Docket No. 60.* An Order and Notice of Hearing was entered in each of the other Captioned Cases, alerting each debtor to their opportunity to appear and be heard in this matter.

5 The Court will recite the factual differences for each specific case, but notes that those differences are immaterial to the Court's analysis and resolution of these matters.

6 Unless otherwise noted, all statutory references are to sections of the United States Bankruptcy Code, 11 U.S.C.A. § 101 *et seq.* Unless otherwise noted, all references to a "Rule" or "the Rules" are to the Federal Rules of Bankruptcy Procedure.

7 Trial Ex. 22.

8 *Id.* at 1, § 1.

9 Trial Ex. 23 at 1, § 2.1. Except for Case No. 17-11172-M, *Gomes*, all of the BK Billing Cases were submitted pursuant to the amended AR Agreement. All further references to the AR Agreement will refer to the agreement as amended.

10 Trial Ex. 22 at 2, § 4.2.

11 *Id.* at 3, § 4.4.

12 Gallon did not use this terminology, but the Court will use the term "BK Billing Model" to refer to the two contract bifurcated filing system provided by BK Billing, which included the factoring of Gallon's attorney fees.

13 *See, e.g.*, Trial Ex. 14.1 (*Wright*). Substantially similar agreements were entered with each of the debtors in the Captioned Cases.

14 In the contracts with debtors, Gallon represented himself as the "Law Firm." The Court will use the term "Gallon" to refer to both J. Ken Gallon, as attorney, and any law firm he may represent.

15 This amount varied by debtor. Details for each debtor are discussed in the next section.

16 Trial Ex. 14.1 at 1.

17 *Id.*

18 *See supra* note 15. As far as the Court is aware, all of the debtors that executed a Pre-Petition Agreement chose this option.

19 The *Sullivan* case included this list of documents plus the Official Form 106Sum, Summary of Your Assets and Liabilities and Certain Statistical Information, required by Bankr. N.D. Okla. Local Rule 1007-1(G).

20 These cases were *Gomes*, *Dirkswager*, *Brown*, *Inman*, *Lawrence*, *Guthrie*, and *Lawson*.

21 Trial Ex. 14.2.

22 *See supra* note 15.

23 Trial Ex. 14.2 at 1.

24 *Id.* at 2–3 (emphasis added). The last sentence was included in each of the Post-Petition Agreements, but it was set out separately in bold and underlined, with instruction for the debtor to initial the clause, only in the *Wright* case.

25 *See supra* note 15.

26 *Motion*, Case No. 17-11936-M, *at Docket No. 38* at 9.

27 *See supra* note 15.

28 Bankruptcy Form 2030.

29 *See supra* note 15.

30 *Id.*

31 Trial Ex. 14.5.

32 Trial Ex. 14.1.

33 Trial Ex. 14.2.

34 Trial Ex. 14.3.

35 Trial Ex. 14.4. This is based on an invoice amount of $1,425, which BK Billing was to collect from Wright.

36 Trial Ex. 14.6.

37 Trial Ex. 14.7.

38 Case No. 17-11936-M, *at Docket No. 4*.

39 Trial Ex. 14.4.

40 Trial Ex. 1.1.

41 Trial Ex. 1.2.

42 Trial Ex. 1.3.

43 Trial Ex. 1.4. *See supra* note 13.

44 Trial Ex. 1.6.

45 Trial Ex. 1.7.

46 Trial Ex. 2.1.

47 Trial Ex. 2.2.
48 Trial Ex. 2.3.
49 Trial Ex. 2.4.
50 Case No. 17-11411-M, *at Docket No. 2.*
51 Trial Ex. 2.4.
52 Trial Ex. 3.1. The Court hesitates to refer to the $1,400 as a "typo" because it was written into a blank by hand, but it does appear to be a mistake.
53 Trial Ex. 3.2.
54 Trial Ex. 3.4.
55 Trial Ex. 3.6.
56 Trial Ex. 3.7.
57 Case No. 17-11410-M, *at Docket No. 2.*
58 Trial Ex. 3.4.
59 Trial Ex. 4.2.
60 Trial Ex. 4.3.
61 Trial Ex. 4.4.
62 Trial Ex. 4.6.
63 Trial Ex. 4.7.
64 Trial Ex. 5.1.
65 Trial Ex. 5.2.
66 Trial Ex. 5.3. The method of payment was not indicated.
67 Trial Ex. 5.4.
68 Trial Ex. 5.6.
69 Trial Ex. 5.7.
70 Case No. 17-11559-M, *at Docket No. 2.*
71 Trial Ex. 5.4.
72 Trial Ex. 6.1. Handwriting obscures the amount of $53 for a credit report on the exhibit submitted to the Court, but its intent in changing the meaning of the printed text is unclear.
73 Trial Ex. 6.2.
74 Trial Ex. 6.3.
75 Trial Ex. 6.4.
76 Trial Ex. 6.6.
77 Trial Ex. 6.7.
78 Case No. 17-11557-M, *at Docket No. 2.*
79 Trial Ex. 6.4.
80 Trial Ex. 7.1.
81 Trial Ex. 7.2.
82 Trial Ex. 7.3.
83 Trial Ex. 7.4.
84 Trial Ex. 7.6.
85 Trial Ex. 7.7.
86 Case No. 17-11558-M, *at Docket No. 2.*
87 Trial Ex. 7.4.
88 Trial Ex. 8.1. The document was executed by Gallon, but not by Sullivan.
89 Trial Ex. 8.2.
90 Trial Ex. 8.3.
91 Trial Ex. 8.4.
92 Trial Ex. 8.6.
93 Trial Ex. 8.7.
94 Trial Ex. 9.1.

95 Trial Ex. 9.2.
96 Trial Ex. 9.3.
97 Trial Ex. 9.4.
98 Trial Ex. 9.7.
99 Trial Ex. 10.1.
100 Trial Ex. 10.2.
101 Trial Ex. 10.3.
102 Trial Ex. 10.4.
103 Trial Ex. 10.6.
104 Trial Ex. 10.7.
105 Case No. 17-11689-M, *at Docket No. 3.* An amended application was filed at Docket No. 10 to change the due dates for payments. This amended application was later granted by the Court. *See Docket No. 16.*
106 Trial Ex. 10.4.
107 Trial Ex. 11.1.
108 Trial Ex. 11.2.
109 Trial Ex. 11.3.
110 Trial Ex. 11.4.
111 Trial Ex. 11.6
112 Trial Ex. 11.7
113 Trial Ex. 12.1. The document was not executed by any party.
114 Trial Ex. 12.2.
115 Trial Ex. 12.4. This is based on an invoice amount of $1,400, which BK Billing was to collect from the Burrises.
116 Trial Ex. 12.6. On October 20, 2017, an amended Disclosure of Compensation was filed, which recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400. *See* Case No. 17-11933-M, *at Docket No. 18.*
117 Trial Ex. 12.7.
118 Case No. 17-11933-M, *at Docket No. 3.*
119 Trial Ex. 12.4.
120 Trial Ex. 13.1.
121 Trial Ex. 13.2.
122 Trial Ex. 13.3.
123 Trial Ex. 13.4.
124 Trial Ex. 13.6.
125 Trial Ex. 13.7.
126 The Non-Factored Cases are those initiated by Gallon under the BK Billing Model, but whose accounts were never submitted to BK Billing because of the issues raised at the October 17 Hearing. *See infra* text accompanying note 150.
127 Trial Ex. 15.3.
128 Trial Tr. at 25–26, May 10, 2018, Case No. 11936-M, *at Docket No. 71.*
129 Trial Ex. 15.6.
130 Trial Ex. 15.7.
131 Case No. 17-12028-M, *at Docket No. 3.* An amended application was filed at Docket No. 13 to change the due dates for payments. This amended application was later granted by the Court. *See Docket No. 15.*
132 Trial Tr. at 25–26, May 10, 2018, Case No. 11936-M, *at Docket No. 71.*
133 Trial Ex. 16.6.
134 Trial Ex. 16.7.
135 Case No. 17-12027-M, *at Docket No. 3.* An amended application was filed at Docket No. 14 to change the due dates for payments. This amended application was later granted by the Court. *See Docket No. 15.*
136 According to Gallon, "Mrs. Miller called me up and basically told me that she had received her income tax return and that she wanted me to get paid and I told her I didn't really know what was going on, but she said that she wanted to pay

me. And so I accepted the payment." *See* Trial Tr. at 27 *ll.* 12–16, May 10, 2018, Case No. 11936-M, *at Docket No. 71. See also* Trial Ex. 19 (note regarding *Miller* case).

137 Trial Ex. 17.3.

138 Trial Tr. at 25–26, May 10, 2018, Case No. 11936-M, *at Docket No. 71.*

139 Trial Ex. 17.6.

140 Trial Ex. 17.7.

141 Case No. 17-12029-M, *at Docket No. 3.* An amended application was filed at Docket No. 11 to change the due dates for payments. This amended application was later granted by the Court. *See Docket No. 13.*

142 The Conventional Cases are Case Nos. 17-11177-M; 17-11179-M; 17-11180-M; 17-11181-M; 17-11182-M; 17-11183-M; 17-11407-M; 17-11408-M; 17-11409-M; 17-11561-M; 17-11562-M; 17-11683-M; 17-11684-M; 17-11685-M; 17-11686-M; 17-11831-M; 17-11934-M; 17-12025-M; 17-12026-M. In addition, Gallon filed one case during this period that had the hallmarks of a BK Billing Case, e.g., an Installment Application was filed, attorney fees of $1,500 were disclosed, etc., but it was dismissed because the debtor was ineligible for a discharge due to § 727(a)(8) (debtor had received a discharge within 8 years before the filing date). *See* Case No. 17-11556-M, *Tracie Lynn Tennant.*

143 These amounts are taken from the Disclosure of Compensation filed in each of the Conventional Cases. These amounts differ from that disclosed on the SOFA in every case.

144 This number represents the attorney fee collected by Gallon, and does not include any amounts for filing fees or other fees Gallon collected for credit reports, counseling, etc.

145 The only required pleading Gallon failed to consistently attach to the petition in the Conventional Cases was the Payment Advice Certification, which was sporadically submitted as a later pleading.

146 *See In re Minardi*, 399 B.R. 841, 849–850 (Bankr. N.D. Okla. 2009). After the Disclosure of Compensation was set for hearing, but prior to the October 17 Hearing, Gallon amended the Disclosure of Compensation in the *Wright* case to exclude only 1) Adversary Proceeding; 2) Amendment(s) to Schedules to add creditors; and 3) Objection to Discharge from the services he agreed to perform for debtors. *See* Trial Ex. 14.6.

147 *See* Trial Tr. at 7 *ll.* 4–18, October 17, 2017, Case No. 17-11936-M, *at Docket No. 29.*

148 Trial Ex. 14.6.

149 Case No. 17-11936-M, *at Docket No. 38.*

150 These are the *Burton*, *Miller*, and *Smith* cases.

151 Case No. 17-11936-M, *at Docket No. 60.* An order giving the debtors an opportunity to appear and be heard at the hearing was also entered in each of the other 16 Captioned Cases.

152 *Id.* at. 7.

153 J. Ken Gallon's Brief Regarding Issues of Compensation, Case No. 17-11936-M, *at Docket No. 65.*

154 *Id.* at 3.

155 *Id.* at 5.

156 *Id.* at 6.

157 *Id.*

158 *Id.*

159 *Id.*

160 *Id.* at 6–7.

161 Trial Tr. at 58 *ll.* 9–24, May 10, 2018, Case No. 11936-M, *at Docket No. 71.*

162 *Id.* at 60.

163 *Id.* at 9–10.

164 *Id.* at 64.

165 The language of the statute requires disclosure of compensation paid or agreed to be paid "for services rendered or to be rendered in contemplation of or in connection with the case by such attorney." § 329(a). There is no issue in this case that the services rendered by Gallon to the various debtors were not related to their bankruptcy cases.

166 (a) Any attorney representing a debtor in a case under this title, or in connection with such a case, whether or not such attorney applies for compensation under this title, shall file with the court a statement of the compensation paid or agreed to be paid, if such payment or agreement was made after one year before the date of the filing of the petition, for services rendered or to be rendered in contemplation of or in connection with the case by such attorney, and the source of such compensation.
§ 329(a).

167 (b) Disclosure of compensation paid or promised to attorney for debtor

Every attorney for a debtor, whether or not the attorney applies for compensation, shall file and transmit to the United States trustee within 14 days after the order for relief, or at another time as the court may direct, the statement required by § 329 of the Code including whether the attorney has shared or agreed to share the compensation with any other entity. The statement shall include the particulars of any such sharing or agreement to share by the attorney, but the details of any agreement for the sharing of the compensation with a member or regular associate of the attorney's law firm shall not be required. A supplemental statement shall be filed and transmitted to the United States trustee within 14 days after any payment or agreement not previously disclosed.

Rule 2016(b).

168 *Id.*

169 *Id.*

170 § 329. *See In re Brown*, 371 B.R. 486, 497 (Bankr. N.D. Okla. 2007), *amended by* 371 B.R. 505 (Bankr. N.D. Okla. 2007).

171 *See Turner v. Davis, Gillenwater & Lynch (In re Inv. Bankers, Inc.)*, 4 F.3d 1556, 1565 (10th Cir. 1993) (*citing In re Bennett*, 133 B.R. 374, 378 (Bankr. N.D. Tex. 1991)).

172 *Id.* (*citing In re NBI, Inc.*, 129 B.R. 212, 222 (Bankr. D. Colo. 1991)).

173 *In re Woodward*, 229 B.R. 468, 474 (Bankr. N.D. Okla. 1999) (*quoting In re Saturley*, 131 B.R. 509, 517 (Bankr. D. Me. 1991)).

174 *In re Perrine*, 369 B.R. 571, 580 (Bankr. C.D. Cal. 2007).

175 *See In re Brown*, 371 B.R. at 497. Rule 2017 reads:

(a) Payment or transfer to attorney before order for relief

On motion by any party in interest or on the court's own initiative, the court after notice and a hearing may determine whether any payment of money or any transfer of property by the debtor, made directly or indirectly and in contemplation of the filing of a petition under the Code by or against the debtor or before entry of the order for relief in an involuntary case, to an attorney for services rendered or to be rendered is excessive.

(b) Payment or transfer to attorney after order for relief

On motion by the debtor, the United States trustee, or on the court's own initiative, the court after notice and a hearing may determine whether any payment of money or any transfer of property, or any agreement therefor, by the debtor to an attorney after entry of an order for relief in a case under the Code is excessive, whether the payment or transfer is made or is to be made directly or indirectly, if the payment, transfer, or agreement therefor is for services in any way related to the case.

Rule 2017.

176 Rule 2017 advisory committee's note (*citing* 2 Collier on Bankruptcy ¶ 329.02 (15th ed. 1980); MacLachlan, Bankruptcy 318 (1956)).

177 § 329 (b) reads:

(b) If such compensation exceeds the reasonable value of any such services, the court may cancel any such agreement, or order the return of any such payment, to the extent excessive, to--

(1) the estate, if the property transferred--

(A) would have been property of the estate; or

(B) was to be paid by or on behalf of the debtor under a plan under chapter 11, 12, or 13 of this title; or

(2) the entity that made such payment.

178 *In re Inv. Bankers*, 4 F.3d at 1565; *In re Smitty's Truck Stop, Inc.*, 210 B.R. 844, 848–49 (10th Cir. BAP 1997).

179 *In re Brown*, 371 B.R. at 499. *See also In re Stewart*, 583 B.R. 775, 783 (Bankr. W.D. Okla. 2018) (*citing In re Brown*).

180 *In re Brown*, 371 B.R. at 499 (*citing In re Hackney*, 347 B.R. 432, 443 (Bankr. M.D. Fla. 2006)) (internal citations and quotations omitted).

181 *In re Smitty's Truck Stop*, 210 B.R. at 849 (*citing In re Maui 14K, Ltd.*, 133 B.R. 657, 660 (Bankr. D. Haw. 1991)).

182 *In re Woodward*, 229 B.R. at 474–75 (disgorgement of all fees). *See also In re Lewis*, 309 B.R. 597 (Bankr. N.D. Okla. 2004) (same); *In re Brown*, 371 B.R. at 486 (same). *Accord In re Inv. Bankers*, 4 F.3d at 1565–66; *In re Smitty's Truck Stop*, 210 B.R. at 848.

183 *In re Stewart*, 583 B.R. at 782.

184 *In re Smitty's Truck Stop*, 210 B.R. at 848 (*quoting Neben & Starrett, Inc. v. Chartwell Fin. Corp. (In re Park-Helena Corp.)*, 63 F.3d 877, 881 (9th Cir. 1995)) (internal citations omitted).

185 Trial Ex. 14-4, 14-6.

186 Rules of Prof'l Conduct, Rule 1.1, Okla. Stat. tit. 5, ch. 1, app. 3-A ("A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness, and preparation reasonably necessary for the representation.").

187 *See, e.g.*, § 504(a) ("Except as provided in subsection (b) of this section, a person receiving compensation or reimbursement under section 503(b)(2) or 503(b)(4) of this title may not share or agree to share–(1) any such compensation or reimbursement with another person[.]") This statute suggests that while sharing of fees is prohibited in some circumstances, not every receipt of fees related to a bankruptcy case is affected. *But see* Rules of Prof'l Conduct, Rule 5.4(a), Okla. Stat. tit. 5, ch. 1, app. 3-A ("A lawyer or law firm shall not share legal fees with a nonlawyer[.]") (listing several exceptions that do not apply here).

188 *In re Stewart*, 583 B.R. at 782. *See also In re Waldo*, 417 B.R. 854, 893 (Bankr. E.D. Tenn. 2009).

189 Rule 2016(b).

190 Rules of Prof'l Conduct, Preamble cmt. 1, Okla. Stat. tit. 5, ch. 1, app. 3-A ("A lawyer, as a member of the legal profession, is a representative of clients, *an officer of the legal system* and a public citizen having special responsibility for the quality of justice.") (emphasis added).

191 The oath required to practice law in Oklahoma reads as follows:

> I do solemnly swear that I will support, protect and defend the Constitution of the United States, and the Constitution of the State of Oklahoma; that I will do no falsehood, or consent that any be done in court, and if I know of any I will give knowledge thereof to the judges of the court, or some one of them, that it may be reformed; I will not wittingly, willingly or knowingly promote, sue, or procure to be sued, any false or unlawful suit, or give aid or consent to the same; I will delay no person for lucre or malice, but will act in the office of attorney in all courts according to my best learning and discretion with all good fidelity as well to the court as to my client, so help me God.

Okla. Stat. tit. 5, ch. 1, § 2. *See also id.*, app. 5, § 1.

192 Rule 3.3. Candor Toward The Tribunal:

> (a) A lawyer shall not knowingly:
> (1) make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by the lawyer[.]

Rules of Prof'l Conduct, Rule 3.3, Okla. Stat. tit. 5, ch. 1, app. 3-A. *See also id.*, Preamble cmt. 12, Okla. Stat. tit. 5, ch. 1, app. 3-A ("Every lawyer is responsible for observance of the Rules of Professional Conduct.").

193 Even if Gallon had received the additional escrow payment, Wright would have paid a 33% markup over the amount Gallon received.

194 Trial Tr. at 60, May 10, 2018, Case No. 11936-M, *at Docket No. 71*.

195 *In re Stewart*, 583 B.R. at 781.

196 Under the original AR Agreement, Gallon received 70% of the invoiced Gomes account, with no escrowed payment.

197 *See, e.g.*, Rules of Prof'l Conduct, Rule 5.4(c), Okla. Stat. tit. 5, ch. 1, app. 3-A ("A lawyer shall not permit a person who recommends, employs, *or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services.*") (emphasis added); *Id.* Rule 1.8(f) ("A lawyer shall not accept compensation for representing a client from one other than the client unless: (1) the client gives informed consent; (2) there is *no interference with the lawyer's independence of professional judgment* or with the client-lawyer relationship[.]") (emphasis added); Rule 1.7(a) ("A concurrent conflict of interest exists if: ...(2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to ... *a third person or by a personal interest of the lawyer.*") (emphasis added).

198 *In re Woodward*, 229 B.R. at 468; *In re Lewis*, 309 B.R. at 597; *In re Brown*, 371 B.R. at 486.

199 *In re Lewis*, 309 B.R. at 602.

200 *Id.* at 603.

201 *In re Brown*, 371 B.R. at 499; *In re Stewart*, 583 B.R. at 783.

202 To be abundantly clear, these fees are ordered disgorged *from Gallon*, and not from BK Billing, over which the Court has not exercised jurisdiction. In addition, the Court will not disturb the voluntary payment of $1,325 made directly to Gallon from the Millers in Case No. 17-12027-M.

203 The Court offers no opinion on how this ruling affects the contractual duties between Gallon and BK Billing.

204 28 U.S.C. § 1930(a) (hanging paragraph).

205 Rule 1006(b)(3)("All installments of the filing fee must be paid in full before the debtor or chapter 13 trustee may make further payments to an attorney or any other person who renders services to the debtor in connection with the case.").

206 *See, e.g.*, Case No. 17-11936-M, *at Docket No. 4.*

207 Rule 9011(b)(3) (emphasis added).

208 *Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 231–32, 130 S.Ct. 1324, 176 L.Ed.2d 79 (2010).

209 *Id.* at 232, 130 S.Ct. 1324.

210 *Id.* (holding that consumer debtors' attorneys qualify as "debt relief agencies," as defined in § 101(12A), and are therefore subject to §§ 526–528).

211 § 526 (as amended by Bankruptcy Technical Corrections Act of 2010, Pub. L. 111-327, § 2(a)(2), 124 Stat. 3557) (emphasis added).

212 *See Grogan v. Garner*, 498 U.S. 279, 287, 111 S.Ct. 654, 112 L.Ed.2d 755 (1991) (The Bankruptcy Code "limits the opportunity for a completely unencumbered new beginning to the 'honest but unfortunate debtor.' ") (*quoting Local Loan Co. v. Hunt*, 292 U.S. 234, 244, 54 S.Ct. 695, 78 L.Ed. 1230 (1934)). *See also* Rule 9011.

213 *Bethea v. Robert J. Adams & Assocs.*, 352 F.3d 1125, 1128 (7th Cir. 2003) (proposes bifurcation of services model; pre-BAPCPA case); *Walton v. Clark & Washington, P.C.*, 469 B.R. 383 (Bankr. M.D. Fla. 2012) (endorses specific bifurcation of services model; provides guidance); *In re Slabbinck*, 482 B.R. 576, 584 (Bankr. E.D. Mich. 2012) (same); *In re Waldo*, 417 B.R. 854 (Bankr. E.D. Tenn. 2009) (rejects model utilized by counsel; endorses bifurcation of services model in dicta); *In re Lawson*, 437 B.R. 609 (Bankr. E.D. Tenn. 2010) (same); *In re Griffin*, 313 B.R. 757, 769–70 (Bankr. N.D. Ill. 2004) (endorses bifurcation of services model in dicta; provides guidance); *In re Abdel-Hak*, No. 12-46329-MBM, 2012 WL 5874317, at *7 (Bankr. E.D. Mich. Nov. 16, 2012) (same).

214 *See In re Jackson*, No. 14-11415, 2014 WL 3722019 (Bankr. W.D. La. July 24, 2014) (two contract procedure used by counsel did not comply with "material requirements" of § 528; both agreements found void under § 526(c)(1)); *In re Green*, No. 14-11458, 2014 WL 3724986 (Bankr. W.D. La. July 24, 2014) (same). *But see In re Slabbinck*, 482 B.R. at 584 n.1 (acknowledged §§ 526–528 added by BAPCPA, but ignored because not raised by any party).

215 Relevant subsections of § 526 read as follows:

> (a) A debt relief agency shall not–
>
> (1) fail to perform any service that such agency informed an assisted person or prospective assisted person it would provide in connection with a case or proceeding under this title;
>
> (2) make any statement, or counsel or advise any assisted person or prospective assisted person to make a statement in a document filed in a case or proceeding under this title, that is untrue or misleading, or that upon the exercise of reasonable care, should have been known by such agency to be untrue or misleading;
>
> (3) misrepresent to any assisted person or prospective assisted person, directly or indirectly, affirmatively or by material omission, with respect to–
>
> (A) the services that such agency will provide to such person; or
>
> (B) the benefits and risks that may result if such person becomes a debtor in a case under this title; or
>
> (4) advise an assisted person or prospective assisted person to incur more debt in contemplation of such person filing a case under this title or to pay an attorney or bankruptcy petition preparer a fee or charge for services performed as part of preparing for or representing a debtor in a case under this title.
>
> (b) Any waiver by any assisted person of any protection or right provided under this section shall not be enforceable against the debtor by any Federal or State court or any other person, but may be enforced against a debt relief agency.
>
> (c)(1) Any contract for bankruptcy assistance between a debt relief agency and an assisted person that does not comply with the material requirements of this section, section 527, or section 528 shall be void and may not be enforced by any Federal or State court or by any other person, other than such assisted person.
>
> (2) Any debt relief agency shall be liable to an assisted person in the amount of any fees or charges in connection with providing bankruptcy assistance to such person that such debt relief agency has received, for actual damages, and for reasonable attorneys' fees and costs if such agency is found, after notice and a hearing, to have–
>
> (A) intentionally or negligently failed to comply with any provision of this section, section 527, or section 528 with respect to a case or proceeding under this title for such assisted person;
>
> (B) provided bankruptcy assistance to an assisted person in a case or proceeding under this title that is dismissed or converted to a case under another chapter of this title because of such agency's intentional or negligent failure to file any required document including those specified in section 521; or
>
> (C) intentionally or negligently disregarded the material requirements of this title or the Federal Rules of Bankruptcy Procedure applicable to such agency.
>
> * * *

NOTELAW

(5) Notwithstanding any other provision of Federal law and in addition to any other remedy provided under Federal or State law, if the court, on its own motion or on the motion of the United States trustee or the debtor, finds that a person intentionally violated this section, or engaged in a clear and consistent pattern or practice of violating this section, the court may--

(A) enjoin the violation of such section; or

(B) impose an appropriate civil penalty against such person.

§ 526 (as amended by Bankruptcy Technical Corrections Act of 2010, Pub. L. 111-327, § 2(a)(2), 124 Stat. 3557).

Section 528 provides in part:

(a) A debt relief agency shall–

(1) not later than 5 business days after the first date on which such agency provides any bankruptcy assistance services to an assisted person, but prior to such assisted person's petition under this title being filed, execute a written contract with such assisted person that explains clearly and conspicuously–

(A) the services such agency will provide to such assisted person; and

(B) the fees or charges for such services, and the terms of payment;

(2) provide the assisted person with a copy of the fully executed and completed contract;

§ 528(a)(1–2).

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Problematic Consumer Debtor Attorney's Fee Arrangements and the Illusion of "Access to Justice"

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The Supreme Court has recognized that under the Bankruptcy Code, the traditional payment model for attorneys representing individual consumer debtors in chapter 7 cases is straightforward: the attorney receives payment for the case in full, generally as a flat fee, prior to filing the case.[1] In recent years, however, attorneys, law firms, and third parties have sought to creatively reimagine the terms and methods of payment for representation of consumer chapter 7 debtors. Some of these alternative arrangements may run afoul of bankruptcy law and ethical obligations. As the statutory watchdog of the bankruptcy system,[2] the United States Trustee Program is acutely familiar with identifying these issues and, where appropriate, taking action to enforce the Code and redress the harms resulting from unethical and substandard practices.[3]

This article will first examine the legal and factual background for the creation of alternative consumer debtor attorney's fee arrangements. Next, the terms and potentially problematic features of some of the more common alternative arrangements the USTP has observed, including illegitimate schemes, fee-only chapter 13 cases, bifurcated fee agreements, and factored fees, will be discussed. Finally, the article will discuss the flawed "access to justice" arguments sometimes raised cynically by practitioners in defense of harmful and noncompliant fee structures.

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[1] *Lamie v. United States Trustee*, 540 U.S. 526, 537, 124 S. Ct. 1023, 1032 (2004) ("It appears to be routine for debtors to pay reasonable fees for legal services before filing for bankruptcy to ensure compliance with statutory requirements.").

[2] The United States Trustee Program has jurisdiction in all judicial districts except those in North Carolina and Alabama.

[3] 28 U.S.C. § 586(a)(3); *see also* H.R. Rep. No. 95-595, at 99 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6049 (United States Trustees "serve as bankruptcy watch-dogs to prevent fraud, dishonesty, and overreaching in the bankruptcy arena.").

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Background

In contrast to chapters 11 and 13, the Bankruptcy Code is relatively silent as to payment of debtor attorney's fees in chapter 7 cases. Because chapter 7 debtor attorneys do not represent the estate, they are not employed under section 327 of the Code, nor may they receive compensation from the estate under section 330.[4] Nevertheless, bankruptcy courts retain the ability to review and reduce unreasonable or undisclosed compensation in chapter 7 cases under section 329 of the Code, and chapter 7 debtor attorneys' transactions with their clients are governed where applicable by sections 526, 527, and 528 of the Code.[5]

The automatic stay is imposed upon filing a voluntary petition.[6] With limited exceptions,[7] it bars collection of pre-petition debt during the pendency of the case. Pre-petition debtor attorney's fees are subject to both the automatic stay and discharge.[8] However, the Ninth Circuit Court of Appeals has held that fees owed for services rendered post-petition, even when based on a pre-petition contract, may be collected without running afoul of the stay or discharge.[9] The only other court of appeals that has addressed this question soundly rejected this approach.[10]

The realities of consumer debtor practice are also relevant. Defenders of alternative fee arrangements point quickly to filing numbers that have trended downward in recent years. True enough, the number of filings doubled between fiscal years 2007 to 2010 and then dropped to current levels that approximate the number of cases filed in 2007.[11] However, it also bears remembering that debtor

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[4] *Lamie*, 540 U.S. at 534, 124 S. Ct. at 1030. In contrast, the Code explicitly provides for payment from the estate to chapter 12 and 13 debtors' attorneys. 11 U.S.C. § 330(a)(4)(B); *Id.* at 540-41.

[5] *See* 11 U.S.C. § 526 (restrictions on debt relief agencies); *Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 236, 130 S. Ct. 1324, 1331 (2010) (attorneys may qualify as "debt relief agencies.").

[6] 11 U.S.C. § 362(a).

[7] 11 U.S.C. § 362(b).

[8] *Rittenhouse v. Eisen*, 404 F.3d 395, 397 (6th Cir. 2005); *Bethea v. Robert J. Adams & Assocs.*, 352 F.3d 1125, 1129 (7th Cir. 2003); *Hessinger and Assocs. v. U.S. Trustee (In re Biggar)*, 110 F.3d 685, 688 (9th Cir. 1997).

[9] *Gordon v. Hines (In re Hines)*, 147 F.3d 1185, 1191 (9th Cir. 1998).

[10] *Bethea*, 352 F.3d at 1128-29 (Noting that "the *Hines* majority wrote that it thought the Code as written . . . is unsatisfactory as a matter of public policy, and it decided to do a little surgery . . . *Hines* conceded that it was going against the Code's language" and holding that the *Hines* reasoning "is not enough to support that decision's holding.").

[11] *See* http://www.uscourts.gov/statistics-reports/caseload-statistics-data-tables. Fiscal years run from October 1 of the previous calendar year to September 30.

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attorney's fees rose by about 45 percent following enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.[12]

Types of Arrangements

Consumer debtors in financial distress sometimes find it difficult to pay the chapter 7 attorney's fee in a lump sum prior to filing the bankruptcy case. Under the traditional model, such debtors who wish to be represented must either delay filing until the fees are paid in full (which may be infeasible in light of pending foreclosure sales or garnishments), or their attorneys must file the case without having received payment in full and with no recourse to compel payment of the balance. Alternative payment arrangements fall into three general categories: outright or potentially fraudulent schemes, fee-only chapter 13 cases, and bifurcated fee agreements (including "factoring" arrangements). In addition to the USTP, all stakeholders in the bankruptcy system should be committed to addressing the first category and vigilant in avoiding potentially problematic issues with the others.

Courts have found that some lawyers have engaged in schemes to obtain payment of their fees in illegitimate ways and in violation of the Code and Rules. A high-profile example was discussed in a recent article in this Journal summarizing a case regarding a national law firm's conduct decided in the Western District of Virginia.[13] In this case, which the USTP brought and which is on appeal, the bankruptcy court imposed sanctions after finding that the law firm engaged in a practice of referring clients to a towing company, which paid the clients' bankruptcy attorney's fees in exchange for taking possession of and in some cases selling the clients' vehicles by priming the lenders' secured claims. Fortunately, these sorts of attorney's fee payment arrangements are not typical, but extreme misconduct presents substantial risks to both participating attorneys and other stakeholders. In the example described above, the court found that lenders holding valid liens may have been harmed by loss of their collateral or by payment of exorbitant fees to recover the collateral. Moreover, the court found that debtors could have been exposed to legal risk, including breach of contract and possible violation of state law. Fee arrangements that are based on potentially fraudulent conduct have and will continue to draw the USTP's scrutiny and, where appropriate, enforcement action.

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[12] Lois R. Lupica. *The Consumer Bankruptcy Fee Study: Final Report*. 20 AM. BANKR. L. REV. 17 (2012).

[13] Roy M. Terry, Jr. and Elizabeth L. Gunn. *UpRight: A Cautionary Tale of a National Consumer Law Firm*. ABI JOURNAL, July 2018, at 32.

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Another method of circumventing the Code's limitations on post-petition payment of chapter 7 attorney's fees which deserves further examination is the practice of placing debtors who are otherwise better served by chapter 7 in chapter 13 cases. In chapter 13, a significant portion of, or even all, attorney's fees can be paid over time under the debtor's plan.[14] This practice has a number of possible disadvantages. Fees in chapter 13, even for "no money down" chapter 13 cases, may be substantially higher than in chapter 7, meaning that these debtors pay more for the same relief they could more easily (and quickly) obtain in chapter 7.[15] Chapter 13 imposes greater obligations on debtors, including requirements to propose, obtain confirmation of, and fund a plan that under the Code must run for a minimum term of 36 months. And even if the goal is to convert the case to chapter 7 once the attorney's fees have been paid, the debtor may run the risk of having the case dismissed for bad faith without obtaining the ultimate benefit for which bankruptcy relief was sought: a discharge. Finally, filing chapter 13 cases in which the prospect for confirmation of, and successful compliance with, a plan is doubtful imposes additional burdens on bankruptcy courts and chapter 13 trustees.

Another recent article in the ABI Journal focused on the virtues of "bifurcation," the practice by which an attorney representing a consumer debtor in a chapter 7 bankruptcy case charges for their services under the color of two fee agreements.[16] This practice also merits scrutiny. Under the first "pre-petition" agreement, the debtor pays a nominal or no fee for work performed on the case prior to filing, such as consultation and the completion and filing of "skeletal" paperwork. After filing the skeletal case, the debtor and attorney enter into a second, "post-petition" agreement, which covers not just usual post-petition services (such as representation at the section 341 meeting and reaffirmations), but also preparation and filing of the schedules, statement of financial affairs, and other required documents. By structuring the fee agreement this way, the attorney purports to avoid creating an unperformed pre-petition contract that would be subject to the automatic stay and discharge.

Bifurcation – particularly in "$0 down" models – is prone to creating a fiction under which pre-petition services are severely undervalued so that the fees for those services can be shifted to the post-petition, non-stayed, non-dischargeable fee

[14] 11 U.S.C. § 330(a)(4)(B).

[15] Katherine M. Porter, Pamela Foohey, Robert M. Lawless, and Deborah Thorne, *'No Money Down' Bankruptcy*, 90 S. CAL. L. REV. 1055, 1077 (2017).

[16] Daniel E. Garrison, *Liberating Debtors from "Sweatbox" and Getting Attorneys Paid*, ABI JOURNAL, June 2018, at 16.

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agreement, or actually eliminating the critical analysis and consultation that a competent attorney should provide prior to the debtor's decision to file. With the possible exception of the Ninth Circuit (due to *Hines*), it is likely impermissible to evade discharge of unpaid fees for pre-petition work by characterizing them as post-petition fees; moreover, fees charged pursuant to a post-petition contract for pre-petition services are unreasonable under section 329(b) of the Code. Further, while proponents of bifurcation emphasize that the debtor's entry into the post-petition agreement is completely independent of the pre-petition agreement and that the debtor could choose to proceed *pro se* or with other counsel for post-petition services, this "choice" may be illusory. The debtor and attorney go into the bifurcated case with the mutual expectation that the attorney will continue representation post-petition, and proceeding either *pro se* or with substitute counsel is difficult and unlikely.

Bifurcation has further evolved into a new practice, "factoring." Under a typical factoring model, the debtor's attorney bifurcates fees as described above, often advertising "$0 down," meaning no fees under the pre-petition contract. Once the case has been filed, the attorney has the client execute the post-petition agreement along with an agreement authorizing a third-party finance company to make automatic periodic debits for the fees due under the post-petition contract. The attorney then assigns the right to collect from the debtor under the post-petition agreement to the third-party finance company in exchange for a lump sum discounted payment, perhaps 70% of the face value of the post-petition contract. Going forward, the finance company has the right to collect payments from the debtor and to take collection action, including to sue and garnish, should the debtor default.

The additional gloss of factoring raises further concerns. Aside from the concerns inherent in bifurcation, factoring may promote unjustifiable inflation of the attorney's fees to make up for the discounted lump sum the attorney will receive from the finance company. In essence, this may be an undisclosed interest or finance charge. In some cases, the client may not have given fully informed consent to the fee arrangement. Further, the factoring arrangement may not be fully disclosed in the attorney's fee disclosure (Form 2030) or in the schedules.[17] The USTP is currently litigating enforcement actions in several bankruptcy courts and will continue to investigate and take action as appropriate when debtor's attorneys

[17] At a minimum, ongoing payments to the finance company on account of the post-petition fees ought to be listed as an expense line item on the debtor's Schedule I/J.

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engage in this sort of conduct in a manner that violates the Bankruptcy Code and Rules.[18]

Is Access to Justice for Debtors or Their Lawyers?

USTP Director Cliff White recently stated that "too often, the phrase 'access to justice' is misused to excuse bad lawyering, or to justify twisting the Bankruptcy Rules for the financial gain of the lawyers."[19] "Access to justice" has become a common phrase in consumer bankruptcy commentary. It generally connotes concern for the ability of consumers in financial distress to access the bankruptcy system, and it is linked to suggested barriers to entry such as the availability of attorneys in rural areas and financial considerations, including the cost of hiring counsel and the terms under which they may be paid.

There may be legitimate concerns about the ability of "honest but unfortunate" consumer debtors to successfully file bankruptcy cases. All stakeholders in the bankruptcy system should be vigilant that the system is functioning as intended for the benefit of debtors and creditors. But too often, the USTP has seen "access to justice" used as a catchphrase to conceal and legitimize schemes designed to benefit professionals. And as described above, these schemes may come at the expense of the debtor and the true goal of the consumer bankruptcy system – the debtor's fresh start.

Two truths must be understood and followed in order to maintain a fair and effective consumer bankruptcy system. First, the economic concerns of consumer lawyers must never trump professional obligations. And second, "access to justice

[18] On September 4, 2018, the Bankruptcy Court for the Northern District of Oklahoma entered an opinion and judgment in favor of the United States Trustee against a consumer debtor attorney using a factoring business model. *In re Wright*, No. 17-11936-M (Bankr. N.D. Okla. Sept. 4, 2018). The court found serious deficiencies in the attorney's conduct, notably that the attorney charged a higher fee to clients using the factoring model than charged to his "conventional" clients. The attorney admitted that in several cases he designated fees for pre-petition services as post-petition, which the court described as "a fraud both on the debtor and the Court." And the court found that the attorney's fee disclosures were "grossly misleading and indicative of a wanton disregard—*to the point of negligence*—for the level of candor required under § 329." (emphasis in original). The court ordered the attorney to disgorge all fees, voided the "post-petition" agreements, and barred the attorney and the factoring company from collecting any additional fees, in 17 cases.

[19] Clifford J. White III, Director, United States Tr. Program, Remarks at the 53rd Annual Seminar of the National Association of Chapter 13 Trustees (June 28, 2018).

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should be about the client. Period."[20] As it has for years, the USTP will continue to investigate and take enforcement action to end harmful substandard practice and misconduct by consumer attorneys.

[20] *Id.*

First Day Motions

Perspective of

Office of the United States Trustee

What Is a "First Day" Hearing?

- Initial hearing in a chapter 11 case where Debtor seeks expedited relief to support continuing operations

- Limited notice to creditors and other parties in interest
  - in some cases, those parties are spread across the country/globe.

United States Trustee "First Day" Role

- Preserve the status quo -- minimum relief necessary to maintain business operations pending formation of the Official Committee of Unsecured Creditors
- Enforce the law and critique the record
- Debtors must demonstrate legal basis for, and present evidence supporting, the relief requested. UST will object where the case for relief is legally or factually deficient
- Debtor must preview "coming attractions" for the court

Before Filing

- Before filing the case, Debtor and other parties should be familiar with jurisdiction's local procedural rules regarding "first day" hearings and for obtaining expedited relief

Before the "First Day" Hearing

- Debtor should file "first day" affidavit or declaration which should include:
  - History (e.g., significant litigation, material transactions)
  - Capital structure
  - Reason(s) for filing
  - "Game plan"
  - Basis for relief

Before the "First Day" Hearing

(continued)

- UST will also request background information from the Debtor and other parties in interest

- During these discussions, the Debtor and other parties in interest should be prepared to advise UST on:
  - Any pre-petition allegations of fraud (e.g., class action lawsuits), related investigation(s) by a governmental unit (e.g., grand jury, SEC)
  - Status of defined benefit plans underfunding issues and Pension Benefit Guaranty Association interest in the case
  - Environmental concerns that may pose an imminent danger to public health or safety

Types of "First Day" Motions

- ❑ Procedural/Operations
- ❑ Pre-Petition Payments

Procedural/Operations

- ❑ Joint Administration
- ❑ Cash Management
- ❑ Customer Programs
- ❑ Utilities

Joint Administration

- Motion should state that Debtors are not seeking substantive consolidation
- Proposed form of caption should have information required by Rule 2002(n) for each Debtor
  - Debtor name
  - name formerly used within eight years prior to bankruptcy filings,
  - last four digits of taxpayer identification number
  - address

Joint Administration

(continued)

- Proposed order should not allow consolidated reporting, including
  - Monthly operating reports
  - Schedules
  - Statements of Financial Affairs
- Proposed order should not modify reporting obligations, including
  - Substantial interests in non-debtors under Rule 2015.3

Cash Management

- UST must receive notice of opening/closing of bank accounts (if debtor-in-possession accounts are not being opened)
- Debtors must print "Debtor in Possession" on self-printed checks and forms immediately
- Must comply with 11 U.S.C. § 345(b) or request temporary waiver (e.g., to 15-30 days) to give the Debtors sufficient time to comply with §345(b) obligations

Cash Management

(continued)

- All of the Debtors' bank accounts must be identified
- Banks' authority to process pre-petition checks should be limited to those items which the Bankruptcy Court has authorized the Debtors to pay
- Debtors must
  - (i) inform banks that are signatories to Uniform Depository Agreements ("UDAs") to "mark" their bank accounts as being held by a debtor in possession; and
  - (ii) assist the UST in getting the non-signatory banks to execute UDAs and to become Authorized Depositories

Cash Management

(continued)

- Debtors must provide information as to whether non-debtors participate in a cash management system
  - Are the Debtors funding operations of non-debtor affiliates?
  - If so, the Debtor must fully disclose this information and any relief should prohibit or limit distributions to non-debtor entities.
- Debtors must agree to trace transfers (including intercompany transfers) so that they may be readily ascertained

Cash Management

(continued)

Order should include:

14. The Debtors shall continue to maintain detailed records in the ordinary course reflecting transfers of cash, if any, including intercompany transfers, so as to permit all such transactions to be readily ascertained.

Customer Programs

- UST will generally not object to request to honor warranty claims if sufficient justification provided

- UST generally will not object to Debtors' request for authority to honor gift cards and other customer promotions if Debtors can demonstrate that they are needed for maintaining value of business

Utilities

- Utilities should not be enjoined from exercising their rights under 11 U.S.C. § 366(c)
- An allowed administrative expense claim is not a form of "security" under 11 U.S.C. § 366(c)(1)(B)
- Debtors cannot use pre-petition deposits provided to utilities as a "credit" against the obligation to tender adequate assurance of post-petition payment (11 U.S.C. § 366(c)(4))

Utilities

(continued)

(Example of an appropriate form of security)

ORDERED, that the Debtors shall, on or before twenty (20) days after the Petition Date, deposit a sum equal to fifty percent (50%) of the Debtors' estimated average monthly cost of Utility Services (~~less the amount of any Utility Services provided by Utility Providers holding prepetition deposits or other security for Utility Services~~) (the "Adequate Assurance Deposit") into an interest-bearing, newly-created, segregated account (the "Adequate Assurance Account"), pending further order of the Court, for the purpose of providing each Utility Provider adequate assurance of payment of its postpetition Utility Services to the Debtors.

Payment of Pre-Petition Claims

- Federal Rule of Bankruptcy Procedure 6003
  - No relief under 11 U.S.C. §§ 327 or 365 and/or use/sale/lease relief under 11 U.S.C. § 363, for 21 days after filing of petition, absent a showing of "immediate and irreparable harm"
- "Necessity of payment" doctrine, if recognized by the Bankruptcy Court, requires evidence that payment must be made to avoid immediate and irreparable harm

Payment of Pre-Petition Claims

(continued)

- Seventh Circuit's ruling in *In re Kmart Corp.*, 359 F. 3d. 866 (7th Cir. 2004), denied use of Section 105 and doctrine of necessity as authority for payment of pre-petition claims
- It is unclear if this prohibition extends to motions to pay employee wages (or other claims entitled to priority), which continue to be routinely approved by some Seventh Circuit courts notwithstanding *Kmart*

Payment of Pre-Petition Wages/Benefits

- Payment of wages and benefits should be subject to "caps" set forth in 11 U.S.C. § 507(a)(4, 5)
- The wage order should not authorize payment of pre-petition bonus or severance obligations and should not authorize such programs going forward
- Debtor(s) should not attempt to "cure" a professional's lack of disinterestedness by paying the pre-petition claim of professional by classifying them as an "independent contractor" or "temporary employee"

Payment of Pre-Petition Wages/Benefits

(continued)

Example of appropriate limitations

2. The Debtor is authorized, but not required, to honor and pay the Employee Obligations, subject to (and capped at) the statutory limitations set forth in 11 U.S.C. §§ 507(a)(4) and 507(a)(5); provided further, that payments on account of prepetition Employee Obligations shall not exceed $[INSERT AMOUNT].

Critical Vendors

- Who are the "critical" vendors?
  - Must provide the list
  - If you can't identify, they can't be critical
- Are they truly "critical"?
  - Sole source?
  - Is the Debtor party to a contract which calls for specific material?
  - Sufficient evidence to support Doctrine of Necessity?
- Limited relief (if any) pending formation of an official committee of unsecured creditors
- Debtors should not have a unilateral right to declare a "default" under a critical vendor order without challenge from the critical vendor

Shippers and Warehousemen Payments Sales & Use Taxes

- Will contracting party refuse to ship without payment of funds?
- Is the payment of sales and use taxes or other "trust fund" taxes necessary to preserve good standing status under state law?

Non-First Day Motions

UST will object to these motions being heard on "First Day"

- ❑ Retention Applications
  - potential exception – claims agent
- ❑ Motion to extend time to file schedules
- ❑ Ordinary Course Professional Motion
- ❑ Interim Compensation Procedures Motion
- ❑ Bid Procedures or Sale Motions
- ❑ KERP, KEIP or Other Bonus Motion
- ❑ Limitation on Equity Treaty Motion
- ❑ Motion to Assume or Reject Leases

USE OF CASH COLLATERAL AND DIP FINANCING

Office of the United States Trustee

Practical Realities

First Days After Filing

- When a business files a chapter 11 bankruptcy, it is generally authorized to continue to operate its business. 11 U.S.C. § 1108.
- Most chapter 11 Debtors have secured debts with liens attaching to cash, accounts receivable, inventory, etc.
- Thus, most Debtors cannot use operating income (assuming it is cash collateral) without consent of secured creditor or court order. 11 U.S.C. § 363(c)(2).
- Because lenders rarely consent without obtaining other relief, Debtors must come to court to gain access to cash for operations immediately after filing the case.

Debtors Obtain Cash Two Ways

- There are generally two means for a Debtor to get access to cash necessary to operate its business post-petition:
  - authorization to use cash collateral
  - Debtor-in-possession (DIP) financing (post-petition credit)
- Because of the almost immediate need for cash, most Debtors seek emergency or expedited consideration of cash collateral or DIP financing.

What is Cash Collateral?

- Section 363(a) defines "cash collateral" as follows:
  - cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents whenever acquired in which the estate and an entity other than the estate have an interest
  - includes the proceeds, products, offspring, rents, or profits of property
  - includes fees, charges, accounts or other payments for the use or occupancy of rooms and other public facilities in hotels, motels, or other lodging properties subject to a security interest as provided in section 552(b) of this title, whether existing before or after the commencement of a case under this title.

When is it Cash Collateral?

Post-Petition Effect of Pre-Petition Lien

- Property acquired post-petition is not subject to a security interest created by a pre-petition security agreement. 11 U.S.C. § 552(a)
- If the security documents provide that the security interest extends to proceeds, products, offspring or profits (as almost all do), then 11 U.S.C. § 552(b)(1) provides that the security interest applies to those proceeds, products, offspring or profits acquired post-petition, unless the court orders otherwise
- 11 U.S.C. § 552(b)(2) applies specifically to rents and use or occupancy fees and charges.

Authority to Use Cash Collateral

- The trustee or DIP cannot use cash collateral unless each entity with an interest in the cash collateral consents or the court authorizes the use, sale or lease of the property after notice and a hearing. Section 363(c)(1-2).

- Section 363(e) provides that the court shall prohibit or condition the use, sale or lease of cash collateral as necessary to provide adequate protection of the interest in cash collateral.

Adequate Protection

- Section 361 defines adequate protection. In summary, adequate protection can take 3 forms:
  - Cash or periodic cash payments
  - Additional or replacement liens
  - Other relief resulting in "indubitable equivalent" of entity's interest
- Burdens:
  - Debtor must prove lender is adequately protected
  - Pre-petition lender must prove validity, priority and extent of its interest in the cash collateral

Motion to Use Cash Collateral -
Rule 4001(b)

- Motion required and must include or attach:
  - Name of each entity with interest in cash collateral
  - Purposes of use
  - Material terms, including duration of use
  - Any adequate protection proposed to be provided to secured creditor(s), or an explanation why each is already adequately protected
  - Credit Agreement
  - Proposed Order
- Generally, a court will allow a single motion to seek both interim and final relief.

Hearings on Cash Collateral

- Court may conduct preliminary or interim hearing within 14 days after service of motion
  - Can only authorize relief necessary to avoid "immediate and irreparable harm" before final hearing
  - Examples of irreparable damage commonly approved for interim cash collateral use are employee wages, purchase of necessary supplies, and insurance
- Final hearing must be at least 14 days after service of motion

DIP Financing – Post-Petition Credit

- 11 U.S.C. § 364 governs post-petition credit
  - 364(a) allows credit in the ordinary course of business as admin expense, *e.g.*, the vendor/supplier with invoice terms of net 30
  - 364(b) administrative priority for post-petition lending (rarely used because most-post-petition lenders want the protections of 364(c) and (d))
  - 364(c) superpriority administrative claim, lien on unencumbered assets, junior lien on encumbered assets
  - 364(d) senior (priming) or equal lien on encumbered assets
- Section 364 also generally requires that DIP show that financing is not available using lower priority protections to lender.
- Some DIP lending will take out original prepetition lender, and some will be in addition to prepetition lending. DIP lender is sometimes the prepetition lender. This requires consideration of other issues addressed later (e.g., roll ups, cross collateralization).

Motion for DIP Financing

Rule 4001(c)

- Motion required and must include or attach:
  - Credit agreement
  - Proposed order
  - Summary of all material provisions of credit agreement and proposed order, including where the provision may be found, including:
    - interest rate
    - maturity
    - events of default
    - liens
    - borrowing limits
    - borrowing conditions
- Generally, a court will allow a single motion to provide for both interim and final relief

Motion for Dip Financing

Rule 4001(c) – cont'd

- Rule 4001(c) also identifies eleven types of relief that must be specifically identified in the motion if in the credit agreement or proposed order:
  - (i) a grant of priority or a lien on property of the estate under §364(c) or (d)
  - (ii) the providing of adequate protection or priority for a prepetition claim, including the granting of a lien on property of the estate to secure the claim, or the use of property of the estate or credit obtained under § 364 to make cash payments on account of the claim

Motion for Dip Financing

Rule 4001(c) – cont'd

- (iii) a determination of the validity, enforceability, priority, or amount of a claim that arose before the commencement of the case, or of any lien securing the claim
- (iv) a waiver or modification of Code provisions or applicable rules relating to the automatic stay
- (v) a waiver or modification of any entity's authority or right to file a plan, seek an extension of time in which the Debtor has the exclusive right to file a plan, request the use of cash collateral under § 363(c), or request authority to obtain credit under § 364
- (vi) the establishment of deadlines for filing a plan of reorganization, for approval of a disclosure statement, for a hearing on confirmation, or for entry of a confirmation order

Motion for Dip Financing

Rule 4001(c) – cont'd

- (vii) a waiver or modification of the applicability of nonbankruptcy law relating to the perfection of a lien on property of the estate, or on the foreclosure or other enforcement of the lien
- (viii) a release, waiver, or limitation on any claim or other cause of action belonging to the estate or the trustee, including any modification of the statute of limitations or other deadline to commence an action
- (ix) the indemnification of any entity
- (x) a release, waiver, or limitation of any right under § 506(c)
- (xi) the granting of a lien on any claim or cause of action arising under §§ 544, 545, 547, 548, 549, 553(b), 723(a), or 724(a)

Hearing on DIP Financing Rule 4001(c)

- Court may conduct preliminary or interim hearing within 14 days after service, but only authorize that which is necessary to avoid "immediate and irreparable harm" pending the final hearing
  - Examples of irreparable damage commonly approved for interim cash collateral use are employee wages, purchase of necessary supplies, and insurance.
- Final hearing must be at least 14 days after service of motion

Similar Issues in Cash Collateral and DIP Financing

- Issues and requirements for approval of use of cash collateral and for approval of DIP Financing often overlap.
- To obtain authority to use cash collateral, Debtors sometimes agree to onerous provisions because the secured creditor generally has significant leverage over the Debtors, who lack other viable financing alternatives.
- In these situations, the UST, a creditors' committee, and the court can be of great assistance to the Debtor.
- The Court can authorize cash collateral use and terms of adequate protection, but it cannot compel a lender to lend upon terms to which it does not agree.

Check Your Local Rules

- Many bankruptcy courts have local rules governing cash collateral and DIP financing. These rules may:
  - Require that Debtors disclose or highlight certain provisions so the court does not have to scour hundreds of pages to find important provisions
  - Require that Debtors identify provisions that the court does not generally permit except in unusual or exceptional circumstances, or provide that certain provisions are "unenforceable"
  - Require that Debtors identify provisions that the court normally allows
  - Impose additional or modified service requirements.

Hearing Day – UST's Role

- The UST, the creditors' committee, and the court often raise similar concerns.
- In the first days of case, the UST tries to preserve the status quo – and afford minimum relief pending formation of a creditors' committee.
- The UST reviews the record to determine whether there is a legal and evidentiary basis for the relief requested
  - Is there evidence of immediate and irreparable injury?
  - Are the proposed payments in the budget necessary?
  - Has the Debtor demonstrated that they tried to get credit under less onerous terms but could not?

Common Requests for Relief

- ❑ Granting priority or lien on property of estate pursuant to 11 U.S.C. § 364(c) or (d)
- ❑ Providing adequate protection or priority or use of property of the estate or credit obtained to make cash payments on account of claim
- ❑ Determination regarding validity, perfection, priority, or amount of a pre-petition claim, or of any lien securing such claim
- ❑ Waiver or modification of the automatic stay
- ❑ Waiver or modification of any entity's authority to file a plan, to seek an extension of time in which the Debtor has the exclusive right to file a plan, or the right to request the use of cash collateral or to request authority to obtain credit
- ❑ Waiver or modification of applicable nonbankruptcy law relating to the perfection of a lien on property of the estate or on the foreclosure or other enforcement of the lien

Common Requests for Relief – Cont'd

- Release, waiver, or limitation on any claim or other cause of action belonging to the estate or the trustee, including any modification of the statute of limitations or other deadline to commence an action
- Indemnification of any entity
- Release, waiver, or limitation of any right to surcharge collateral under section 506(c)
- Granting a lien on any claim or cause of action (usually avoidance actions)
- Provisions for "carve-outs" for professionals' fees and expenses

Potentially Objectionable Terms

- Cross-collateralization clauses - clauses that secure prepetition debt with postpetition assets in which the secured party would not otherwise have a security interest based on its prepetition security agreement or applicable law
  - e.g., pre-petition agreement provides for lien only on accounts receivable, while post-petition lien proposed on accounts receivable, inventory and real estate
- "Roll-ups" - provisions deeming pre-petition debt to be post-petition debt or using post-petition loans from a pre-petition secured creditor to pay part or all of that secured creditor's pre-petition debt
  - other than as provided in 11 U.S.C. § 552(b), which deals with security interests in proceeds and profits
- Provisions or findings of fact that bind estate or parties in interest, including committees or subsequently appointed trustees on validity, perfection or amount of the pre-petition lien or debt

Potentially Objectionable Terms- Cont'd

- ❑ Provisions or findings of fact that bind estate or parties in interest with respect to the relative priorities of the secured party's lien and liens held by persons who are not party to the stipulation
  - For example, an order approving a stipulation providing that the secured party's lien is a "first priority" lien without reference to prior permitted liens
- ❑ Waivers of, or grants of liens on, rights under 11 U.S.C. § 506(c),unless waiver or grant is effective only during period in which Debtor is authorized to use cash collateral or borrow funds.
  - could otherwise bind future trustee to preserve and care for collateral with no means to fund that duty
- ❑ Provisions that divest Debtor or trustee of discretion in formulating plan or administering estate or that limit their ability to seek relief from the court they would otherwise be entitled to seek
- ❑ Releases of, or limitations on, liability for the creditor's alleged prepetition conduct, e.g., torts or breaches of contract

Potentially Objectionable Terms- Cont'd

- Waivers of, or liens on, any of estate's rights arising under avoidance actions (11 U.S.C. §§ 544 et seq.) as well as 11 U.S.C. §§ 723(a) and 724(a) or the proceeds of any such rights
- Automatic relief from the automatic stay upon default, conversion to Chapter 7, or appointment of a trustee
- Waivers and modifications of the procedural requirements for foreclosure mandated under applicable non-bankruptcy law
- Waivers or limitations, effective on default or expiration, of right to move for authorization to use cash collateral in the absence of the secured party's consent
- Findings of fact on matters extraneous to the approval process

Potentially Objectionable Terms- Cont'd

- Provisions providing unreasonable treatment with respect to fees or professionals retained by a creditors' committee compared to any carve-outs provided for professionals retained by the Debtor in possession or trustee
- Provisions that provide an inadequate carve-out for a subsequently appointed trustee in the case, whether before or after conversion.
- Provisions that place venue in a jurisdiction other than bankruptcy court in event of a dispute
- Provisions that require Debtor to pay secured creditor's expenses or attorneys' fees without notice or review by UST, creditors' committee, if any, or court
- Provisions that seek to limit the court's supervisory powers, such as by declaring a default in the event that a trustee or examiner is appointed

Department of Justice

STATEMENT OF

CLIFFORD J. WHITE III
DIRECTOR
EXECUTIVE OFFICE FOR UNITED STATES TRUSTEES
U.S. DEPARTMENT OF JUSTICE

BEFORE THE

SUBCOMMITTEE ON REGULATORY REFORM,
COMMERCIAL AND ANTITRUST LAW
COMMITTEE ON THE JUDICIARY
U.S. HOUSE OF REPRESENTATIVES

FOR A HEARING CONCERNING

H.R. 3553,
THE "BANKRUPTCY ADMINISTRATION
IMPROVEMENT ACT OF 2017"

PRESENTED

SEPTEMBER 26, 2018

Statement of Director Clifford J. White III
Executive Office for United States Trustees
U.S. Department of Justice
Before the Subcommittee on Regulatory Reform,
Commercial and Antitrust Law
Committee on the Judiciary
U.S. House of Representatives
September 26, 2018

Mr. Chairman, Ranking Member, and Members of the Subcommittee:

I appreciate the opportunity to appear before you today to discuss chapter 7 trustee compensation, including the proposal contained in H.R. 3553, the "Bankruptcy Administration Improvement Act of 2017." The United States Trustee Program (USTP or Program) appoints and oversees approximately 1,100 chapter 7 trustees who serve as fiduciaries for bankruptcy estates in liquidation. These trustees handle the day-to-day activities of approximately 600,000 chapter 7 cases and distribute on average about $3 billion annually from the assets of estates.

As the "watchdog" of the bankruptcy system, the USTP can attest to the crucial role of chapter 7 trustees in ensuring that bankruptcy estates are administered fairly and efficiently. They are on the frontline and, in most cases, are the only representative of the bankruptcy system with whom debtors and creditors have contact. It is a direct result of the chapter 7 trustees' efforts that debtors are provided the "fresh start" they seek and creditors receive repayment to which they are entitled by law.

Over the past many years, the Congress has given chapter 7 trustees additional statutory responsibilities. Yet trustee compensation has not kept pace with these added duties or with inflation. Although there has been consensus on the need to provide trustees with additional compensation, there has not been consensus on the appropriate source(s) of that funding. We urge the Congress to break the logjam to ensure that the bankruptcy system can continue to benefit from a skilled and competent corps of chapter 7 trustees.

Chapter 7 Trustee Duties

The chapter 7 trustee serves as the representative of the bankruptcy estate and is a fiduciary charged with protecting the interests of all estate beneficiaries. Section 704 of the Bankruptcy Code enumerates 12 overarching duties of a chapter 7 trustee. Chief among those are to investigate the financial affairs of the debtor, collect and reduce to money property of the estate as expeditiously as is compatible with the best interests of parties in interest, and provide a full and complete accounting of the administration of a case. The list also includes changes made by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), including new responsibilities relating to domestic support obligations, health care bankruptcies, and the administration of employee benefit plans.

Notably, chapter 7 trustees also support the USTP in both its civil and criminal enforcement responsibilities. On the civil side, this includes referring cases to the United States Trustees that may warrant enforcement action, such as cases in which a debtor causes unreasonable delay, conceals or destroys property, or otherwise fails to comply with bankruptcy requirements. On the criminal side, trustees refer suspected bankruptcy or bankruptcy-related fraud to the USTP, and offer important assistance to the Program and law enforcement, including reporting on their review of the debtor's financial information and testifying at trial.

One recent example of the USTP partnership with private trustees in ferreting out fraud involves a case in the Southern District of New York. The chapter 7 trustee successfully pursued a now former bankruptcy lawyer who embezzled funds from a chapter 11 estate. After the USTP's Manhattan office investigated the lawyer for a lack of proper accounting of sales proceeds, it obtained a court order converting the case to chapter 7 and appointed the trustee. In coordination with the USTP, the chapter 7 trustee immediately commenced discovery and obtained court orders holding the attorney in contempt and issuing a bench warrant for his failure to turn over documents and funds paid without court approval. Meanwhile, the USTP continued to investigate the conduct of the attorney in the converted case, as well as his representation of clients in other bankruptcy cases. The investigation revealed many financial irregularities, such that the USTP referred the lawyer's conduct to its federal and state law enforcement partners. In March 2018, the lawyer pled guilty in federal district court to one count of embezzlement from a bankruptcy estate and, in May 2018, pled guilty to two state charges relating to his embezzlement of funds from his attorney escrow account. Sentencing is scheduled for October in both the federal and state criminal proceedings.

Though more than 90 percent of chapter 7 cases are no-asset cases – meaning that the debtor does not own any non-exempt assets that can be liquidated for the benefit of creditors – trustees must still devote significant time to review the financial information filed in the case, question the debtor under oath about assets and liabilities, and perform other statutory duties. Trustees must undertake these responsibilities even in no-asset cases in which the debtor qualifies for a waiver of the filing fee, and the trustee receives no fee. In fact, it is often only by performing these time-consuming activities that trustees can identify additional assets to bring into the estate for the benefit of creditors, as well as verify the debtor's and other parties' compliance with bankruptcy law.

Chapter 7 Trustee Compensation History

For carrying out these important case administration responsibilities, chapter 7 trustees receive compensation from two sources. First, trustees are paid $60 per case from the fees paid by the debtor upon the filing of a bankruptcy petition. This is sometimes referred to as the "no-asset" fee. In addition, in those cases in which assets are available for distribution to creditors, pursuant to section 326 of the Bankruptcy Code, chapter 7 trustees also receive a percentage of those distributions based on a sliding scale. This "percentage fee" also is referred to as the "trustee commission." Currently, the percentage fee ranges from 25 percent on the first $5,000 of distributions to three percent on amounts above $1 million.

The amount of the no-asset fee has not been adjusted over the past 24 years. Accordingly, if Congress was correct in its assessment in 1994 that the no-asset fee should be set

at $60, then that amount should be $100 today to account for inflation alone, and probably higher if the increased demands on trustees resulting from BAPCPA are considered.

Beyond the fixed no-asset fee that has lagged far behind inflation, the statutory formula for calculating the percentage fee on distributions in asset cases also has not changed since 1994. But in the 2005 BAPCPA amendments, Congress added a provision to ensure that courts would award these fees "as a commission." The USTP adopted the legal position that a trustee was entitled to the maximum percentage fee absent "extraordinary circumstances," such as substandard performance, a wholly disproportionate discrepancy between the trustee's effort in achieving the distribution as compared with the fee calculation under the statutory formula, or other factors that apply only in rare instances.

The USTP's position on the percentage fee has been adopted by the United States Courts of Appeals for the Fourth and Fifth Circuits. But some courts still employ methodologies that yield lower compensation, perhaps appreciably so in some cases. We respectfully disagree with those courts and believe that those courts are unnecessarily depressing trustee compensation and failing to give full meaning to the text of the statute.

In contrast to the lack of a compensation increase for chapter 7 trustees, one academic study showed that, in the years immediately after BAPCPA, debtor attorneys' fees rose by about 45 percent. Lois R. Lupica, *The Consumer Bankruptcy Fee Study: Final Report*, 20 Am. Bankr. L. Rev. 17 (2012). Although attorneys' fees vary significantly among local markets, customary fees nationally exceed $1,000 and may be significantly higher. In most jurisdictions, chapter 7 trustees may employ themselves as an attorney paid by the estate for performing non-trustee legal work in a case, such as litigation. Even when court-approved attorneys' fees paid to the trustee are added to the no-asset fee and trustee commissions, total compensation paid to chapter 7 trustees has decreased in six of the last ten fiscal years. In most of those years, the increases and decreases were modest; but, in FY 2017, trustee compensation plummeted by 18 percent.

The compensation decreases may help explain two other statistical changes that have occurred in the chapter 7 system. First, the number of chapter 7 trustees has decreased by about 20 percent over the past decade. The decrease in the number of trustees is due, in large part, to prudent decisions by United States Trustees not to fill vacancies due to lower filing rates. Nevertheless, limited recruitment data show that the number of applicants for chapter 7 trustee vacancies has decreased significantly, from an average of 58 candidates in 2010 to 20 candidates last year.

Although it is difficult to measure the precise impact of diminished compensation, it stands to reason that continual decreases in compensation may threaten the financial viability of some trustee operations and impede the recruitment of the best qualified candidates. These possible adverse impacts are of particular concern in light of recent filing trends that suggest that previous reductions in filing levels have stabilized and filings may start to increase. It is critical to the bankruptcy system that we are able to retain and recruit the highest caliber of trustees to serve as estate fiduciaries.

Funding an Increase in Chapter 7 Trustee Compensation

Under H.R. 3553, the fee for filing a chapter 7 case would increase by $60 to fully fund a proposed increase in the no-asset fee to $120 per case. In addition, the Bill would index the no-asset fee and make a technical clarification to 11 U.S.C. § 330(a)(7) governing the chapter 7 trustee percentage fee. The annual aggregate cost of increasing the no-asset fee to $120 would be about $27 million based on current filing rates.

Raising the chapter 7 filing fee to increase the no-asset fee paid to trustees is reasonable because more than 90 percent of chapter 7 cases are no-asset cases that require the expenditure of substantial trustee time and resources. The impact of such an increase, however, would be borne by debtors who may already be in dire financial straits.

Other options also have been identified in the past. For instance, the formula in section 326 for awarding trustees a percentage fee on distributions to creditors could be altered to allow for a higher percentage fee on larger estates. Those costs would be borne by creditors. Such an increase may not be the entire solution, however, because the benefits and costs would not be borne evenly across all cases or jurisdictions. That is because state laws generally determine the value of assets that debtors may exempt from bankruptcy estates, and those laws vary greatly. Therefore, not all trustees would benefit similarly from the statutory change because trustees in states with more debtor-friendly exemption laws typically administer fewer asset cases. Congress could, however, designate any increase in the percentage fee to fund the no-asset fee increase.

In addition, a variety of other fees that are imposed by the courts on litigants (*e.g.*, fees for filing motions in a case) could be raised and allocated to chapter 7 trustees. These fees are paid by stakeholders who are the most fully engaged in bankruptcy cases through litigation or otherwise.

The source of additional trustee compensation may well involve a combination of the above and other possible sources.

Conclusion

Chapter 7 trustees do an outstanding job administering bankruptcy cases fairly and efficiently. Much of the work they perform is in no-asset cases in which the fee, even with a reasonable increase, is below the cost of providing the service. Accordingly, chapter 7 trustees deserve an increase in compensation levels that have not changed over the past 24 years.

I appreciate the Subcommittee's attention and would be happy to answer any questions.

Annual National Review

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Chapter 13 Case Review and Update on Chapter 13 Issues

SUMMARY NUMBER:
§1327(b)
GRV

KEY CODE SECTION(S): §1306(a),

KEY TOPIC(S): Property of the Estate

COURT and JUDGE: USBC DNM Judge Thuma

CASE NAME and CITE: *In re Gonzales*, 578 B.R. 363 (Bankr. NM 2018)

CASE NUMBER: 13-17-12712 TL

DATE DECIDED: July 16, 2018

NOTEWORTHY ISSUE: Whether a taxing authority creditor of debtor's counsel can levy the Chapter 13 Trustee to collect funds owed by the Chapter 13 Trustee to debtor's counsel.

HOLDING: Yes.

FACTS: Chapter 13 case is confirmed. Debtor's counsel ("Counsel") files a fee application. An order awarding Counsel fees is entered. Counsel owes monies to NMTR. NMTR serves a tax levy on the Chapter 13 Trustee ("Trustee") to collect mones owed to Counsel under the attorneys fee order. Trustee requests direction form the court about how to respond to the tax levy.

The court finds that the Trustee (as the duly appointed Chapter 13 trustee in the case, not individually) is indebted to Counsel as a result of the court order allowing his fees. The court finds that the tax levy served by NMTR on the Chapter 13 Trustee, although somewhat ambiguous and unclear, includes debts owed by the Trustee to Counsel.

The significant issue that required resolution was whether the funds paid by the debtor to the Trustee pursuant to the plan, and held by the Trustee, were property of the estate subject to the automatic stay under §362. §1327(a) provides that, unless otherwise provided for in the plan or order confirming the plan, confirmation of the plan vests all property of the estate in the debtor. §1306(a) implies that a bankruptcy estate will exist until the case is closed, dismissed, or converted, and will be augmented by after-acquired property and post-petition wages. So the issue is whether payments made be the debtor to the Trustee pursuant to a Chapter 13 Plan are property of the bankruptcy estate. After considering the approaches of various other courts, the court found that upon confirmation of the chapter 13 plan, pre-confirmation payments made by the debtor pursuant to the chapter 13 plan are transferred to the debtor, free and clear of the claims and interests of creditors provided for in the plan, thus losing their status as property of the estate. Post-confirmation payments made by the debtor constitute property of the estate until the case is closed, dismissed or converted.

As a result, the monies paid to the Trustee by the debtor' prior to confirmation pursuant to the terms of the Plan were "transferred" to the debtors' upon confirmation of the Plan, were not property of the estate and were subject to the tax levy. Post-confirmation payments made by the debtors constituted property of the estate and were not subject to the tax levy.

SUMMARY NUMBER:
and (a)(4)(A)
GRV

KEY CODE SECTION(S): 727(a)(2)(A)

KEY TOPIC(S): Discharge

COURT and JUDGE: USBC DNM Judge Thuma

CASE NAME and CITE: In re Jayme; Monge vs. Jayme, 2018 WL 3218104

CASE NUMBER: 15-10504 TL; Adversary No. 15-1079 T

DATE DECIDED: June 29, 2018

NOTEWORTHY ISSUE: Whether the debtors should be denied a discharge under 11 U.S.C. §727(a)(2)(A) and/or (a)(4)(A).

HOLDING: Yes, debtors made false oaths in their bankruptcy petition, schedules and SOFA and gave false trial testimony about material facts and with fraudulent intent.

FACTS: Debtors had filed numerous prior bankruptcys either individually or as husband and wife. In this Chapter 7, a creditor of the debtors filed an adversary proceeding maintaining that debtors should not receive a discharge under §727(a)(2(A) and/or (a)(4)(A). The court entered an order denying the debtors' discharge, finding:

1. Debtors petitions, bankruptcy schedules and SOFA's filed in their prior bankruptcy cases could not be reconciled with their duty of accurate and full disclosure.

2. Debtors, with fraudulent intent, omitted several names they had used in the past from their petition.

3. Debtors failed to disclose prior bankruptcys and the omission was intentional and with fraudulent intent.

4. Debtors failed to disclose certain assets they owned and the failure to disclose was done either intentionally or with reckless indifference to the truth.

5. Debtors gave false trial testimony with fraudulent intent and was sufficiently material to constitute a false oath.

In summary, the court stated as follows: the Court is left with the firm conviction that Defendants care little for the truth unless the truth coincides with their perceived economic interests. When the two coincide, Defendants will tell the truth. Otherwise, Defendants have no problem omitting, twisting, shading, and misrepresenting the truth.

SUMMARY NUMBER: TMC

KEY CODE SECTION(S): § 348 & § 1326(a)(2)
KEY TOPIC(S): Attorney's Fees at Conversion

COURT and JUDGE: USBC DNM Judge Jacobvitz

CASE NAME and CITE: In re Walton

CASE NUMBER: 18-10735 JA

DATE DECIDED: January 28, 2019

NOTEWORTHY ISSUE: Whether debtor's counsel may be paid from the balance on hand held by the chapter 13 trustee when the case has been converted to a chapter 7.

HOLDING: Yes, with Court approval of the fees and a "knowing" and "voluntary" Assignment.

FACTS: Prior to confirmation, Debtor voluntary converted her chapter 13 bankruptcy case to chapter 7. Debtor was represented by counsel. Debtor's Counsel filed a fee application prior to filing the Notice of Conversion. In her application, Counsel not only sought an award of her fees, but also sought authorization for the Chapter 13 Trustee to pay her fee from the balance on hand. Attached to the fee application was an Assigment, which was notarized, and was executed post-petition. By the Assignment, Debtor assigned her interest in undisbursed funds held by the Chapter 13 Trustee, to be paid to Counsel for unpaid fees in the event of conversion or dismissal.

The Assignment contained 4 major components:

1. An explanation of what the Assignment was intended to do;
2. A statement that acknowledges that if not paid, the outstanding fees would otherwise be discharged in the chapter 7;
3. A statement that the Assignment is "knowing" and "voluntary"; and
4. A statement that acknowledges debtor's awareness to obtain advice of other counsel.

The Chapter 13 Trustee objected to the fee application solely on the grounds that she did not want to be the responsible party in determining whether the Assignment and process by which Counsel sought payment of her fees, given SCOTUS's opinion in *Harris v. Viegelahn*, 135 S. Ct. 1829 (2015).

DISCUSSION: Conversion of a bankruptcy case is governed by § 348. When a case is converted from chapter 13 to chapter 7, the funds on hand (consisting of post-petition earnings) are not property of the chapter 7 estate, unless bad faith is established. This same section, subsection (e) terminates the service of the chapter 13 trustee. It should be noted that the Supreme Court stated that the service of the chapter 13 trustee is *immediately* terminated upon the filing of the Notice of Conversion – there need not be an Order entered, a chapter 7 trustee assigned, no hearing is required – the termination is immediate.

A claim for attorney's fees would still have a priority status in the chapter 7, but as most chapter 7 cases are "no asset" cases, they ultimately would be discharged. *See* § 348(d). Additionally, any priority claim for fees in the chapter 7 is subordinate to chapter 7 administrative expenses.

Prior to *Harris*, if a case was converted pre-confirmation the chapter 13 trustee would disburse attorney's fees upon court approval under § 1326(a)(2), which states that if a plan is not confirmed, the trustee shall disburse any such payments paid, but not yet due and owing to creditors, to the debtor, but only after deducting any unpaid claim allowed under § 503(b). However, since SCOTUS's opinion, the chapter 13 trustee is no longer permitted to make that disbursement, as her "services" have been terminated, and thus, she has been stripped of her authority to do so.

Thus, to be paid attorney's fees from funds on hand held by the chapter 13 trustee, the Court must approve the award of attorney's fees and the Assignment must be "knowing" and "voluntary".

"Knowing" means that Counsel must inform debtor, in writing, that he/she could keep the funds held by the chapter 13 trustee and would never be obligated to pay those fees.

"Voluntary" means that the Assignment should be executed pre-petition, so that debtor has sufficient time to seek other Counsel/advise should he/she not wish to sign the Assignment. However, it can be ratified if filed post-petition and/or post-conversion (although not all courts may agree with this).

SUMMARY NUMBER:
GRV
Objection

KEY CODE SECTION(S): §553
KEY TOPIC(S): Claims

COURT and JUDGE: USBC DNM Judge Thuma

CASE NAME and CITE: In re Williams, 2018 WL 3559098

CASE NUMBER: 17-13118 TA

DATE DECIDED: July 23, 2018

NOTEWORTHY ISSUE: Whether ex-husband creditor was entitled to set off or recoup his alimony obligations to debtor ex-wife with her property settlement obligation to him.

HOLDING: Yes.

FACTS: As part of divorce proceeding, debtor and husband enter into a marital settlement agreement (the "MSA") that required husband to pay alimony to wife in the amount of $322/month for 10 years. The MSA required wife to pay certain credit card and other debt incurred by the parties during the marriage.

Debtor files for relief under chapter 13. Husband files a proof of claim in the amount of $18,000, contending that was the amount he was owed by debtor under the Marital Settlement Agreement. In this proof of claim, husband asserts that the claim was secured by a right of setoff. Husband's claim is based on having to pay a debt that debtor had agreed to pay in the MSA. Debtor files an objection to husband's claim asserting that husband's claim was unsecured and not subject to setoff or recoupment.

Court finds that claim of husband is secured by a right of setoff or recoupment.

Setoff is proper if the offsetting obligations arose pre-petition and are "mutual." The court found that both obligations were pre-petition: (1) pursuant to the MSA, husband owed debtor alimony in the amount of $36,640 – so this constituted a debt owing by a creditor to the debtor that arose before the commencement of the bankruptcy case (even if payment of the obligation was to be made over a period of time post-petition); and (2) debtor was indebted to husband under the terms of the MSA – debtor's agreement to pay the obligations she assumed in the MSA. The debts are "mutual" since they were both created under the terms of the MSA.

Recoupment is an equitable doctrine that, in bankruptcy, permits a creditor to withhold funds owed to the debtor if the debtor owes money to the creditor arising from the same transaction. If the offsetting obligations are found in a single contract, courts usually find that the "same transaction" requirement has been met. In bankruptcy, recoupment should be allowed if the claims are so closely intertwined that allowing the debtor to escape its obligations would be inequitable. In this case, both obligations related to the MSA, a single contract. The equities

in the case favor recoupment. It would not be fair to require husband to pay the alimony obligation while not requiring debtor to pay her obligation to husband.

Ethics and Professionalism

A Fireside Chat on Ethics in Bankruptcy

With William Slease, Chief Disciplinary Counsel for the State Bar of NM

Facilitated by: Leslie D. Maxwell, Maxwell Law, P.C.

- Conflicts of Interest:
  - May I represent two clients who are not adverse now but may become so? How likely does the possibility need to be?
  - Can you represent two creditors of the same class? Different classes?
  - Creditor and a committee?
  - The DIP and the Debtor?
  - How "disinterested" are you? Is it okay that my personal mortgage is with the same bank that I'm stripping a lien for my client?

- Attorney's Duty
  - Pigs get fat, hogs get slaughtered. How much exemption planning is okay?
  - Reaffirmation agreements require your signature, what if you don't give it?
  - How far do I have to dig into a debtor's finances to have done proper due diligence?
  - Heart surgeons do heart surgery. Bankruptcy lawyers file bankruptcies. Is it okay to advise a BK when other options might be better?

- Advertising
  - How much communication with potential clients is too much?
  - What statements cross the line?
  - How far can I mine public records for clients?

- Civil Disobedience
  - If Rosa Parks had been a lawyer, would sitting in the front of the bus disbarred her?
  - When do my political or religious beliefs impede my fitness to serve? Do they?

- Confidentiality
  - When do my political or religious beliefs impede my fitness to serve? Do they?
  - What do I do when my client has illegal income or expenses? What if you know they claim assets that were actually stolen etc.?

- Attorney Client Relationship
  - What to do when firing a client.
  - A prospective client is dissatisfied with his current representation. Can you talk to him? How do you get paid after the case has already been filed?
  - What do I do when my client has illegal income or expenses? What if you know they claim assets that were actually stolen etc.?

SELECTED RULES

- RULE 16-103 DILIGENCE:
  - A lawyer shall act with reasonable diligence and promptness in representing a client.

- RULE 16-106 CONFIDENTIALITY OF INFORMATION:
  - A. Disclosure of information generally. A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted by Paragraph B of this rule.
  - B. Disclosure of information; specific circumstances. A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary:
    - (1) to prevent reasonably certain death or substantial bodily harm;
    - (2) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services;
    - (3) to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services;
    - (4) to secure legal advice about the lawyer's compliance with these rules;
    - (5) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved or to respond to allegations in any proceeding concerning the lawyer's representation of the client;
    - (6) to comply with other law or a court order; or
    - (7) to detect and resolve conflicts of interest arising from the lawyer's change of employment or from changes in the composition or ownership of a firm, but only if the revealed information would not compromise the attorney-client privilege or otherwise prejudice the client.
  - C. Inadvertent or unauthorized disclosure of information. A lawyer shall make reasonable efforts to prevent the inadvertent or unauthorized disclosure of, or unauthorized access to, information relating to the representation of a client.

- RULE 16-107 CONFLICT OF INTEREST; CURRENT CLIENTS:
  - A. Representation Involving Concurrent Conflict of Interest. Except as provided in Paragraph B of this rule, a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:
    - (1) the representation of one client will be directly adverse to another client; or
    - (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.
  - B. Permissible Representation When Concurrent Conflict Exists. Notwithstanding the existence of a concurrent conflict of interest under Paragraph A of this rule, a lawyer may represent a client if:

- (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;
- (2) the representation is not prohibited by law;
- (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and
- (4) each affected client gives informed consent, confirmed in writing.

- RULE 16-108 DECLINING OR TERMINATING REPRESENTATION:
  - A. Business transactions with or adverse to client. A lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:
    - (1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing in a manner that can be reasonably understood by the client;
    - (2) the client is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel on the transaction; and
    - (3) the client gives informed consent, in a writing signed by the client, to the essential terms of the transaction and the lawyer's role in the transaction, including whether the lawyer is representing the client in the transaction.
  - B. Use of information limited. A lawyer shall not use information relating to representation of a client to the disadvantage of the client unless the client gives informed consent, except as permitted or required by these rules.
  - C. Client gifts. A lawyer shall not solicit any substantial gift from a client, including a testamentary gift, or prepare on behalf of a client an instrument giving the lawyer or a person related to the lawyer any substantial gift unless the lawyer or other recipient of the gift is related to the client. For purposes of this paragraph, related persons include a spouse, child, grandchild, parent, grandparent or other relative or individual with whom the lawyer or the client maintains a close, familial relationship.
  - D. Literary or media rights. Prior to the conclusion of representation of a client, a lawyer shall not make or negotiate an agreement giving the lawyer literary or media rights to a portrayal or account based in substantial part on information relating to the representation.
  - E. Financial assistance. A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:
    - (1) a lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter; and
    - (2) a lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client.
  - F. Compensation from third party. A lawyer shall not accept compensation for representing a client from one other than the client unless:
    - (1) the client gives informed consent;
    - (2) there is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and
    - (3) information relating to representation of a client is protected as required by Rule 16-106 NMRA of the Rules of Professional Conduct.
  - G. Representation of two or more clients. A lawyer who represents two or more clients shall not participate in making an aggregate settlement of the claims of or against the

clients, or in a criminal case an aggregated agreement as to guilty or nolo contendere pleas, unless each client gives informed consent, in a writing signed by the client. The lawyer's disclosure shall include the existence and nature of all the claims or pleas involved and of the participation of each person in the settlement.

- H. Prospective malpractice liability limitation. A lawyer shall not:
  - (1) make an agreement prospectively limiting the lawyer's liability to a client for malpractice unless the client is independently represented in making the agreement; or
  - (2) settle a claim or potential claim for such liability with an unrepresented client or former client unless that person is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel in connection therewith.
- I. Proprietary interest in cause of action. A lawyer shall not acquire a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client, except that the lawyer may:
  - (1) acquire a lien authorized by law to secure the lawyer's fee or expenses; and
  - (2) contract with a client for a reasonable contingent fee in a civil case.
- J. Client-lawyer sexual relationships. A lawyer shall not have sexual relations with a client unless a consensual sexual relationship existed between them when the client-lawyer relationship commenced.
- K. Lawyer association. While lawyers are associated in a firm, a prohibition in the foregoing Paragraphs A through I that applies to any one of them shall apply to all of them.

- RULE 16-116 DECLINING OR TERMINATING REPRESENTATION:
  - A. Mandatory Disqualification. Except as stated in Paragraph C, a lawyer shall not represent a client or, where representation has commenced, shall withdraw from the representation of a client if:
    - (1) the representation will result in violation of the Rules of Professional Conduct or other law;
    - (2) the lawyer's physical or mental condition materially impairs the lawyer's ability to represent the client; or
    - (3) the lawyer is discharged.
  - B. Permissive Withdrawal. Except as stated in Paragraph C, a lawyer may withdraw from representing a client if:
    - (1) withdrawal can be accomplished without material adverse effect on the interests of the client;
    - (2) the client persists in a course of action involving the lawyer's services that the lawyer reasonably believes is criminal or fraudulent;
    - (3) the client has used the lawyer's services to perpetrate a crime or fraud;
    - (4) the client insists upon taking action that the lawyer considers repugnant or with which the lawyer has a fundamental disagreement;
    - (5) the client fails substantially to fulfill an obligation to the lawyer regarding the lawyer's services and has been given reasonable warning that the lawyer will withdraw unless the obligation is fulfilled;
    - (6) the representation will result in an unreasonable financial burden on the lawyer or has been rendered unreasonably difficult by the client; or
    - (7) other good cause for withdrawal exists.

- C. Representation Required. A lawyer must comply with applicable law requiring notice to or permission of a tribunal when terminating a representation. When ordered to do so by a tribunal, a lawyer shall continue representation notwithstanding good cause for terminating the representation.
- D. Orderly Termination. Upon termination of representation, a lawyer shall take steps to the extent reasonably practicable to protect a client's interests, such as giving reasonable notice to the client, allowing time for employment of other counsel, surrendering papers and property to which the client is entitled and refunding any advance payment of fee or expense that has not been earned or incurred. The lawyer may retain papers relating to the client to the extent permitted by other law.

Real Life Professional & Ethical Dilemmas in Consumer Bankruptcies:

(a guide for case preparation and client interaction, what is appropriate under the model rules and accompanying advisory opinions)

Presented to the Southeastern Bankruptcy Law Institute
Atlanta, Georgia
March 21-23, 2013

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Introduction:

> "If you're betwixt and between, trust the one with red hair." O.R. Melling, *The Hunter's Moon*

On matters of ethics, bankruptcy lawyers often find themselves "betwixt and between" – betwixt the seemingly immutable principal of "attorney-client privilege" and the bedrock bankruptcy principle of "disclosure, disclosure, disclosure...." -- between the need to represent your client competently and the reality that your client has limited resources – and facing the reality that a bankruptcy judge – unlike a state or federal trial court judge – is not as likely to allow you to withdraw.

What follows are some common ethical dilemmas and a suggested approach – besides just trusting the one with the red hair!

ReSources:

Besides your state's rules, there are many excellent resources on ethics issues, including the ABA website and advisory opinions, state law advisory opinions, and the like. I also recommend Cornell's website: http://www.law.cornell.edu/ethics/aba/current/ABA_CODE.HTM#

Decision Matrix:

When faced with an ethics dilemma, I use the following decision matrix:

- Is there a Rule in my jurisdiction that expressly governs/applies? If so, STOP! (Follow the Rule!)
- If not, are there Comments to the Rule that expressly govern/apply? If so, STOP! (Follow the Comment!)
- If not, is there a Case interpreting the Rule or Comment? If so, STOP! (Follow the Case!)
- If not, are there Advisory Opinions in my jurisdiction? If so, STOP! (Follow the Advisory Opinion!)
- If there is nothing in my jurisdiction, is the Rule in my jurisdiction substantially similar to the Model Rules of Professional Conduct? If so, STOP! (Follow the Comments, Cases, or Advisory Opinions applying the Model Rules!)
- If not, ask yourself:
    - What would the Judge who I am in front of say? (If I would lose my credibility and integrity, then STOP!)
    - What would my Grandma say? (If my Grandma would be ashamed of me, then STOP!)
    - What would my law practice Mentor say? (maybe STOP!, depending on what you think the Judge or your Grandma would say)
    - Last resort: ask a bunch of other practitioners...

No obvious answer? Take the high road!
Still stymied? Ask the question out loud...
Also don't forget – legal "conflicts" – vs. practical/business/personal ones

CLIENT SCENARIOS:

 # 1: The High Maintenance/Unreasonable/Demanding/Threatening Debtor Client:

Client Zsa Zsa Givememore fires you during her chapter 13 and accuses you of being rude, not returning phone calls (she calls you every day, several times a day), not fighting for her rights, and not telling her that she had to make ongoing mortgage payments in order to keep her home. In fact, she insists that you told her that her mortgage payments on her $500,000 house were included in her $300 a month trustee payment, and had she known that she would have to make mortgage payments in addition to trustee payments, she never would have filed a chapter 13. You have ruined her life and she wants a copy of her file and is going to "The Bar" about you.

- Do you have to give her the original file or can you give her a copy?
- What information do you have to give her?

- Who pays for the copies?
- Do you have to return every phone call that a client makes?
- Can you disclose attorney-client information to the malpractice attorney that you are about to retain?
- Other issues.....

 # 2: Prospective Avoidance of Malpractice Risks? May I Contract My Way Out of It?

You have survived your first bar complaint and prevailed on your first malpractice claim. You do not ever want to repeat this experience, thus, you modify your attorney-client contract to limit your malpractice liability. Any client that wants you to represent them must sign this contract.

- Can you contractually limit malpractice liability?
- Other Issues....?

 # 3: You Have the Savior Complex:

John Jon is dissatisfied with his current chapter 13 attorney and wants to retain you to represent him in his chapter 13.

- Can you speak with him while he is still being represented by counsel?
- After speaking with the Debtor, you realize that his complaints against his attorney have some validity and you would like to represent him...
  A) How do you get paid in a chapter 7?
  B) How do you get paid in a chapter 13?
  C) Does it make a difference if the case has already been confirmed?

 # 4: Why Can't We All Just Get Along??? Divorce Issues

You represent Mr. and Mrs. Robinson in a chapter 13. Halfway through their 60-month plan, Mr. Jones notifies you that he is divorcing his wife because she had an affair with their 21-year-old pool boy. There is an employer deduction order in effect against his wages. He assures you that the divorce will be civil because of their children.

- Can you continue to represent both?
- If so, is there anything you should do?

 # 5: The More the Merrier – Multiple Client Conflicts

Billy Bob is a happy client. He is so happy that he has referred his mother, sister, grandmother, first cousin, girlfriend and boss to you. You would like to thank Billy Bob for his efforts.

- Can you send Billy Bob a $50 gift card to the Big Steer Steak House to thank him for his referrals?

- If not, can you send him the gift card for his birthday?
- What if Billy Bob is an attorney?
- Does representing Billy Bob's boss create a potential conflict of interest? What if his boss is the sole owner of the business?

 # 6: Real Estate Issues

Mr. Rogers is in your office for a bankruptcy consultation. He has about $50,000 in credit card debt, $5,000 in recent income tax debt, a modest car payment, and a large mortgage payment. He has sole custody of his children. Due to his children's cheerleading and baseball expenses, he has been struggling to make his mortgage payments. He understands that his children will have to reduce their extracurricular activities. He also knows that he cannot afford to make mortgage payments and needs a smaller house.

- Should you counsel him to stop making mortgage payments prior to filing his bankruptcy and start saving for moving expenses?
- What if Mr. Rogers has rental property he wants to surrender? Can he continue to accept rent and keep the rent?
- Mr. Rogers now wants to keep his residence – his friend told him that he could have that second "interest only" lien stripped. The online websites, Zillow and eppraisal, report low fair market value estimations. The tax assessment also is low. Mr. Rogers has his house appraised just to be sure and is surprised at how high his house appraises. According to the appraisal, he is not eligible for lien stripping.
    a. Do you have to disclose this appraisal?
    b. What if Mr. Rogers wants to file a chapter 7? Are you obligated to tell him that chapter 7 lien stripping is yet to be decided by the appeals courts?

 # 7: Means Test Run Arounds?

Mr. and Mrs. Exciting enjoy good incomes as teachers. Both live very frugally. They have a modest mortgage, two 15-year-old cars that they intend to drive until the wheels fall off, and lots of credit card debt and medical debt due to illnesses. Because of their frugal lifestyle, they currently do not qualify for a chapter 7.

- Should you counsel them to finance two cars to help them qualify for a chapter 7?
- What about counseling them to finance two reliable cars while they still have good credit as their current cars are 15 years old and they will have to pay high interest rates if something happens to their cars after they file bankruptcy?
- Can you counsel them to tithe or make monetary charitable contributions?
- What about contributing money to their elderly parents for their support?

 # 8: Starving Chapter 7 Trustees (Do We Feel Sorry?)

Mr. Ima Grinch has been a chapter 7 trustee for a number of years and has enjoyed comfortable living as such. Lately, however, the number of asset cases has dwindled and

the living has not been as comfortable and Mr. Grinch has had to administer cases with unexempt assets of less than $2,000. Unfortunately, after the fees related to this administration are paid, there is little left over for the unsecured creditors.

- Chapter 7 Trustee issues?
- Ethical issues for Debtors filing "fee only" Chapter 13s?

 # 9: No Good Deed Goes Unpunished

You represent Buy Here/Pay More Used Cars and it has just received notice that it was listed as a creditor in a chapter 13. After reviewing the plan, it becomes evident that Debtor's attorney is new to the bankruptcy world and this is probably his first plan. He has proposed to pay full contract interest of 28% on a car purchased more than 910 days ago.

- Are you obligated to tell him about *Till* interest?
- Flip it around – what about a creditor's attorney who knows his or her client's lien is not perfected and files a stay relief motion – what can you affirmatively represent?

Appendix

Decision matrix: applicable model rules

Rule 1.16 Declining or Terminating Representation

a) Except as stated in paragraph (c), a lawyer shall not represent a client or, where representation has commenced, shall withdraw from the representation of a client if: ...

(3) the lawyer is discharged.

...

(c) A lawyer must comply with applicable law requiring notice to or permission of a tribunal when terminating a representation. When ordered to do so by a tribunal, a lawyer shall continue representation notwithstanding good cause for terminating the representation.

d) Upon termination of representation, a lawyer shall take steps to the extent reasonably practicable to protect a client's interests, such as giving reasonable notice to the client, allowing time for employment of other counsel, surrendering papers and property to which the client is entitled and refunding any advance payment of fee or expense that has not been earned or incurred. The lawyer may retain papers relating to the client to the extent permitted by other law.

Comment:

[4] A client has a right to discharge a lawyer at any time, with or without cause, subject to liability for payment for the lawyer's services. Where future dispute about the withdrawal may be anticipated, it may be advisable to prepare a written statement reciting the circumstances.

...

Assisting the Client upon Withdrawal

[9] Even if the lawyer has been unfairly discharged by the client, a lawyer must take all reasonable steps to mitigate the consequences to the client. The lawyer may retain papers as security for a fee only to the extent permitted by law. See Rule 1.15.

Rule 1.15 Safekeeping Property

(a) A lawyer shall hold property of clients or third persons that is in a lawyer's possession in connection with a representation separate from the lawyer's own property. Funds shall be kept in a separate account maintained in the state where the lawyer's office is situated, or elsewhere with the consent of the client or third person. Other property shall be identified as such and appropriately safeguarded. Complete records of such account funds

and other property shall be kept by the lawyer and shall be preserved for a period of [five years] after termination of the representation.

(b) A lawyer may deposit the lawyer's own funds in a client trust account for the sole purpose of paying bank service charges on that account, but only in an amount necessary for that purpose.

(c) A lawyer shall deposit into a client trust account legal fees and expenses that have been paid in advance, to be withdrawn by the lawyer only as fees are earned or expenses incurred.

(d) Upon receiving funds or other property in which a client or third person has an interest, a lawyer shall promptly notify the client or third person. Except as stated in this rule or otherwise permitted by law or by agreement with the client, a lawyer shall promptly deliver to the client or third person any funds or other property that the client or third person is entitled to receive and, upon request by the client or third person, shall promptly render a full accounting regarding such property.

(e) When in the course of representation a lawyer is in possession of property in which two or more persons (one of whom may be the lawyer) claim interests, the property shall be kept separate by the lawyer until the dispute is resolved. The lawyer shall promptly distribute all portions of the property as to which the interests are not in dispute.

Rule 1.4: Communication

(a) A lawyer shall:

(1) promptly inform the client of any decision or circumstance with respect to which the client's informed consent, as defined in Rule 1.0(e), is required by these Rules;

(2) reasonably consult with the client about the means by which the client's objectives are to be accomplished;

(3) keep the client reasonably informed about the status of the matter;

(4) promptly comply with reasonable requests for information; and

(5) consult with the client about any relevant limitation on the lawyer's conduct when the lawyer knows that the client expects assistance not permitted by the Rules of Professional Conduct or other law.

(b) A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.

Comment:

[4] A lawyer's regular communication with clients will minimize the occasions on which a client will need to request information concerning the representation. When a client makes a reasonable request for information, however, paragraph (a)(4) requires prompt compliance with the request, or if a prompt response is not feasible, that the lawyer, or a member of the lawyer's staff, acknowledge receipt of the request and advise the client when a response may be expected. A lawyer should promptly respond to or acknowledge client communications.

(h) "Reasonable" or "reasonably" when used in relation to conduct by a lawyer denotes the conduct of a reasonably prudent and competent lawyer.

Rule 1.9 Duties to Former Clients

(a) A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing.

(b) A lawyer shall not knowingly represent a person in the same or a substantially related matter in which a firm with which the lawyer formerly was associated had previously represented a client.

(1) whose interests are materially adverse to that person; and

(2) about whom the lawyer has acquired information protected by Rules 1.6 and 1.9(c) that is material to the matter; unless the former client gives informed consent, confirmed in writing.

(c) A lawyer who has formerly represented a client in a matter or whose present or former firm has formerly represented a client in a matter shall not thereafter:

(1) use information relating to the representation to the disadvantage of the former client except as these Rules would permit or require with respect to a client, or when the information has become generally known; or

(2) reveal information relating to the representation except as these Rules would permit or require with respect to a client.

Rule 1.6: Confidentiality of Information

(a) A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted by paragraph (b).

(b) A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary:

(1) to prevent reasonably certain death or substantial bodily harm;

(2) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services;

(3) to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services;

(4) to secure legal advice about the lawyer's compliance with these Rules;

(5) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client;

(6) to comply with other law or a court order; or

(7) to detect and resolve conflicts of interest arising from the lawyer's change of employment or from changes in the composition or ownership of a firm, but only if the revealed information would not compromise the attorney-client privilege or otherwise prejudice the client.

Rule 1.8 Conflict of Interest: Current Clients: Specific Rules

(a) A lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:

(1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing in a manner that can be reasonably understood by the client;

(2) the client is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel on the transaction; and

(3) the client gives informed consent, in a writing signed by the client, to the essential terms of the transaction and the lawyer's role in the transaction, including whether the lawyer is representing the client in the transaction.

...

(h) A lawyer shall not:

(1) make an agreement prospectively limiting the lawyer's liability to a client for malpractice unless the client is independently represented in making the agreement; or

(2) settle a claim or potential claim for such liability with an unrepresented client or former client unless that person is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel in connection therewith.

Comment:

Limiting Liability and Settling Malpractice Claims

[14] Agreements prospectively limiting a lawyer's liability for malpractice are prohibited unless the client is independently represented in making the agreement because they are likely to undermine competent and diligent representation. Also, many clients are unable to evaluate the desirability of making such an agreement before a dispute has arisen, particularly if they are then represented by the lawyer seeking the agreement. This paragraph does not, however, prohibit a lawyer from entering into an agreement with the client to arbitrate legal malpractice claims, provided such agreements are enforceable and the client is fully informed of the scope and effect of the agreement. Nor does this paragraph limit the ability of lawyers to practice in the form of a limited-liability entity, where permitted by law, provided that each lawyer remains personally liable to the client for his or her own conduct and the firm complies with any conditions required by law, such as provisions requiring client notification or maintenance of adequate liability insurance. Nor does it prohibit an agreement in accordance with Rule 1.2 that defines the scope of the representation, although a definition of scope that makes the obligations of representation illusory will amount to an attempt to limit liability.

[15] Agreements settling a claim or a potential claim for malpractice are not prohibited by this Rule. Nevertheless, in view of the danger that a lawyer will take unfair advantage of an unrepresented client or former client, the lawyer must first advise such a person in writing of the appropriateness of independent representation in connection with such a settlement. In addition, the lawyer must give the client or former client a reasonable opportunity to find and consult independent counsel.