

## COLLECTING JUDGMENTS

Strategies for Success

March 31, 2016

### BANKRUPTCY AND CREDITOR REPRESENTATION

by

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Just because a debtor files for bankruptcy does not mean that the creditor is finished or that the underlying debt can be discharged. The creditor has several options in bankruptcy. However, the creditor must proceed promptly, with caution and diligence.

#### **A. What to Do When the Creditor Gets Notice of a Bankruptcy?**

The filing of a bankruptcy immediately operates as an automatic stay of all collection actions against a debtor and his or her property. 11 U.S.C. §362(a). Specifically, the automatic stay prohibits the following kinds of action:

(1) the commencement or continuation of any judicial or administrative proceeding (e.g., a lawsuit); (2) the enforcement of a judgment against the debtor or his property; (3) an act to gain possession of property of the debtor; (4) the creation, enforcement, or perfection of any lien against the debtor's property; (5) any attempt to create, enforce or perfect a lien to the extent such lien secures a claim that arose before the commencement of this action; (6) to collect, assess or recover a claim; (7) any setoff of any debt owing to the creditor; and (8) the commencement or continuation of a proceeding in the US. Tax Court.

If the debtor files for bankruptcy under Chapter 13, the automatic stay extends to any individual who is liable on a consumer debt with the debtor. 11 U.S.C. §1301.

Any action taken in violation of the automatic stay is void and without effect. *Franklin Sav. Ass'n v. Office of Thrift Supervision*, 31 F.3d 1020 (10<sup>th</sup> Cir. 1994). Importantly, the automatic stay does not stop a debtor's actions or claims against creditors or third parties. *Victor Foods, Inc. v. Crossroads Economic Development of St. Charles County, Inc.*, 977 F.2d 1224 (8<sup>th</sup> Cir. 1992);

*Martin-Trigona v. Champion Federal Sav. and Loan Ass'n*, 892 F.2d 575 (7<sup>th</sup> Cir. 1989). A debtor may continue to pursue claims and/or counterclaims against a creditor in a non-bankruptcy forum even while the creditor is prohibited from continuing its claims against the debtor.

Creditor's beware: violations of the automatic stay are sanctionable. *In re Skinner*, 917 F.2d 444 (10<sup>th</sup> Cir. 1990); *In re Aspen Limousine Svc., Inc.*, 198 B.R. 341 (D.Colo. 1996). Individual debtors have a cause of action for damages for violations of the automatic stay, including attorney's fees. 11 U.S.C. §362(k). Entities can seek sanctions for stay violations under 11 U.S.C. §105(a). *Standard Indus., Inc., v. Aquila, Inc. (In re C.W. Mining Co.)*, 625 F.3d 1240 (10<sup>th</sup> Cir. 2010).

### 1. Meeting of Creditors

Under 11 U.S.C. §341, the United States Trustee must hold a meeting of creditors after the filing of the bankruptcy case. When the creditor receives the bankruptcy notice from the Court, the date for such meeting is on the notice. All debtors must appear and be examined under oath at the meeting of creditors as to their financial affairs. *Id.* The Court may not attend the meeting. *Id.*

Typically, the meeting affords creditors a "free" examination of the debtor similar to examinations under C.R.C.P. 69. Any matter relevant to a debtor's financial affairs, including the pre-petition transfer of assets can be inquired at the meeting. Counsel is not required to appear for the creditor at these meetings; the creditor may appear *pro se*, even if the creditor is a corporation or company. 11 U.S.C. §341(c). Although a debtor may take the 5<sup>th</sup> Amendment privilege, the court may make an adverse inference from the failure to testify. *In re Martinez*, 126 Fed.Appx. 890 (10<sup>th</sup> Cir. 2005).

In a Chapter 7 case, a trustee is appointed from a panel of trustees by the United States Trustee. In a Chapter 13 case in Colorado, there are two "standing" Chapter 13 Trustees: Sally Zeman and Douglas Keil. These trustees conduct many examinations of the debtors and, there may not be sufficient time for a creditor to fully examine the debtor. The creditor may make an *ex parte* request to the Bankruptcy Court to examine the debtor under Fed.R.Bankr.P. 2004 - which is literally described as the "fishing expedition" rule. Rule 2004 is much broader than C.R.C.P. 69 or C.R.C.P. 30.

## 2. Proof of Claim

Whether the debtor files Chapter 7 or Chapter 13, a creditor should always file a proof of claim in the case. Typically, Chapter 7 cases are “no asset” cases and unless the Trustee recovers property, there may not be a distribution. The deadline to file a claim is 90 days after the first date set for the meeting of creditors. Fed.R.Bankr.P. 3002(c). In a “no asset” case, the creditor will not initially receive the form for the proof of claim. The creditor should pay attention to further notices it receives from the Bankruptcy Court as there may be a later date to file the claim. In a Chapter 13 case, a form will be mailed with the notice of the meeting of creditors. In a Chapter 11 case, if the debtor has listed the creditor as not disputed, not contingent, and liquidated, then the creditor need not file a proof of claim if the creditor agrees with the amount listed by the debtor. 11 U.S.C. §1111(a). If the debtor lists the creditor as disputed, contingent or unliquidated, or if the creditor disagrees with the amount listed by the debtor, the creditor should file a proof of claim with the court.

The filing of a proper proof of claim is *prima facie* evidence of the debt. Fed.R.Bankr.P. 3001(f). There are very specific rules on the information that must be contained in the proof of claim. Fed.R.Bankr.P. 3001(c). If the claim is based on a writing, the creditor must attach a copy of the document. Fed.R.Bankr.P. 3001(c)(1). Moreover, the creditor must attach supporting information, including an itemization if the claim includes interest, fees, expenses or other charged. Fed.R.Bankr.P. 3001(c)(2). Failure to provide this documentation and information, may preclude the creditor from introducing such information in a contested hearing. Fed.R.Bankr.P. 3001(c)(2)(D). *See In re Reynolds*, 470 B.R. 138 (Bankr.D.Colo. 2012).

The form may be obtained from the Bankruptcy Court. <http://www.cob.uscourts.gov/forms.asp>. The deadline for filing proofs of claim (known as the “bar date”) cannot be extended under the excusable neglect standard. *Jones v. Arross*, 9 F.3d 79 (10th Cir.1993). However, if the claim is allowed, the creditor will receive a pro rata distribution of assets, following payment of administrative expenses and the Trustee’s fee. 11 U.S.C. §§726, 502, 507, 326.

### 3. Deadline to Object to Discharge and/or Dischargeability

Under Rule 4004(a), a creditor has 60 days after the first date set for the meeting of creditors to file a complaint objecting to a debtor's discharge under Chapter 7, 11 U.S.C. §727(a). The deadline to object to discharge in a Chapter 11 case is no later than the first date set for the hearing on confirmation. In a Chapter 13 case, a motion objecting to the debtor's discharge must be filed no later than 60 days after the first date set for the meeting of creditors.

A new time period for filing complaints objecting to discharge commences when a Chapter 11 or Chapter 13 case is converted to a Chapter 7 case. No new time period is available, however, if a case started in Chapter 7, and the applicable period expired in that original chapter, and the case thereafter was converted to Chapter 11 or 13 and then reconverted to Chapter 7. *See* Fed.R.Bankr.P. 1019(3).

Similarly, under Rule 4007 of the Bankruptcy Rules, a complaint to determine the dischargeability of a debt under 11 U.S.C. §523(c) shall be filed no later than 60 days after the first date set for the meeting of creditors under §341(a) in a Chapter 7, Chapter 11, or Chapter 13 case.

All of these deadlines are typically identified on the Notice of Bankruptcy Case, Meeting of Creditors, & Deadlines issued by the Bankruptcy Court and sent to the creditors. Counsel should calendar the deadlines and consult with the creditor to determine whether it is appropriate to object to a debtor's discharge and/or the dischargeability of the creditor's debt.

### 4. Deadline to Object to Chapter 13 Plan

When a debtor files a case under Chapter 13, they are required to also file a Chapter 13 Plan which tells creditors how they will be repaid, typically over time. *See* 11 U.S.C. §1322. The Notice of Chapter 13 Bankruptcy Case issued by the Court will typically set forth the date of the confirmation hearing, but not the specific date for filing objections to the plan. The last day to file an objection to a Chapter 13 Plan is three (3) court days before the date of the first date set for the meeting of creditors. Fed.R.Bankr.P. 2002(b), 9006 and L.B.R. 3051-1.

Objections to a plan must comply with L.B.R. 3051-1 and clearly specify the grounds upon which they are based and cite applicable legal authority. The Bankruptcy Court will not consider general objections. If the Court denies confirmation of a plan but permits the debtor to file a new

plan, then the Court will set a new date for the filing of objections. However, if the creditor did not file an objection to the initial plan, it may not receive notice of the new deadline to object to the new plan. The creditor and counsel must therefore pay close attention to the proceedings in a Chapter 13 case.

#### 5. Deadline to Object to Exemptions

In Colorado, debtors may claim various exemptions under state law. Personal property is mostly covered under C.R.S. §§13-54-102 and 102.5. Real property that is a debtor's homestead is covered under C.R.S. §38-41-201. There are additional exemptions available under Colorado law which may apply to other kinds of property.

The deadline to object to a debtor's claim of exemption is 30 days after the *conclusion* of the meeting of creditors or within 30 days after any amendment to the debtor's schedules is filed, whichever is later. Fed.R.Bankr.P. 4003(b).

Pre-bankruptcy planning, including whether to move assets from a non-exempt status to exempt status, is not, by itself, fraudulent. *In re Carey*, 938 F.2d 1073 (10th Cir.1991). However, if there is an intent to defraud creditors, usually evidence of the "badges of fraud," courts will deny the exemption for "bad faith." *In re Mueller*, 867 F.2d 568 (10th Cir.1989); *In re Ludwig*, 345 B.R. 310 (Bankr.D.Colo.2006). *See also*, C.R.S. §38-8-105. Generally, the "skinny pig" will maintain his or her exemptions, and the "fat hog" will be denied exemptions and possibly lose the asset. *In re Beaudin*, 2010 WL 3748735 (Bankr.D.Colo. 2010); *but see Law v. Siegel*, 134 S. Ct. 1188 (2014) (holding that bankruptcy court may not surcharge debtor's exemption even in light of bad faith conduct).

#### **B. May the Creditor Obtain Relief from the Automatic Stay?**

There are certain circumstances that a creditor may obtain relief from the automatic stay. If the creditor has a security interest in property, the creditor should determine whether there is any equity in the property over and above the creditor's lien. If there is no equity, or if the creditor's lien is not adequately protected (e.g., lack of insurance, continuing use resulting in diminution, declining value), then the creditor may seek relief from stay under 11 U.S.C. §362(d) which provides:

On request of a party in interest and after notice and a hearing, **the court shall grant relief from the stay** provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay –

1. for cause, including the lack of adequate protection of an interest in property of such party in interest;
2. with respect to a stay of an act against property under subsection (a) of this section, if –
  - (a) the debtor does not have an equity in such property; and
  - (b) such property is not necessary to an effective reorganization;
3. with respect to a stay of an act against *single asset real estate* under subsection (a), by a creditor whose claim is secured by an interest in such real estate, unless, not later than the date that is 90 days after the entry of the order for relief (or such later date as the court may determine for cause by order entered within that 90-day period) or 30 days after the court determines that the debtor is subject to this paragraph, whichever is later –
  - (a) the debtor has filed a plan of reorganization that has a reasonable possibility of being confirmed within a reasonable time; or
  - (b) the debtor has commenced monthly payments that –
    - (I) may, in the debtor’s sole discretion, notwithstanding section 363(c)(2), be made from rents or other income generated before, on, or after the date of the commencement of the case by or from the property to each creditor whose claim is secured by such real estate (other than a claim secured by a judgment lien or by an unmatured statutory lien); and
    - (ii) are in an amount equal to interest at the then applicable nondefault contract rate of interest on the value of the creditor’s interest in real estate; or
4. with respect to a stay of an act against real property under subsection (a), by a creditor whose claim is secured by an interest in such real property, if the court finds that the filing of the petition was part of a scheme to delay, hinder, and defraud creditors that involved either –
  - (a) transfer of all or part ownership of, or other interest in, such real property without the consent of the secured creditor or court approval;  
or
  - (b) multiple bankruptcy filings affecting such real property.

If recorded in compliance with applicable State laws governing notices of interest or liens in real property, an order entered under paragraph (4) shall be binding in any other case under this title purporting to affect such real property filed not later than 2 years after the date of the entry of such order by the court, except that a debtor in

a subsequent case under this title may move for relief from such order based upon changed circumstances or for good cause shown, after notice and a hearing. Any Federal, State, or local governmental unit that accepts notices of interest or liens in real property shall accept any certified copy of an order described in this subsection for indexing and recording.

The automatic stay does not prevent a judgment creditor from attempting to recover on a supersedeas bond even though the indemnity on such bond is secured by a debtor's property. *Edwards v. Armstrong World Indus.*, 6 F.3d 312 (5<sup>th</sup> Cir. 1993), *rev'd on another issue, sub nom., Celotex Corp. v. Edwards*, 115 S. Ct. 1493 (1995). Courts look to various factors to determine whether relief from the automatic stay is appropriate to continue with non-bankruptcy litigation. *In re Curtis*, 40 B.R. 795, 799-800 (Bankr.D.Utah 1984). Such factors include the impact of the litigation on the bankruptcy case, the status of the case as of the bankruptcy filing, and the cost to the debtor of litigating in multiple forums. *Id.*

### **C. Chapter 7 - Liquidation Versus Chapter 13 - Reorganization**

Generally speaking, a debt is secured only up to the value of the collateral. 11 U.S.C. §506(a). Any amounts that are owed in excess of the value are unsecured. In an individual Chapter 7 or Chapter 13 case, such value with respect to personal property is determined using the replacement value. 11 U.S.C. §506(b). The Bankruptcy Code sets forth a priority scheme under which creditors may receive payment on their claims. 11 U.S.C. §502. Administrative expenses of the bankruptcy, including the trustee's fees and costs, have priority over unsecured claims. 11 U.S.C. §§503, 326, 502, 726, 1326.

If there are non-exempt assets available for distribution in a Chapter 7 case, the Trustee will make the distributions at the end of the case. 11 U.S.C. §726. Thus, it is important for the creditor to timely file a proof of claim in order to receive a distribution. However, if the Chapter 7 Trustee has funds left over after an initial distribution to timely filed claims, the Trustee may pay tardily filed claims. 11 U.S.C. §726(a)(2).

In a Chapter 13 case, the confirmed Plan will dictate how and when each creditor may receive payment on their claim. Chapter 13 is typically used to stretch out payments to secured creditors to cure any defaults, to domestic support creditors for any arrears, and/or to pay tax liabilities over time.

If a Chapter 13 debtor is not paying unsecured creditors in full, the debtor must devote all of their net disposable income over the applicable commitment period (typically 3 to 5 years) for their plan if the Chapter 13 Trustee or an unsecured creditor objects to the plan. 11 U.S.C. §1325(b)(1).

#### **D. Asset Sales, Financing, Surcharge and Cash Collateral Issues**

The Chapter 7 Trustee, or the debtor-in-possession in a Chapter 13 case, may use, sell or lease secured property in the ordinary course of business. 11 U.S.C. §363(b). The Trustee or debtor may also sell the secured property free and clear of liens in certain circumstances. 11 U.S.C. §363(f). The Trustee or debtor may even sell property the debtor co-owns with a non-debtor. 11 U.S.C. §363(h)

During bankruptcy, a debtor must provide adequate protection to a secured creditor if the debtor is retaining and/or using the secured property. 11 U.S.C. §361. The form of adequate protection can be cash payments, additional or replacement liens or other relief designed to protect the secured creditor. *Id.*; *United Savings Ass'n v. Timbers of Inwood Forest Associates, Ltd.*, 484 U.S. 365 (1988).

Under *Chaussee v. Morning Star Ranch Resorts Company*, 64 B.R. 818 (Bankr.D.Colo. 1986), a debtor in possession may use a secured creditor's cash collateral in much the same fashion as a receiver would be permitted to use cash from operations under state law. In other words, a Chapter 13 or Chapter 11 debtor may continue to operate its business in the ordinary course and use a secured creditor's collateral in the debtor's cash to fund operations. However, the Trustee must obtain court approval to use, sell or lease secured property outside of the ordinary course, or obtain the consent of the secured creditor. 11 U.S.C. §363(c)(2).

Under 11 U.S.C. § 506(c), a debtor-in-possession "may recover from property securing an allowed secured claim the reasonable, necessary costs and expenses of preserving, or disposing of, such property to the extent of any benefit to the holder of such claim." *See Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 6, fn. 3 (2000).

A debtor or trustee in bankruptcy may incur unsecured debt in the ordinary course without court approval. 11 U.S.C. §364(a). Any credit or debt outside the ordinary course or granting of liens against property requires court approval. 11 U.S.C. §§364(b) and (c).



## **E. Discharge and Dischargeability**

In a Chapter 7 case where the debtor is an individual, the court must grant the debtor a discharge of all of his or her debts unless one or more of 12 different factors are met. 11 U.S.C. §727(a). Such factors include a debtor's fraudulent transferring of assets, concealment of assets, destruction of records, making a false oath, failing to explain satisfactorily any loss of assets or deficiency of assets to meet the debtor's liabilities. *Id.* This provision is typically referred to as the "fresh start" provision and/or the "big discharge." "Exceptions to discharge are to be narrowly construed, and because of the fresh start objectives of bankruptcy, any doubt is to be resolved in the debtor's favor." *In re Sandoval*, 541 F.3d 997, 1001 (10th Cir. 2008) (quotation omitted).

Generally, all of a debtor's debts are subject to discharge in bankruptcy. Under 11 U.S.C. §523(a), there are certain types of debts that cannot be discharged. Such debts include:

- (1) taxes or customs duty to the Federal government;
- (2) money, property, services or extension or renewal of credit obtained by false pretenses; or by use of a statement in writing that is materially false; respecting the debtor's or an insider's financial condition; on which the creditor reasonably relied.
- (3) unscheduled debts, if known to the debtor;
- (4) any debt for fraud, defalcation while acting in a fiduciary capacity, embezzlement or larceny;
- (5) domestic support obligation;
- (6) any debt for willful or malicious injury by the debtor to another or to property of another;
- (7) government penalty or fine;
- (8) unless excepting the debt would impose undue hardship on the debtor and dependents for any educational loan;
- (9) debt for death or personal injury caused while operating a vehicle while intoxicated;
- (10) debt scheduled in a prior case in which the debtor waived discharge or was denied discharge;
- (11) debt owed to FDIC under an order or to an insured credit union;
- (12) debt for malicious or reckless failure or fulfill any commitment to the FDIC;
- (13) payment of an order of restitution that was issued under Title 18, U.S.C.;
- (14) incurred to pay a tax owed to a state or other governmental unit that would be nondischargeable pursuant to paragraph 1 or fines or penalties imposed under Federal election law;
- (15) payments to a spouse, former spouse, or child of the debtor under a separation agreement or divorce decree;
- (16) home owner's association dues and assessments;
- (17) fee imposed on a prisoner for filing a case, motion, complaint, or appeal;

- (18) debt owed to pension fund or profit sharing plan; and
- (19) debt incurred due to violation of Federal Securities Laws.

Claims under Colorado's Mechanic's lien Trust Fund Statute are not dischargeable in bankruptcy. C.R.S. §38-22-127; 11 U.S.C. §523(a)(4); *In re Regan*, 477 F.3d 1209 (10<sup>th</sup> Cir. 2007). Under *Bullock v. BankChampaign, N.A.*, 569 U.S. \_\_\_\_, No. 11-1518, 2013 WL 1942393 \* 4 (May 13, 2013), there is a heightened standard of scienter for claims under Section 523(a)(4). *Id.* A plaintiff must show that a debtor had knowledge of, or gross recklessness in connection with, the improper nature of the debtor's her conduct. *Id.* To recover treble damages under Section 523(a)(4), a creditor must prove specific evidence of violation of Colorado's Civil Theft Statute. C.R.S. §18-4-405; *Itin v. Ungar*, 17 P.3d 129 (Colo. 2000).

As with a claim under Section 727(a), claims under Section 523(a) are construed liberally in favor of the debtor and strictly against the creditor. *In re Warren*, 512 F.3d 1241, 1248 (10<sup>th</sup> Cir. 2008)(quoting *Gullickson v. Brown*, 108 F.3d 1290, 1292 (10<sup>th</sup> Cir.1997)).

#### **F. Means Testing and "Abusive Filing"**

Individual debtors whose debts are primarily consumer debts must pass a "means test" based upon their current monthly income; otherwise, they are not eligible for a Chapter 7 case. 11 U.S.C. §707(b). However, if a simple majority of a debtor's debts are non-consumer related, then the "means test" provisions of the Bankruptcy Code do not apply. *Id.* Whether to seek dismissal of a consumer case under an abuse is a difficult and complex one. If a trustee files a motion to dismiss a Chapter 7 case for abuse and the Court grants the motion and finds that either the debtor or the debtor's attorney violated Fed.R.Bankr.P. 9011, the Court may award the Trustee all of his or her costs, including attorney's fees, or a civil penalty. 11 U.S.C. §707(b)(4). Conversely, the Bankruptcy Court may award a debtor all reasonable costs, including attorney's fees, incurred in contesting a motion to dismiss for abuse if the Court finds that the position of the party filing the motion violated Fed.R.Bankr.P. 9011 and the Court denied the motion. 11 U.S.C. §707(b)(5).

If a consumer debtor does not qualify for a Chapter 7 case, typically because their income exceeds the IRS guidelines, they may file a Chapter 13 bankruptcy case or Chapter 11 bankruptcy case depending upon the size of their debt. 11 U.S.C. §109(e). Only individual debtors who have regular income and whose secured debts are less than \$1,149,525, and noncontingent, liquidated unsecured debts are less than \$383,175 are eligible for a Chapter 13 bankruptcy case. *Id.* If their debts exceed those limits, the debtor has the option of filing a Chapter 11 case.

#### **G. Reclamation Claims and Preferences.**

A seller of goods on credit may demand to reclaim the goods upon the buyer's insolvency. C.R.S. §4-2-702. Bankruptcy recognizes this state law right. 11 U.S.C. §546(c). If a contractor or materialman does provide goods and desires to reclaim, they must take action timely. The demand must be made within 20 days of the bankruptcy filing, so long as the goods were supplied within the last 45 days. *Id.*

A creditor of a debtor should also be concerned about payments it received within the 90 days prior to a debtor's bankruptcy filing. Payments made to or for the benefit of a creditor of a debtor within 90 days on account of an old debt are avoidable by a Chapter 7 Trustee (or Chapter 11 debtor), if the creditor received more than it would have in a liquidation. 11 U.S.C. §547(b). Transferring balances from one credit card to another is a preferential transfer. *Parks v. FIA Card Services, N.A. (In re Marshall)*, 550 F.3d 1251 (10<sup>th</sup> Cir. 2008). A debtor is presumed insolvent in the 90 days before bankruptcy. 11 U.S.C. §547(f). However, creditors who receive payments in the ordinary course of business or for contemporaneous exchange for new value have defenses to the avoidance claims. 11 U.S.C. §547(c).

#### **H. Landlord-Tenant Issues.**

If you are a landlord, there are special protections available to you in bankruptcy. As discussed above, the automatic stay prohibits any eviction action or collection action for pre-bankruptcy rents. 11 U.S.C. §362(a)(6). However, if a residential landlord obtained an order or judgment for possession *before* the bankruptcy case was filed, the landlord may proceed with the eviction without seeking relief from the bankruptcy court. 11 U.S.C. §362(b)(22).

Once the bankruptcy case is filed and until a debtor rejects a lease, the debtor must perform all duties under the lease in a timely manner. *See* 11 U.S.C. §365(d)(3). If the debtor fails to perform the obligations under the lease, including rents, the landlord may have an administrative claim against the bankruptcy estate if the claim meets the requirements of 11 U.S.C. §503(b) as a reasonable and necessary expense of preserving the estate. *General Am. Transport, Inc. v. Martin (In re Mid Region Petroleum, Inc.)*, 1 F.3d 1130 (10<sup>th</sup> Cir. 1993).

If debtor-in-possession or Trustee intends to assume a lease in bankruptcy, if there was a default in the lease, the debtor-in-possession or Trustee must cure all monetary obligations at the time of assumption, compensate the landlord for any actual pecuniary loss, and provide adequate assurance of future performance. 11 U.S.C. §365(b). A debtor cannot be in breach of a lease merely by filing bankruptcy. 11 U.S.C. §365(e).

The debtor-in-possession or Trustee may reject any unexpired lease. 11 U.S.C. § 365(a). In a Chapter 7 case, if the Trustee does not assume or reject a lease of residential property within 60 days after the voluntary case was filed, the lease is automatically deemed rejected. 11 U.S.C. §365(d)(1). In a Chapter 11 or 13 case, the debtor-in-possession or Trustee has until the confirmation of the plan to assume or reject the lease. 11 U.S.C. §365(d)(2). With respect to nonresidential real property, the lease is deemed rejected on the earlier of 120 days after the voluntary case is filed, or the date of the entry of an order confirming a plan. 11 U.S.C. §365(d)(4).

Except in certain narrowly circumscribed instances, rejection of an executory contract or lease constitutes a material breach. 11 U.S.C. § 365(g). As a legal fiction, such a breach is deemed to have occurred on the day immediately prior to the commencement of the bankruptcy, so rejection claims are treated as pre-petition claims. 11 U.S.C. §§ 365(g)(1) & 502(g). If a lease is rejected, the landlord has a claim against the bankruptcy estate for the rent reserved by such lease, without acceleration, for the greater of one year, or 15 percent, not to exceed three years, of the remaining term of such lease, following the earlier of: (i) the date of the filing of the petition; and (ii) the date on which the lessor repossessed, or the leasee surrendered, the leased property, plus, any unpaid rent due under such lease, without acceleration, on the earlier of such dates. 11 U.S.C. §502(b)(6). The landlord must file a proof of claim with the Bankruptcy Court for such “rejection damages.” For any

unpaid post-petition rents and charges, the landlord must timely file a motion to allow the claim under 11 U.S.C. §503(b).

#### **I. Reaffirmation Agreements and Secured Personal Property.**

Under 11 U.S.C. §524(c), certain kinds of debts may be reaffirmed during a bankruptcy case. The effect of reaffirming a debt is that while the debt may be dischargeable, the debtor has agreed to waive his or her discharge as to that one debt. There are very specific requirements, disclosures and forms for a reaffirmation agreement. 11 U.S.C. §524(k). Such forms are available at <http://www.uscourts.gov/FormsAndFees/Forms/BankruptcyForms.aspx>. The reaffirmation agreement must be entered into prior to the entry of a discharge, the debtor must receive the required disclosures, and the agreement must be filed with the Court. 11 U.S.C. §524(c). Failure to follow all of the requirements for a reaffirmation agreement will result in a discharge of the debt.

Under 11 U.S.C. §521(a)(2), an individual debtor is required to state his/her intention to surrender, redeem or reaffirm the debt to a creditor whose debt is secured by personal property and then to timely perform such intention. Section 521(a)(2) provides in relevant part:

- (a) The debtor shall –
- (2) if an individual debtor’s schedule of assets and liabilities includes consumer debts which are secured by property of the estate -
  - (A) within thirty days after the date of the filing of the petition under Chapter 7 of this title or on or before the date of the meeting of creditors, whichever is earlier, or within such additional time as the court, for cause, within such period fixes, the debtor shall file with the clerk a statement of his intention with respect to the retention or surrender of such property and, if applicable, specifying that such property is claimed as exempt, that the debtor intends to redeem such property, or that the debtor intends to reaffirm debts secured by such property;
  - (B) within 30 days after the first date set for the meeting of creditors, under section 341(a), or within such additional time as the court, for cause, within such 30-day period fixes, the debtor shall perform his intention with respect to such property, as specified by subparagraph (A) of this paragraph; and
  - (C) nothing in subparagraph (A) and (B) of this paragraph shall alter the debtor’s or the trustee’s rights with regard to such property under this title, except as provided in section 362(h).

Pursuant to 11 U.S.C. §362(h), the automatic stay provided pursuant to §362(a) shall terminate with respect to personal property securing a debt and such personal property shall cease to be property of the estate unless the debtor timely files a statement of intention under §521(a)(2)(A) and timely performs such intention under §521(a)(2)(B) unless the court determines:

On motion of the trustee filed before the expiration of the applicable time set by section 521(a)(2), after notice and a hearing, that such personal property is of consequential value or benefit to the estate, and orders appropriate adequate protection of the creditor's interest, and orders the debtor to deliver any collateral in the debtor's possession to trustee.

11 U.S.C. §362(h)(2).

In addition, with respect to a purchase money security interest, 11 U.S.C. §521(a)(6) provides that an individual debtor in a Chapter 7 case may not retain possession of personal property as to which a creditor has an allowed claim for the purchase price secured in whole or part by an interest in such personal property, unless the debtor, not later than 45 days after the first meeting of creditors either enters into a reaffirmation agreement with the creditor under Section 524(c) with respect to the claim secured by such property, or redeems such property from the security interest pursuant to Section 722.

Section 521(a)(6) further provides that if the debtor fails to act within the 45-day period, the stay under §362(a) is terminated with respect to such personal property, such property shall no longer be property of the estate, and the creditor may take whatever action as to such property as is permitted by applicable non-bankruptcy law, unless the Court determines on the motion of the trustee filed before the expiration of such 45-day period, and after notice and a hearing, that such property is of consequential value or benefit to the estate, orders appropriate adequate protection of the creditor's interest, and orders the debtor to deliver any collateral in the debtor's possession to the trustee.

## **K. Jurisdictional Issues in Bankruptcy Court**

In *Stern v. Marshall*, the Supreme Court held the Bankruptcy Court lacked authority under Article III of the Constitution to enter a final judgment on a Debtor's counterclaims brought in response to a creditor's proof of claim in the case. 131 S.Ct. 2594 (2011). The Supreme Court found that Congress overstepped its authority in authorizing bankruptcy judges, under Article I of the U.S. Constitution, to hear and decide "non-core" matters, essentially private-right controversies. The counterclaims in *Stern* were state law claims that did not implicate a public right under the Bankruptcy Code. Thus, the Supreme Court found that only Article III courts (or state courts of general jurisdiction) could decide private-right disputes.

When a claim for relief invokes "plenary" jurisdiction, the claim is outside the jurisdiction granted to the Bankruptcy Court. *In re Ball Four, Inc.*, slip op., Case No. 12-1036 EEB, Docket No. 80 at 6 (Bankr.D.Colo., Sept. 30, 2013)(Brown, J.). In other words, when a claim seeks to bring assets from outside into a bankruptcy estate, the Bankruptcy Court lacks jurisdiction to fully adjudicate such claims. *Id.* at 8. State law claims of breach of contract and implied duty of good faith and fair dealing claims are "related to," non-core matters. *Id.*

Following *Stern*, the Supreme Court again weighed in the morass of bankruptcy jurisdiction in *Executive Benefits Insurance Agency v. Arkison*, 134 S.Ct. 2165 (2014). In *Arkison*, the Chapter 7 bankruptcy trustee filed a complaint asserting both federal and state law claims, including fraudulent transfers claims. The question in *Arkison* was whether the bankruptcy judge's submission of proposed findings of fact and conclusions of law to the U.S. District Court for *de novo* review was sufficient under *Stern*. The Supreme Court said that since the bankruptcy court could not enter a final judgment, *de novo* review by the District Court comported with Article III jurisdiction and *Stern*. The Supreme Court however did not decide the question of whether a party's actions during litigation resulted in an implied consent to bankruptcy court jurisdiction over the non-core claims.

Recently, in *Wellness International Network v. Sharif*, 135 S.Ct. 1932 (2015), the Supreme Court held that bankruptcy courts may enter final judgments on non-core claims if a litigant consents, either express or implied. The Court found that the consent must be knowing and

voluntary. In doing so, the Court adopted the functional approach set forth in *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833 (1986). Thus, litigants may waive their right to a determination by an Article III court and have their cases decided by the Article I bankruptcy judges.

1. Concurrent Jurisdiction of Federal Bankruptcy Courts and State Courts

Pursuant to 11 U.S.C. §523(a)(3), a discharge in bankruptcy does not discharge a debt under Sections 523(a)(2)[fraud], (a)(4)[fiduciary fraud, embezzlement, larceny], or (a)(6)[willful and malicious injury], if the debt was not listed in the bankruptcy case and the creditor did not have actual notice of the case. If a creditor then commences an action in state court, a debtor may argue that the action violates the bankruptcy stay (or injunction), or assert the bankruptcy discharge as an affirmative defense. *See* 11 U.S.C. §§362(a); 524(a); C.R.P.C. 8(c); Fed.R.Civ.P. 8(c).

This issue was addressed in *In re Manning*, Case No. 10-23188-HRT (Bankr. D. Colo. June 19, 2012). *Manning* overruled the earlier *In re Padilla* decision holding that:

Moreover, even if the Herbs' State Court Complaint made no claim to post-petition damages, it does make claims of nondischargeability that are cognizable under § 523(a)(3)(B). The State Court enjoys jurisdiction, concurrent with the federal courts, to determine if any of those obligations are nondischargeable under 11 U.S.C. § 523(a)(3)(B).

In another case, *In re Everly*, 346 B.R. 791 (B.A.P. 8th 2006), the Court notes:

In short, the penalty to the debtor for failing to schedule a [debt under § 523(a)(2)(4) or(6)] or otherwise inform the creditor of the bankruptcy is forfeiture of the right to enjoy exclusive federal jurisdiction and loss of the sixty-day limitations period applicable in the exclusive jurisdiction actions." *In re Jenkins*, 330 B.R. 625, 631 (Bankr.E.D.Tenn.2005)(quoting *First Nat'l Ins. Co. of Am. v. Bartomeli (In re Bartomeli)*), 303 B.R. 254, 269 797\*797 (Bankr.D.Conn.2004); Fed. R. Bankr.P. 4007(b).

Likewise, *In re Massa*, 217 B.R. 412 (Bankr. W.D.N.Y. 1998), held that:

[C]oncurrent jurisdiction to determine that an unsecured debt is nondischargeable pursuant to Section 523(a)(3)(B) exists from the moment a debtor files the schedules required by Section 521 and Rule 1007 and they fail to list a prepetition debt "of a kind specified" in Section 523(a)(2), (4), (6) or (15) with the name of the creditor holding the debt, and continues until either: (a) the schedules are amended so that a timely request for a determination of dischargeability is reasonably possible; or (b)



the bankruptcy court or a state court with concurrent jurisdiction makes a determination of dischargeability pursuant to Section 523(a)(3)(B), notwithstanding that the creditor holding the unsecured debt may have received notice or had actual knowledge of the debtor's bankruptcy case; and (2) once the state court assumes and exercises its concurrent jurisdiction to determine that an unsecured debt is nondischargeable pursuant to Section 523(a)(3)(B), the *Rooker-Feldman Doctrine* is applicable and the bankruptcy court can no longer assume jurisdiction, pursuant to Section 524(a) or otherwise, to correct any erroneous determination.

So, the applicable court will have to decide at least four things:

- a. Is the debt of a kind described in § 523(a)(2), (4), or (6)?
- b. Was the debt listed or scheduled (as that term has been interpreted) under § 521(1) of the Bankruptcy Code with the name of the plaintiff?
- c. Did the plaintiff have actual knowledge of the case in time to timely file an adversary proceeding in the bankruptcy court under § 523(a)(2), (4), or (6)?
- d. Does the plaintiff's case have merit?

**K. Last Words:**

Deadlines in bankruptcy are extremely important and the failure to observe them or to act timely can jeopardize the creditor's rights, claims or interests in the case. Consultation with competent bankruptcy counsel, and/or conducting extensive research on a creditor's rights and remedies in bankruptcy is highly recommended before proceeding in the bankruptcy case.

**About the presenter:** Ken Buechler specializes in representing small and closely-held businesses, individuals with complex debt structures, and fiduciaries who recover assets from Ponzi schemes. His work includes creditor-debtor workouts, as well as bankruptcy reorganization and liquidations. Ken has been involved in representing creditors, debtors, trustees and creditors' committees in such industries as real estate investment and development, hotels, heavy equipment, residential and commercial construction, trucking, oil and gas, farming and dairy operations, banking, and municipalities. His bankruptcy practice also includes the restructuring side of representing debtors, including financial work outs and asset protection.



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## RESOURCEFUL LINKS

U.S. Bankruptcy Court, Colorado: [www.uscourts.cob.gov](http://www.uscourts.cob.gov).

American Bankruptcy Institute: [www.abiworld.org](http://www.abiworld.org).

CM/ECF [case filing] for Colorado Bankruptcy Court: <https://ecf.cob.uscourts.gov>.

National PACER home page: [www.pacer.gov](http://www.pacer.gov).

U.S. Trustee's Office, for Region 19: <http://www.justice.gov/ust/r19/index.htm>

More on Bankruptcy Basics and further resources:

<http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics.aspx>

<http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyResources.aspx>