SUFFOLK ACADEMY OF LAW
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ZOOM PROGRAM

ANNUAL BANKRUPTCY UPDATE

FACULTY

Hon. Alan S. Trust, U.S. Bankruptcy Court Judge
Hon. Robert E. Grossman, U.S. Bankruptcy Court Judge
Hon. Louis A. Scarcella, U.S. Bankruptcy Court Judge
Christine Black Esq., Assistant U.S. Trustee
Shari Barak, Esq., Peter Corey, Esq., Dawn Kirby, Esq., Adam Wofse, Esq.

Program Coordinator: Richard L. Stern, Esq.

June 23, 2020
Suffolk County Bar Association, New York

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BANKRUPTCY UPDATE PROGRAM
JUNE 23, 2020
VIA ZOOM
SUFFOLK COUNTY BAR ASSOCIATION
4 PM – 6 PM

PROPOSED AGENDA:

4:00 – 4:05 pm	Introduction
4:05 – 4:30 pm	Small Business Reorganization Act update (Dawn Kirby)
4:30 – 4:50 pm	Recent national cases of interest (Chris Black)
4:50 – 5:20 pm	Recent EDNY decisions (Sal LaMonica)
5:20 – 5:40 pm	Chapter 13 cases and COVID (Shari Barak & Peter Corey)
5:40 – 6:00 pm	Judges' Forum – what they have to say

THE HONORABLE ALAN S. TRUST
United States Bankruptcy Judge for the Eastern District of New York

The Honorable Alan S. Trust ascended to the bench on April 2, 2008, and sits in the Eastern District of New York. He is an adjunct professor of law at the St. John's University School of Law, a past Chair of the Bankruptcy Law Section of the Federal Bar Association, a member of the Board of Directors of that Section, and has served as the CLE Committee chair. He is also President of the Eastern District of New York Chapter of the Federal Bar Association, and serves as CLE Committee co-chair. He is a member of the Editorial Board of the American Bankruptcy Institute *Journal*, is a coordinating editor for the *Journal,* and for several years has had responsibility for the *Dicta* column. He is also a member of the American Bankruptcy Institute and the National Conference of Bankruptcy Judges.

During his tenure on the bench, Judge Trust has been designated by the Second Circuit Court of Appeals to mediate cases in the Southern District of New York and to sit in the District of Connecticut bankruptcy court. Judge Trust also serves on the Judiciary Data Working Group under the auspices of the Administrative Offices of the United States Courts.

Judge Trust is a frequent speaker and author for numerous CLE events and seminars, addressing bankruptcy, mediation and ethics issues. He is a trained mediator, and was instrumental in the creation of a Pro Bono Mediation Program and the formation of the Consumer Lawyer Advisory Committee adopted by the Bankruptcy Court for Eastern District of New York.

Judge Trust attended Syracuse University, graduating summa cum laude in 1981, and as a member of Phi Beta Kappa. He attended New York University School of Law, where he served on the Law Review from 1982-83, and graduated cum laude in 1984. After graduation, he relocated to Dallas, Texas to begin his law practice. Judge Trust opened his own law firm (Trust.Law.Firm, P.C.) in Dallas in December 1995, and managed that firm until appointed to the bench.

Robert E. Grossman

A graduate of Rider University, Robert E. Grossman earned his J.D. in 1973 from Brooklyn Law School. He began his legal career at the Securities and Exchange Commission in the Division of Enforcement in a group associated with the Division of Corporate Finance. After leaving the SEC, Judge Grossman founded and served as general counsel to a large financial services company that focused on acquiring and operating distressed assets.

Most recently, Judge Grossman practiced in the area of corporate law, business reorganization and litigation at Duane Morris. A significant part of his practice focused on providing advice to troubled or newly restructured companies, and investors, with respect to the financing needs of such companies. Judge Grossman has extensive experience in complex bankruptcy and creditor rights litigation for both individuals and institutions and has represented parties in the restructuring and transfer of assets in the bankruptcy court. Experienced in the intricacies of bankruptcy and restructuring matters across a wide range of industries, including real estate and healthcare, he represented borrowers, secured creditors, landlords and owners across the United States. Prior to joining Duane Morris, Judge Grossman was the chair of the restructuring practice group at Arent Fox, directing almost 20 professionals in matters across the United States and in Europe.

Judge Grossman is an adjunct professor at Touro Law School. He is also a past Chair of the International Secured Transactions and Insolvency Committee of the American Bar Association, Section of International Law and is a frequent speaker both in the United States and Europe. In addition, Judge Grossman was the past president of the Brooklyn Law School Alumni Association.

Courtroom Deputy: Madrie Tagle
Law Clerks: Lynn Ryan, Catherine Cozzette,

Louis A. Scarcella was sworn in as a United States Bankruptcy Judge for the Eastern District of New York on May 16, 2014. At the time of his appointment, he was a shareholder in the law firm of Farrell Fritz, P.C. where he was the Bankruptcy Practice Group Leader. During his tenure at Farrell Fritz, P.C. he had a diverse restructuring and litigation practice representing debtor entities, secured creditors, creditors' committees, equity interests, and parties seeking to purchase the assets of, or invest in, financially troubled companies. Before joining Farrell Fritz, P.C., Judge Scarcella was a partner in the law firm of Phillips Nizer LLP where he served as chair of the bankruptcy and creditors' rights practice group.

Judge Scarcella has practiced bankruptcy law exclusively during his career in private practice and has written and lectured on both business and consumer bankruptcy topics. He is a contributing author to Collier Bankruptcy Practice Guide and is an Adjunct Professor of bankruptcy law at the Maurice A. Deane School of Law at Hofstra University. He is a member of the Federal Bar Council, the American Bankruptcy Institute and the National Conference of Bankruptcy Judges.

CHRISTINE H. BLACK

Currently, the Assistant United States Trustee for the Eastern District of New York, Central Islip Division, Ms. Black was previously employed in the bankruptcy unit at Robinson Brog Leinwand Greene Genovese & Gluck, P.C., first as an associate in 1990 and from 1997 until 2008, as a partner. At Robinson Brog, Ms. Black represented debtors, creditors, creditors' committee, and chapter 7 and chapter 11 trustees in numerous bankruptcy and adversary proceedings, including discharge and dischargeability actions, claims allowance and preference litigation. Before joining Robinson Brog in 1990, Ms. Black was a trial attorney with the Office of the United States Trustee for the Eastern District of New York and had previously worked for a bankruptcy firm and chapter 7 trustee handling chapter 7, chapter 11 and chapter 13 matters in the Bankruptcy courts for the Southern and Eastern Districts of New York. Ms. Black is the author of "Chapter 7 Trustee's Ex Parte Request to Use U.S. Marshall to Search Debtor's Home for Undisclosed Assets Complies with the Fourth Amendment,"published in ABI Commercial Fraud Task Force Committee newsletter.

KIRBY AISNER & CURLEY LLP

Dawn Kirby, Esq.

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Dawn Kirby is a bankruptcy attorney with over 25 years' experience representing corporate and consumer debtors and creditors in bankruptcy and restructuring matters.

She received her Juris Doctor degree from Brooklyn Law School where she received honors and was a semi-finalist in the Conrad B. Duberstein National Bankruptcy Moot Court Competition. She received her Bachelor of Arts degree from Skidmore College, with a double major in Government and History.

Dawn was previously a partner at DelBello Donnellan Weingarten Wise & Wiederkehr LLP in White Plains, New York, and a member of the Financial Restructuring Group at King & Spalding LLP in New York City and Atlanta.

Dawn serves as a mediator in commercial and bankruptcy matters, having completed a 40-hour mediation training course sponsored by St. John's Law School and the American Bankruptcy Institute. She also Dawn co-founded the *pro se* bankruptcy clinic at Legal Services of the Hudson Valley which provides bankruptcy counseling to individuals who fall below the Federal poverty line.

Dawn is active in many professional organizations:

New York State Bar Association
- Member, House of Delegates
- Former Member, Committee on Women in the Law, Nominating Committee

Westchester County Bar Association
- Past President (2014 – 2015)
- Co-Chair: Golf Committee, Awards Committee, By-Laws Committee
- Former Co-Chair, Bankruptcy Committee

Westchester Women's Bar Association
- Past President (2005 – 2007)
- Former Co-Chair, Bankruptcy Committee

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ADAM P. WOFSE is a partner at LaMonica Herbst & Maniscalco, LLP. Adam represents debtors in Chapters 7, 11 and 13, creditors, creditors' committees, Chapter 7 trustees and Chapter 11 operating trustees.

Adam has represented Chapter 11 debtors in a variety of reorganization cases, including in the fields of: construction and mechanical industries; health care and durable medical equipment providers; nursery school and child care providers; houses of worship; real estate owners and developers; restaurants and food service providers; hardware and alarm companies; golf courses; boating marinas; self-storage facilities; and cosmetic and online retailers.

Adam represented the Visiting Nurse Association of Long Island (VNA) in its Chapter 11 case, which resulted in a confirmed reorganization plan and a sale of substantially all of the assets of the VNA to a large health care conglomerate, providing payment in full to all creditors, plus interest to unsecured creditors.

Adam has written bankruptcy articles and served as a seminar panelist for:

- Co-author of the New York Law Journal's Long Island Bankruptcy Column (2002-2004)
- Long Island Turnaround Management Association (website).
- Panelist Nassau County Bar Association, Bankruptcy Committee
- Panelist for New York State Bar Association, Bankruptcy Committee
- Panelist for Eastern District of the New York Chapter of the Federal Bar Association
- Speaker for Bankruptcy Court for the Eastern District of New York, Nuts and Bolts Bankruptcy Electronic Case Filing Presentation.

Adam has also provided pro bono bankruptcy legal services to The Safe Center LI.

Shari Barak, Esq. is a Member of Shapiro DiCaro and Barak and the Managing Attorney of the Melville office. She has extensive experience in real estate and commercial law, including residential mortgage foreclosures, closings, litigation, evictions and bankruptcy law involving representation of secured creditors

She is co-chair of the Consumer Lawyer Advisory Committee for the Eastern District, Central Islip. She is a member of the New York State Bar Association, Nassau County Bar Association, Suffolk County Bar Association, Hudson Valley Bankruptcy Bar Association, and the Capital Region Bar Association, the American Bankruptcy Institute, National Creditors Bar Association and the National Association for Chapter 13 Trustees.

She attended George Washington University as an undergraduate and for law school.

PETER COREY, is a member of the law firm of Macco & Corey, PC, where he practices exclusively in the area of bankruptcy, insolvency and creditor's rights. Mr. Corey has represented financial institutions, banks, car finance companies, various creditors as well as individual and corporate debtors and Trustees in every aspect of Bankruptcy for the past 18 years. He graduated, Cum Laude, with a B.S. from John Jay College of Criminal Justice and a J.D. degree from St. John's University School of Law. Mr. Corey is the staff attorney to one of the Standing Chapter 13 Trustees for the Eastern District of New York. He is a member of the Suffolk County Bar Association, where he formerly served as Co-Chairman of the Bankruptcy and Insolvency Committee.

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Eastern District of New York
Bankruptcy Update Program
April 24, 2020

The New Subchapter V
The Small Business Reorganization Act

Dawn Kirby, Esq.
Kirby Aisner & Curley LLP

The Small Business Reorganization Act ("SBRA") was signed into law on August 23, 2019 and became effective on February 19, 2019. The SBRA created a new subchapter of Chapter 11 which is meant to streamline and reduce the prohibitive costs of reorganizing a debtor with no more than $2,725,625 in secured and unsecured debt.

Options

The SBRA is available to both businesses and individuals. A debtor must opt-in to Subchapter V. The SBRA does not repeal the existing small business reorganization provisions, but rather provides an alternative. A SARE may not elect Subchapter V.

The election is located in Item 13 of the Voluntary Petition. Rule 1020 will continue to provide the UST and other parties in interest an opportunity to object to the designation within 30 days after the conclusion of the §341(a) meeting.

Status Conference and Report

The SRBA requires a status conference within the first 60 days of the Petition Date. The debtor must file a report at least 14 days before the conference (46 days into the case) disclosing its efforts to attain a consensual plan of reorganization. §1188(c)

Plan Within 90 Days

The debtor must file a Plan within 90 days of the Petition Date. The period may be extended if "attributable to circumstances for which the debtor should not justly be held accountable. §1189(b)

Only the Debtor May File a Plan

Only the debtor may file a Plan, no competing plans are permitted. §1181(a)

No Committee

No committee will be appointed under Subchapter V unless the court for cause orders otherwise. §1181(b)

No UST Fees

Quarterly US Trustee fees are inapplicable.

No Disclosure Statement

No disclosure statement is required unless the court for cause orders otherwise. §1181(b). A plan shall include a brief history of the business operation of the debtor, a liquidation analysis and projections with respect to the ability of the debtor to make payments under the proposed plan of reorganization. §1190

If the court orders a disclosure statement, the provisions of §1125(f) "shall apply". §1187(c). That means the court can determine the plan itself provides adequate information, the disclosure statement may be a standard form implemented by local rules, the court may conditionally approve a DS subject to final approval at the confirmation hearing, solicitation of acceptances and rejections may move forward based on a conditionally approve DS, and there may be a single combined hearing on adequacy of the DS and confirmation.

No Absolute Priority Rule

The rule that owners of a company that is not paying its creditors in full may not retain their interest unless an impaired class votes to accept the plan unless they contribute new value [§1129(b)] does not apply. This permits business owners a greater opportunity to retain ownership interests.

Modified Cramdown Rules

If all impaired classes do not vote to accept the plan, the court may confirm the plan so long as it does not discriminate unfairly and is "fair and equitable" §1191(b)

The term fair and equitable has been modified to mean

(A) All of the projected disposable income of the debtor within a 3-year period (or longer not to exceed 5 years) will be paid to creditors under the plan; or

(B) There is a reasonable likelihood that the debtor will be able to make all payments under the plan and the plan provides appropriate remedies (including liquidation of non-exempt assets) to protect creditors if payments are not made.

Disposable income is defined as – for individuals - income not reasonably necessary for the maintenance of the debtor or a dependent, a DSO that becomes payable after the

Petition Date and – for businesses – expenditures necessary for the continuation, preservation or operation of the business. §1191(d)

In an individual case, if the plan is approved without the consent of all impaired classes, property of the estate includes all acquired post-petition property and earnings.

Appointment of a Trustee

The SBRA provides for a Subchapter V trustee to be appointed in every case, but with limited powers. This adds an additional layer of cost to the Debtor.

The Trustee's duties include:

Facilitate the development of a consensual plan and make distributions under the plan. §1183(a).

Account for all property received.

Examine proofs of claim and object to improper filings.

Opposed the debtor's discharge, if advisable.

Furnish information concerning the estate if requested by a party in interest

Make a final report and account of the administration of the estate.

If the debtor is removed as debtor-in-possession (ie., fraud, dishonesty, incompetence, gross mismanagement), the trustee must file MORs, operate the business, and may enter into ordinary course transactions and obtain ordinary course unsecured credit or incur unsecured debts as an administrative expense. §1183(b)(5)

If the debtor is an individual and owes a DSO, the Trustee must provide notice to the person the DSO is owed to and the child support enforcement agency. §1183(b)(6)

The Trustee is required to appear at certain hearings:

60-day status conference.

Any hearing concerning the value of property subject to a lien.

Plan confirmation hearing.

Any hearing regarding modification of a plan.

Any hearing concerning the sale of property.

Plan Payments: The Trustee acts as a conduit for plan payments. The Trustee collects plan payments until confirmation. The Trustee must also ensure that the debtor commences payments under a confirmed plan. If the plan is consensual, the Trustee makes the initial distribution. If the plan is nonconsensual (all impaired classes do not vote in favor), the Trustee makes all payments under the plan. If the plan is not confirmed, the Trustee returns the payments made thus far to the debtor after deducting unpaid administrative claims, adequate protection payments to secure creditors and the Standing Trustee's fee. §1194(a). After notice and a hearing, the court may authorize the Trustee to make adequate protection payments to a secured creditor.

Term: If the plan is confirmed with consent of all impaired classes, the Trustee's term ends at confirmation. If the plan is not confirmed with consent of all impaired classes, the Trustee's term continues for the life of the plan unless the plan or confirmation order provides otherwise. §1194(b)

Fee: Hourly billing plus expenses as approved by the Court.

Discharge

The SBRA provides that a debt that is payable after the term of the plan (ie, long term secured debt) is not discharged. §1192

Business Loans Collateralized by Owner's Residence

The SBRA provides that the debtor may now modify the rights of a holder of a claim secured only by a security interest in real property that is the debtor's principal residence if the new value received in connection with the loan was not used primarily to acquire the real property and used primarily in connection with the small business of the debtor. §1190(3)

Administrative Expenses and "Gap" Period Claims Paid Through Plan

Normally §503(b) administrative expenses and "gap" period claims in an involuntary case must be paid in full on the effective date. The SBRA permits those claims to be paid over time through the plan. §1191(e)

The Plan Can be Modified After Confirmation

If circumstance warrant a modification after confirmation, after notice and a hearing the court may permit modification of the plan. The voters of claims in impaired classes may change their original vote within a period fixed by the court. §§ 1193(c), (d)

Disinterestedness

The distinterestedness standard is modified to permit a professional retained under §327(a) to have a claim of less than $10,000 against the debtor. §1195

Preference Actions

A broader change to all bankruptcy cases required the preference plaintiff to have undertaken "reasonable due diligence in the circumstances of the case" and "taking into account a party's known or reasonably knowable affirmative defenses". §547(b)

The $10,000 threshold is increased to $25,000 for actions that must be commenced in the jurisdiction where the defendant is located, not in the jurisdiction where the debtor's case is filed. §1409(b)

KeyCite Yellow Flag - Negative Treatment
Disagreed With by In re Denby-Peterson, 3rd Cir.(N.J.), October 28, 2019

719 F.3d 72
United States Court of Appeals,
Second Circuit.

In re Christopher WEBER, Debtor.
Christopher Weber, Plaintiff–Appellee,
v.
SEFCU, Defendant–Appellant,
Andrea E. Celli, Chapter 13 Trustee, Trustee.

Docket No. 12–1632–bk.
|
Argued: Dec. 4, 2012.
|
Decided: May 8, 2013.

Synopsis
Background: Upon finding that secured creditor violated the Bankruptcy Code's automatic stay provision, the United States District Court for the Northern District of New York, Suddaby, J., 477 B.R. 308, reversed an order of the United States Bankruptcy Court for the Northern District of New York, Littlefield, J., and remanded to the Bankruptcy Court for a determination regarding sanctions. Creditor appealed.

Holdings: The Court of Appeals, Susan L. Carney, Circuit Judge, held that:

[1] creditor's refusal to return the vehicle to debtor promptly upon learning of his Chapter 13 bankruptcy filing constituted an unlawful "exercise [of] control" over the "property" of his estate in violation of the automatic stay, and

[2] because secured creditor intended to retain debtor's repossessed vehicle upon learning of debtor's bankruptcy filing, creditor "willfully" violated automatic stay.

Affirmed and remanded.

Procedural Posture(s): On Appeal.

West Headnotes (6)

[1] **Bankruptcy**⇐Conclusions of law; de novo review

Court of Appeals conducts a plenary review of a decision of a district court functioning in its capacity as an appellate court in a bankruptcy case, and thus, reviews de novo the bankruptcy court's legal conclusions.

6 Cases that cite this headnote

[2] **Bankruptcy**⇐Repossession

Although secured creditor's repossession of debtor's vehicle before debtor filed his Chapter 13 petition lawfully overrode debtor's immediate possessory rights, the parties agreed that New York law afforded debtor at least a continuing equitable interest in the vehicle; therefore, creditor's refusal to return the vehicle to debtor promptly upon learning of his Chapter 13 bankruptcy filing constituted an unlawful "exercise [of] control" over the "property" of his estate in violation of the automatic stay. 11 U.S.C.A. §§ 362, 541, 542.

15 Cases that cite this headnote

[3] **Bankruptcy**⇐Enforcement of Injunction or Stay

Bankruptcy Code's automatic stay provision requires a creditor in possession of property seized as security, but subject to a state-law-based residual equitable interest in the debtor, to deliver that property to the trustee or debtor-in-possession promptly after the debtor has filed a petition in bankruptcy under Chapter 13. 11 U.S.C.A. § 362.

14 Cases that cite this headnote

[4] **Bankruptcy**⇐Repossession

Secured creditor's belief that Chapter 13 debtor had not provided "adequate protection" for creditor's security interest in debtor's vehicle did not excuse creditor's violation of automatic stay by failing to surrender repossessed vehicle promptly upon learning of debtor's Chapter 13 bankruptcy filing. 11 U.S.C.A. §§ 362, 542.

9 Cases that cite this headnote

[5] **Bankruptcy**⇐Enforcement of Injunction or Stay

A creditor "willfully" violates Bankruptcy Code's automatic stay provision when it knows of the filing of the petition and hence of the automatic stay, and has the general intent simply to perform the act found to violate the stay; no specific intent to violate the stay is necessary. 11 U.S.C.A. § 362.

13 Cases that cite this headnote

[6] **Bankruptcy**⇐Damages and attorney fees

Because secured creditor intended to retain debtor's repossessed vehicle upon learning of debtor's Chapter 13 bankruptcy filing, creditor "willfully" violated automatic stay provision, and was thus liable for damages, costs, and attorney fees. 11 U.S.C.A. § 362(h, k).

16 Cases that cite this headnote

Attorneys and Law Firms

*73 Gary A. Lefkowitz (William B. Schiller, on the brief), Schiller & Knapp, LLP, Latham, NY, for Defendant–Appellant.

Richard Croak, Albany, NY, for Plaintiff–Appellee.

Tara Twomey (Ray DiGuiseppe, on the brief), National Consumer Bankruptcy Rights Center, San Jose, CA, for amicus curiae National Association of Consumer Bankruptcy Attorneys, in support of Plaintiff–Appellee.

Before: CABRANES, RAGGI, and CARNEY, Circuit Judges.

Opinion

SUSAN L. CARNEY, Circuit Judge:

Defendant SEFCU, a lender, appeals from a judgment of the United States District Court for the Northern District of New York (Suddaby, *J.*) reversing an order of the United States Bankruptcy Court for the Northern District of New York (Littlefield, *J.*) and remanding the case to the Bankruptcy Court for further proceedings. The District Court concluded that SEFCU violated the automatic stay provision of the Bankruptcy Code, 11 U.S.C. § 362, when, after lawfully repossessing a vehicle belonging to the debtor, plaintiff Christopher Weber, it failed to deliver the vehicle to him notwithstanding its knowledge of the debtor's pending petition under Chapter 13 of the Bankruptcy Code. The District Court affirmed, holding that, by declining to surrender the vehicle absent a turnover order and protection SEFCU considered adequate, the lender wrongfully "exercised control" over the vehicle in contravention of section 362 and *74 was liable for Weber's related damages, attorneys' fees, and costs.

On appeal to our Court, SEFCU challenges the District Court's interpretation of section 362 and other relevant provisions of the Bankruptcy Code, and argues that, under the authority of *Manufacturers & Traders Trust Co. v. Alberto (In re Alberto),* 271 B.R. 223 (N.D.N.Y.2001), it was entitled to retain the vehicle notwithstanding the pending bankruptcy proceedings. For the reasons set forth below, we AFFIRM the judgment of the District Court and REMAND the cause to the district court for a determination of the amount of damages, costs, and attorneys' fees that SEFCU owes Weber under section 362(k), and any other proceedings consistent with this opinion.

BACKGROUND

The relevant facts are undisputed.[1]

In August 2006, Weber and SEFCU (identified in Bankruptcy Court pleadings as the "State Employees Federal Credit Union")[2] entered into a loan agreement pursuant to which SEFCU obtained a security interest in Weber's vehicle, a pickup truck. The loan agreement entitled SEFCU to repossess Weber's vehicle upon default.

In 2009, SEFCU became entitled to proceed against Weber. As a result, on January 10, 2010, SEFCU took possession of Weber's vehicle pursuant to the loan agreement, and, by notices dated January 10 and 11, 2010, advised him of his right under New York law to redeem the vehicle upon payment of amounts due and certain costs. Four days after the seizure, on January 14, Weber filed a voluntary petition for relief under Chapter 13 of the Bankruptcy Code, 11 U.S.C. §§ 109(e), 1301–08, 1321–30, in the United States Bankruptcy Court for the Northern District of New York. Weber's attorney concurrently gave SEFCU written notice of Weber's bankruptcy filing, and, invoking the stay imposed by Bankruptcy Code section 362, 11 U.S.C. § 362(a), requested the vehicle's return.

One week later, SEFCU still had the vehicle, and accordingly, on January 22, Weber filed an adversary proceeding against SEFCU seeking its return so that, as later explained by his counsel to the Bankruptcy Court, he could "continue his construction business" during the pendency of his petition. On March 1, with the vehicle still in SEFCU's possession, the Bankruptcy Court entered an order requiring SEFCU to show cause why it should not return the vehicle and why the court should not grant Weber an award of damages for SEFCU's violation of section 362 and for other relief. On March 4, the court heard argument on the order to show cause, and, although the record does not reflect entry of a related order at that time, SEFCU is reported to have returned the vehicle to Weber the following day.

The proceedings in the Bankruptcy Court continued, as Weber sought damages for his inability to use the vehicle between January 14 and March 5, attorneys' fees, and sanctions. In November 2010, SEFCU moved for summary judgment, *75 putting to the Bankruptcy Court the question of law whether SEFCU's failure to release the vehicle promptly after the petition was filed constituted a "willful" violation of the automatic stay under subsections (a) and (k)(1) of section 362 (providing for recovery of damages, costs, and attorneys' fees for "any willful violation of a stay"). SEFCU maintained that there was no violation, and that an earlier district court decision in other proceedings, *Alberto,* 271 B.R. 223 (N.D.N.Y.2001), gave it a reasonable basis for declining to release the vehicle absent a court order issued pursuant to Bankruptcy Code section 542, 11 U.S.C. § 542 (relating to "Turnover of property to the estate"). Weber, for his part, argued that *Alberto* was wrongly decided, and that section 362 required SEFCU to release the vehicle promptly after the petition was filed. The Bankruptcy Court, in a brief Order, granted summary judgment for SEFCU.

Weber appealed to the District Court. Relying primarily on the Supreme Court's decision in *United States v. Whiting Pools, Inc.,* 462 U.S. 198, 103 S.Ct. 2309, 76 L.Ed.2d 515 (1983), and rejecting the reasoning of the *Alberto* court, the district court concluded that SEFCU was bound to release the vehicle to Weber, the debtor-in-possession, upon learning of Weber's pending Chapter 13 proceedings. The district court further determined that, having failed to do so, SEFCU violated section 362. Because it knew of the petition and retained the vehicle, SEFCU's violation was willful, making it liable for damages and attorneys' fees. *Weber v. SEFCU,* 477 B.R. 308, 311 (N.D.N.Y.2012). SEFCU timely appealed.

DISCUSSION

[1] We conduct a "plenary review" of a decision of "a district court functioning in its capacity as an appellate court in a bankruptcy case." *Mazzeo v. United States (In re Mazzeo),* 131 F.3d 295, 301 (2d Cir.1997). Thus, we review *de novo* the bankruptcy court's legal conclusions. *Resolution Trust Corp. v. Best Prods. Co. (In re Best Prods. Co.),* 68 F.3d 26, 29 (2d Cir.1995). As noted above, the relevant facts are not contested; we have no occasion to subject them to further review.

Under Bankruptcy Code section 541, governing "Property of the estate," the act of filing a petition for

bankruptcy creates an estate comprised of (as relevant here) "all legal or equitable interests of the debtor in property as of the commencement of the [bankruptcy] case." 11 U.S.C. § 541(a)(1). Section 541 gathers into the estate all such interests in property, "wherever located and by whomever held." *Id.* § 541(a).

To assemble the bankruptcy estate, section 542 of the Code requires that, during bankruptcy proceedings, an entity "in possession, custody, or control" of certain property in the estate "*shall deliver* " that property to the trustee, "unless such property is of inconsequential value or benefit to the estate." 11 U.S.C. § 542(a) (emphasis added). The property subject to this delivery obligation is "property that the trustee may use, sell, or lease under section 363," which grants broad powers over the estate's property to the trustee.[3] *Id.* ***76** In a Chapter 13 bankruptcy, the debtor "remain [s] in possession of all property of the estate"—acting in effect as trustee under section 542(a)—unless the debtor's reorganization plan provides otherwise. 11 U.S.C. § 1306(b).[4] The delivery obligation of section 542(a) thus contemplates the debtor-in-possession as the recipient of the property of the estate.

While bankruptcy proceedings are pending, the automatic stay provisions of section 362 work with sections 541 and 542 to shelter the debtor's estate from action by creditors, enabling the debtor to get the relief and fresh start that are among the goals of the bankruptcy regime.[5] Thus, under section 362, filing a bankruptcy petition automatically effects a stay of "any act to obtain possession of property of the estate ... or to exercise control over property of the estate." 11 U.S.C. § 362(a)(3). Those who violate section 362 are liable for related damages and costs: under section 362(k), a debtor "injured by any willful violation of a stay provided by [section 362] *shall recover* actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages." *Id.* § 362(k)(1) (emphasis added).

We first consider whether SEFCU's refusal to return the vehicle to Weber promptly upon learning of his Chapter 13 bankruptcy filing constituted an unlawful "exercise [of] control" over the "property" of his estate, in violation of the automatic stay. We then examine whether SEFCU may be excused from promptly surrendering the vehicle because Weber had not provided "adequate protection" for SEFCU's security interest in the vehicle. Finally, because we conclude that SEFCU's actions did violate section 362, we then turn to the question whether, in light of its reliance on *Alberto,* SEFCU's violation was nonetheless "willful" under section 362(k), making it liable for Weber's actual damages, costs, and attorneys' fees under that section.

I.

[2] As observed above, section 541(a) provides that a bankruptcy estate is comprised of "all legal or equitable interests in property as of the commencement of the case."[6] Although SEFCU's repossession ***77** of the vehicle before Weber filed his petition lawfully overrode Weber's immediate possessory rights, the parties agree that New York law afforded Weber at least a continuing equitable interest in the vehicle. *See Wornick v. Gaffney,* 544 F.3d 486, 490 (2d Cir.2008) ("Whether the debtor has a legal or equitable interest in property such that it becomes property of the estate under section 541 is determined by applicable state law." (internal quotation marks omitted)). That interest arose from Weber's right pursuant to the state Uniform Commercial Code to redeem the vehicle before sale. *See* N.Y. U.C.C. § 9–623.[7] It was this right that SEFCU acknowledged and identified for Weber in its notice to him dated January 11. Weber's equitable interest thus constituted "property" of the bankruptcy estate under section 541. Neither party seriously challenges the scope of that definition.

Rather, Weber and SEFCU dispute whether, by failing to surrender the vehicle immediately upon receiving notice of the petition's filing, SEFCU "exercise[d] control" over Weber's equitable interest in the vehicle and thereby violated the stay imposed by section 362. The Supreme Court's decision in *United States v. Whiting Pools, Inc.,* 462 U.S. 198, 103 S.Ct. 2309, 76 L.Ed.2d 515 (1983), provides important guidance for our resolution of this issue.

The dispute in *Whiting Pools* arose when, to satisfy a tax lien, the IRS seized all of the tangible personal property of the corporation. One day after the seizure, the corporation filed for bankruptcy. The IRS moved for relief from the automatic stay, wishing to be free to sell the personal property that it had seized in satisfaction of the tax debts owed. The debtor corporation counterclaimed and, in the bankruptcy court, successfully sought an order under section 542 that required the IRS to

return the property to the estate. *Id.* at 199–201, 103 S.Ct. 2309.

The Supreme Court affirmed the bankruptcy court's turnover order. Characterizing the IRS's interest in the seized property as "its lien"—not ownership—and analogizing the Service's right to effect a seizure to the remedies available to private secured creditors, the Court described the seizure as "not determin[ing] the Service's rights to the seized property, but merely bring[ing] the property into the Service's legal custody." *Id.* at 210–11, 103 S.Ct. 2309. It explained that "[i]n effect, § 542(a) grants to the estate a possessory interest in certain property of the debtor that was not held by the debtor at the commencement of reorganization proceedings," *id.* at 207, 103 S.Ct. 2309, and "requires an entity ... holding any property of the debtor that the trustee can use ***78** under § 363 to turn that property over to the trustee." *Id.* at 205–06, 103 S.Ct. 2309.

The Court underscored the Congressional intent, in shaping the definition of "property" set forth in section 541(a), to include "a broad range" of property in the estate, and indeed, to capture "any property made available to the estate by other provisions of the Bankruptcy Code." *Id.* at 204–05, 103 S.Ct. 2309. Section 542(a) is such a provision. It requires delivery to the trustee of "any property of the debtor that the trustee can use under § 363," including property repossessed by a secured creditor. *Id.* at 205–06, 103 S.Ct. 2309. "Any other interpretation of § 542(a)," the Court declared, "would deprive the bankruptcy estate of the assets and property essential to its rehabilitation effort and thereby would frustrate the congressional purpose behind the reorganization provisions." *Id.* at 208, 103 S.Ct. 2309.

For these reasons, the Court restricted the IRS—like any other creditor seizing property in which it held a security interest—to seeking protection of its interests "according to the congressionally established bankruptcy procedures, rather than by withholding the seized property from the debtor's efforts to reorganize." *Id.* at 212, 103 S.Ct. 2309.

Similarly, here, SEFCU seized Weber's vehicle before Weber filed for bankruptcy, but under New York law, Weber retained at least an equitable interest in the property notwithstanding its repossession. SEFCU did not automatically obtain an ownership interest in the vehicle: its rights to seize and sell were subject to U.C.C. provisions of state law, including certain continuing rights held by Weber, and also subject to the rights and remedies established by the Bankruptcy Code. *Whiting Pools* teaches that, upon Weber's filing of his bankruptcy petition, Weber's equitable interest under state law gave the bankruptcy estate a possessory right in the secured property, as property that the trustee could use under section 363. Under section 542, that right took precedence over the state law possessory right of SEFCU. *See id.* at 207, 103 S.Ct. 2309.

It is true that *Whiting Pools* involved a Chapter 11 corporate reorganization, and that the Supreme Court expressly reserved judgment as to whether its analysis would also apply to Chapter 13 personal reorganizations like Weber's. 462 U.S. at 208 n. 17, 103 S.Ct. 2309. But, like other courts to have addressed the issue, we observe that the language of sections 541, 542, and 362 applies to the "estate," not just the "reorganization estate." *See Austein v. Schwartz (In re Gerwer),* 898 F.2d 730, 734 (9th Cir.1990) (cited in *In re Velichko,* 473 B.R. 64, 67 (Bankr.S.D.N.Y.2012)). We see no reason—and the parties have presented none—to restrict application of the reasoning of the *Whiting Pools* Court to corporate reorganizations: the same concerns apply fully in the Chapter 13 context as well. *See, e.g., Thompson v. General Motors Acceptance Corp.,* 566 F.3d 699, 705–06 (7th Cir.2009) (applying *Whiting Pools* in Chapter 13 setting and observing that the "purpose of reorganization bankruptcy, *be it corporate or personal,* is to allow the debtor to regain his financial foothold and repay his creditors") (emphasis added). As noted above, Weber required his vehicle to conduct his construction business; Whiting Pools required its equipment and other personal property to conduct its business. In each case, the reorganization's chances for success would seem markedly improved if operations could be maintained during the pendency of the petition and formulation of the plan.

Whiting Pools does not resolve, however, whether by demanding a turnover order of the bankruptcy court or "adequate ***79** protection" as a condition of its relinquishment, SEFCU "exercise[d] control" over the vehicle in contravention of the stay. In *Whiting Pools,* the IRS—unlike SEFCU—moved for relief from the stay, and did not simply wait for the debtor to initiate an adversary proceeding or seek a turnover order under section 542. *Id.* at 201, 103 S.Ct. 2309. Thus, the Court there held only that the bankruptcy court properly ordered the IRS to return the seized property to the estate

under section 542. *Id.* at 212, 103 S.Ct. 2309.

The district court's decision in *Alberto,* relied upon by SEFCU here, directly addressed the question left unanswered by *Whiting Pools.* The *Alberto* court concluded that a secured creditor did *not* violate the automatic stay when, after learning of the debtor's bankruptcy, it failed immediately to return a debtor's repossessed vehicle. 271 B.R. at 228. Rather, the court held that before such a secured creditor was obligated to surrender the collateral to the estate, the debtor must "take[ ] an affirmative step," such as obtaining a turnover order under section 542. *Id.* at 227. Because (as it found) a repossessed vehicle was not part of the debtor's estate until such an action had occurred, the court reasoned that a creditor that had taken possession of its security did not "exercise control" over "property" of the estate by declining to surrender the possessory interest to the estate. *Id.* at 228. Since the debtor no longer had a possessory interest, the court concluded, the creditor "did not 'act to obtain possession ... or to exercise control' of the vehicle in violation of the stay, since it already lawfully possessed and controlled the vehicle when the stay went into effect." *Id.* at 226 (alteration in original) (quoting 11 U.S.C. § 362(a)(3)).

We find the *Alberto* court's reasoning unpersuasive. Section 541 expressly provides that the "property" of Weber's estate includes equitable interests, and Weber's right to redeem and other rights catalogued above, together with his lingering claim to ownership of title, comprise such an interest. That SEFCU had already effected a repossession does not alter the conclusion that the equitable interest is property of the estate: section 541 provides further that the estate is comprised of property "wherever located and by whomever held." 11 U.S.C. § 541(a). Nor was Weber obligated to initiate an additional proceeding. Section 542 requires that any entity in possession of property of the estate deliver it to the trustees, without condition or any further action: the provision is "self-executing." *Collier on Bankruptcy* § 542.02 (16th ed. 2012) ("By its express terms, [section 542] is self-executing, and does not require that the trustee take any action or commence a proceeding or obtain a court order to compel the turnover."). And *Whiting Pools* teaches that the filing of a petition will generally transform a debtor's equitable interest into a bankruptcy estate's possessory right in the vehicle.

[3] As for whether SEFCU's refusal to return the vehicle to the estate violated the stay, section 362 forbids any act to "obtain possession" or "exercise control" over the property of the estate. We need consult only an ordinary dictionary to confirm that a typical definition of "control" is: "To exercise authority over; direct; command." Webster's New World College Dictionary (4th ed. 2002). In light of that definition, we see no way to avoid the conclusion that, by keeping custody of the vehicle and refusing Weber access to or use of it, SEFCU was "exercising control" over the object in which the estate's equitable interest lay, and its retention of the vehicle violated the stay.

*80 The Bankruptcy Amendments and Federal Judgeship Act of 1984 (the "1984 Amendments") confirms our conclusion. The 1984 Amendments, passed after the *Whiting Pools* decision in 1983, broadened the already sweeping provisions of the automatic stay even further to prohibit expressly not only "acts to obtain possession" of property of the estate, but also "any act ... to exercise control over the property of the estate." Pub. L. No. 98–353, 98 Stat. 333, 371. This significant textual enlargement is consonant with our understanding and the Supreme Court's interpretation that Congress intended to prevent creditors from retaining property of the debtor in derogation of the bankruptcy procedure and the broad goals of debtor protection discussed above, without regard to what party was in possession of the property in question when the petition was filed. As the Seventh Circuit has pointed out, "Although Congress did not provide an explanation of that amendment, the mere fact that Congress expanded the provision to prohibit conduct above and beyond obtaining possession of an asset suggests that it intended to include conduct by creditors who seized an asset pre-petition." *Thompson,* 566 F.3d at 702 (citation omitted).

The rule adopted by the *Alberto* court and urged on us by SEFCU—that some additional act by the debtor is required before the creditor is obligated to surrender the property—would, in contrast, place on the debtor or trustee the burden of undertaking a series of adversary proceedings to pull together the bankruptcy estate, and thereby increase the costs of administering the estate and decrease the assets available to effect a successful reorganization. In our view, the plain language of section 542 (directing that those in custody of assets of the estate "shall deliver" them to the trustee); the approach of the *Whiting Pools* Court to equitable interests and bankruptcy estates; and the broad language of the 1984 Amendments enlarging the scope of the automatic stay point unmistakably away from any Congressional desire to impose such an additional burden on debtors seeking

bankruptcy protection. As the Eighth Circuit wrote,

> [I]f persons who could make no substantial adverse claim to a debtor's property in their possession could, without cost to themselves, compel the debtor or his trustee to bring suit as a prerequisite to returning the property, the powers of a bankruptcy court ... to collect the estate for the benefit of creditors would be vastly reduced.

Knaus v. Concordia Lumber Co. (In re Knaus), 889 F.2d 773, 775 (8th Cir.1989) (internal quotation marks omitted). SEFCU has identified no basis for concluding that Congress intended this result.

The district court's decision in *Alberto* also runs counter to the strong trend of decisions from our sister Circuits. For example, the Seventh Circuit has bluntly ruled that "a plain reading of the Bankruptcy Code's provisions, the Supreme Court's decision in [*Whiting Pools*], and various practical considerations require that a creditor immediately return a seized asset in which a debtor has an equity interest to the debtor's estate upon his filing of Chapter 13 bankruptcy." *Thompson,* 566 F.3d at 700; *see also* *Knaus,* 889 F.2d at 775. Bankruptcy Appellate Panels from other Circuits agree. *E.g.,* *Unified People's Fed. Credit Union v. Yates (In re Yates),* 332 B.R. 1, 7 (10th Cir. BAP 2005); *TranSouth Fin. Corp. v. Sharon (In re Sharon),* 234 B.R. 676, 682 (6th Cir. BAP 1999); *Abrams v. Sw. Leasing & Rental Inc. (In re Abrams),* 127 B.R. 239, 243 (9th Cir. BAP 1991).

*81 Only the Eleventh Circuit has adopted a contrary approach, and those decisions have largely relied on readings of state law with regard to the relative legal property interests of debtor and secured creditor after a lawful repossession. *See* *Bell–Tel Fed. Credit Union v. Kalter (In re Kalter),* 292 F.3d 1350, 1356–60 (11th Cir.2002) (applying Florida law); *Charles R. Hall Motors, Inc. v. Lewis (In re Lewis),* 137 F.3d 1280, 1284–85 (11th Cir.1998) (applying Alabama law).

In our view, the majority rule adheres more faithfully to the text of the Bankruptcy Code and the reasoning of *Whiting Pools.* In addition, sound policy supports the majority's reading of the statutory text:

> The primary goal of reorganization bankruptcy is to group *all* of the debtor's property together in his estate such that he may rehabilitate his credit and pay off his debts; this necessarily extends to all property, even property lawfully seized pre-petition. An asset actively used by a debtor serves a greater purpose to both the debtor and his creditors than an asset sitting idle on a creditor's lot.

Thompson, 566 F.3d at 702 (citations omitted) (emphasis in original).

We therefore join the majority of other Circuits to have addressed this issue and conclude that section 362 requires a creditor in possession of property seized as security—but subject to a state-law-based residual equitable interest in the debtor—to deliver that property to the trustee or debtor-in-possession promptly after the debtor has filed a petition in bankruptcy under Chapter 13.

II.

[4] SEFCU argues that even if the Code did not permit SEFCU to await a turnover order before relinquishing the vehicle, SEFCU was entitled to withhold the vehicle until Weber offered or the court ordered Weber to provide SEFCU "adequate protection" for SEFCU's security interest. Appellant's Br. 15. We need not pause long over this argument, for the plain text of the Bankruptcy Code contradicts this position. As we have observed, section 542(a) provides without qualification that anyone in possession of the property of the estate "shall deliver" it to the trustee. 11 U.S.C. § 542(a). The Code requires the creditor first to surrender the property. Only then or in conjunction with that surrender may it proceed to "request" from the Bankruptcy Court "adequate protection" for its interests. 11 U.S.C. §§ 362(d),

363(e).[8] The provisions authorizing imposition of such protection operate only upon application of the creditor to the Bankruptcy Court. Unlike section 542(a), these are not self-executing.

SEFCU points to no provision of the Code permitting a creditor to withhold property of the estate until the debtor has offered protection that is "adequate" in the *creditor's* view, separate from any formal proceeding before the Bankruptcy Court. Rather, the Code provides for protection ***82** that the *court* deems adequate: "[O]n request of an entity that has an interest in property used ... by the trustee, the court ... shall prohibit or condition such use ... as is necessary to provide adequate protection of such interest." 11 U.S.C. § 363(e). *See Sharon,* 234 B.R. at 683 (holding that "[t]here is no 'exception' ... that excuses [the creditor's] refusal to deliver possession of the Debtor's car based on [the creditor's] subjective opinion that adequate protection offered by the Debtor was not 'adequate' "). To hold otherwise would permit a creditor holding the debtor's property at the time of the debtor's bankruptcy filing to "negotiat[e] a better security package" than other creditors, thereby ensuring that creditor "a position above other secured creditors" and circumventing the bankruptcy court's authority to approve the debtor's plan to repay his or her debts. *Thompson,* 566 F.3d at 707.

SEFCU points principally to the Fourth Circuit's decision in *Tidewater Finance Co. v. Moffett (In re Moffett),* 356 F.3d 518 (4th Cir.2004), in support of the proposition that a secured creditor may await delivery of what it deems adequate protection before surrendering the debtor's property to the estate. But *Moffett* is inapposite. That case did not concern the creditor's assessment of whether the debtor's proffered protection was "adequate." Rather, there, the creditor moved in the bankruptcy court for relief from the stay, seeking permission to sell the previously repossessed vehicle. *Id.* at 520. The Fourth Circuit agreed with the bankruptcy court that the debtor's reorganization plan provided "adequate protection" to the creditor and declined to lift the stay, requiring the creditor to return the vehicle to the debtor. *Id.* at 523.

We easily conclude that SEFCU's belief that Weber had not provided "adequate protection" for SEFCU's security interest in the vehicle does not cure SEFCU's violation of section 362.

III.

Finally, SEFCU asserts that even if its actions violated section 362, its violation was not "willful" within the meaning of section 362(k), and therefore the court may not require it to pay Weber's damages, costs, or attorneys' fees, or to impose any sanction. SEFCU asserts primarily that, because it relied in good faith on the *Alberto* decision and the "rule and custom" of the Northern District of New York, any violation that it committed should not be deemed "willful" under section 362(k). Appellant's Br. at 3.

We appreciate that, since one district court rendered its decision in *Alberto,* a practice may have developed in the Northern District of New York under which creditors felt entitled to await a turnover order and that SEFCU may therefore have felt justified in failing to surrender Weber's vehicle absent a court order. Nothing prevented SEFCU from surrendering the vehicle in response to Weber's request, however: it always was free to do so, and free concurrently to move the Bankruptcy Court for entry of an order that would—in the *court's* view—provide "adequate protection" to SEFCU. The creditor's error in this regard does not justify placing costs related to the vehicle's retention on the debtor.

[5] [6] Indeed, SEFCU misconstrues the meaning of "willful" as our Circuit law has construed the term in the context of section 362. A creditor willfully violates section 362 when it knows of the filing of the petition (and hence of the automatic stay), and has the general intent simply to perform the act found to violate section 362; no specific intent to violate section 362 is necessary. As we wrote over twenty years ago, "any deliberate act taken in ***83** violation of a stay, which the violator knows to be in existence, justifies an award of actual damages." *Crysen/Montenay Energy Co. v. Esselen Assocs., Inc. (In re Crysen/Montenay Energy Co.),* 902 F.2d 1098, 1105 (2d Cir.1990); *see also In re Dominguez,* 312 B.R. 499, 508 (Bankr.S.D.N.Y.2004) ("[S]o long as the violator possessed general intent in taking actions which have the effect of violating the automatic stay the intent required by § 362(h) is satisfied."); *Yates,* 332 B.R. at 7 ("Whether the party believes in good faith that it had a right to the property is not relevant to whether the act was willful or whether compensation must be awarded." (internal quotation marks omitted)). Section 362(k) operates to compensate the debtor who has been injured by the violation, in line with the distribution of the procedural

burden struck by the statute, as discussed above, in favor of the estate and the bankruptcy mechanism. Because it intended to retain Weber's vehicle, SEFCU acted "willfully," and is liable for damages, costs, and attorney's fees under section 362(k)(1).

Although its good faith is insufficient to excuse SEFCU from liability for Weber's actual damages, it may prevent the imposition of punitive damages, which in any event Weber's counsel has conceded he no longer seeks.[9] *See Crysen/Montenay Energy Co.,* 902 F.2d at 1105 ("An additional finding of maliciousness or bad faith on the part of the offending creditor warrants the further imposition of punitive damages...."); *see also In re Velichko,* 473 B.R. at 69–70 (imposition of punitive damages premised on finding that secured creditor acted in bad faith by forcing debtors to sign reaffirmation agreement before relinquishing their vehicle).

CONCLUSION

For the foregoing reasons, we conclude that by failing to deliver the repossessed vehicle to the debtor-in-possession promptly after receiving notice of the pending petition, SEFCU willfully violated section 362(a), and is liable under section 362(k) for Weber's actual damages, costs, and attorney's fees. The order of the district court is AFFIRMED, and the cause remanded to the district court for further proceedings consistent with this opinion. The district court may, if it chooses, remand the cause to the bankruptcy court for adjudication of the remaining issues, including Weber's costs.

All Citations

719 F.3d 72, 69 Collier Bankr.Cas.2d 1168, Bankr. L. Rep. P 82,484

Footnotes

1 In proceedings before the Bankruptcy Court, the parties submitted a "Combined statement of facts not subject to material dispute," pursuant to Local Rule 7056 of the Bankruptcy Court for the Northern District of New York. We draw the facts presented here from that statement.

2 According to The Daily Gazette, which covers Schenectady and Albany, the State Employees Federal Credit Union officially changed its name to "SEFCU" in 1990. Lee Coleman, *Credit Unions Going Strong in Region,* The Daily Gazette, Apr. 29, 2012, at B1.

3 Section 363, as applicable here, provides: "[U]nless the court orders otherwise, the trustee may enter into transactions, including the sale or lease of property of the estate, in the ordinary course of business, without notice or a hearing, and may use property of the estate in the ordinary course of business without notice or a hearing." 11 U.S.C. § 363(c)(1); *see also United States v. Whiting Pools, Inc.,* 674 F.2d 144, 149 (2d Cir.1982) (Friendly, *J.*), *aff'd,* 462 U.S. 198, 103 S.Ct. 2309, 76 L.Ed.2d 515 (1983). The trustee may also use, sell, or lease property of the estate outside the ordinary course of business, upon notice and a hearing before the bankruptcy court. 11 U.S.C. § 363(b)(1); *see also Motorola, Inc. v. Official Comm. of Unsecured Creditors and JPMorgan Chase Bank, N.A. (In re Iridium Operating LLC),* 478 F.3d 452, 466 (2d Cir.2007).

4 The debtor-in-possession may exercise many of the rights and powers of a bankruptcy trustee, including the right to use, sell, or lease property of the estate. 11 U.S.C. §§ 1303, 1304(b) ("Unless the court orders otherwise, a debtor engaged in business may operate the business of the debtor and, subject to any limitations on a trustee under sections 363(c) and 364 of this title and to such limitations or conditions as the court prescribes, shall have, exclusive of the trustee, the rights and powers of the trustee under such sections.").

5 The iconic description of the overriding purpose of section 362 is drawn directly from the section's legislative history:

> The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy.

H.R.Rep. No. 95–595, at 340–41 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6296–97; *see also United States v. Colasuonno,* 697 F.3d 164, 172 (2d Cir.2012).

6 In relevant part, section 541 provides:

> (a) The commencement of a case under [11 U.S.C. §§ 301, 302, or 303] creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:
>
> (1) [Subject to exceptions not relevant here,] all legal or equitable interests of the debtor in property as of the commencement of the case.

7 Weber retained other rights under state law consistent with his status as the equitable owner of the vehicle. These rights included a right to notification before the creditor disposed of the vehicle, N.Y. U.C.C. § 9–611, and a right to receive any surplus from the sale of the vehicle, *id.* § 9–615(d)(1). In addition, we observe that Weber may have retained legal title to the vehicle. *See, e.g.,* N.Y. U.C.C. § 9–609; N.Y. Veh. & Traf. Law § 2115. But the parties have not briefed this question and we do not decide it here. That Weber has a colorable claim to have retained legal title to the truck, in addition to his acknowledged equitable interests in the vehicle, arguably serves to distinguish this case, however, from those in which legal title transferred to the creditor automatically upon repossession (or never was in the debtor to begin with). We express no view about the bearing of section 362 upon the latter situations.

8 In relevant part, section 362(d) 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.

In relevant part, section 363(e) provides:

> Notwithstanding any other provision of this section, at any time, on request of an entity that has an interest in property used, sold, or leased ... by the trustee, the court, with or without a hearing, shall prohibit or condition such use, sale or lease as is necessary to provide adequate protection of such interest.

9 At oral argument, Weber's counsel confirmed that Weber does not seek punitive damages.

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KeyCite Yellow Flag - Negative Treatment
Certiorari Granted by City of Chicago, Illinois v. Fulton, U.S., December 18, 2019

926 F.3d 916
United States Court of Appeals, Seventh Circuit.

IN RE: Robbin L. FULTON, Debtor-Appellee.
Appeal of: City of Chicago
In re: Jason S. Howard, Debtor-Appellee.
Appeal of: City of Chicago
In re: George Peake, Debtor-Appellee.
Appeal of: City of Chicago
In re: Timothy Shannon, Debtor-Appellee.
Appeal of: City of Chicago

No. 18-2527, No. 18-2793, No. 18-2835, No. 18-3023
|
Argued May 14, 2019
|
Decided June 19, 2019

Synopsis
Background: Bankruptcy court issued rule to show cause why city should not be sanctioned for refusing to release Chapter 13 debtor's vehicle, which had been impounded because of unpaid parking tickets. The United States Bankruptcy Court for the Northern District of Illinois, Jacqueline P. Cox, J., 584 B.R. 252, entered judgment in favor of debtor, and city appealed. In separate Chapter 13 case, debtor moved to enforce automatic stay by requiring city to release vehicle, and the United States Bankruptcy Court for the Northern District of Illinois, Deborah Lee Thorne, J., 588 B.R. 811, granted motion. City appealed. In yet another case, debtor again filed motion to enforce stay against city, which motion was granted by the United States Bankruptcy Court for the Northern District of Illinois, Carol A. Doyle, J., 590 B.R. 467, and city appealed. Finally, city appealed from a grant of like relief by the United States Bankruptcy Court for the Northern District of Illinois, Jack B. Schmetterer, J., 2018 WL 2570109, and city appealed.

Holdings: Consolidating cases for purposes of appeal, the Court of Appeals, Flaum, Circuit Judge, held that:

[1] city violated stay by its continued postpetition retention of motor vehicles impounded prepetition;

[2] stay exception for "any act to perfect, or to maintain or continue the perfection of, an interest in property" did not permit city to continue to retain possession of motor vehicles; and

[3] "police or regulatory power" exception to automatic stay did not apply.

Affirmed.

Procedural Posture(s): On Appeal; Motion to Enforce Automatic Stay.

West Headnotes (21)

[1] **Bankruptcy**⇐Moot questions

Issues relating to creditor's alleged violation of automatic stay are not mooted by dismissal of underlying bankruptcy case. 11 U.S.C.A. § 362(a).

[2] **Bankruptcy**⇐Sanctions, in general

Court must have the power to compensate victims for violations of automatic stay and to punish the violators, even after conclusion of underlying bankruptcy case. 11 U.S.C.A. § 362(a).

[3] **Bankruptcy**⇐Conclusions of law; de novo review
Bankruptcy⇐Clear error

On appeal in bankruptcy case, the Court of Appeals reviews bankruptcy court's factual findings for clear error and its conclusions of law de novo. Fed. R. Bankr. P. 8013.

[4] **Bankruptcy**⇐Repossession

Creditor "exercises control" over property of the estate in violation of automatic stay when, subsequent to filing of bankruptcy petition, creditor refuses to return property of debtor that it has repossessed prepetition. 11 U.S.C.A. § 362(a)(3).

7 Cases that cite this headnote

[5] **Bankruptcy**⇐Notice to creditors; commencement

Stay provision that bars creditor from exercising control over property of the estate becomes effective immediately upon filing bankruptcy petition and is not dependent upon the debtor first bringing a turnover action. 11 U.S.C.A. §§ 362(a)(3), 542.

1 Cases that cite this headnote

[6] **Bankruptcy**⇐Repossession

Creditor that has repossessed debtor's motor vehicle prepetition is required to turn over such property of the estate following commencement of debtor's bankruptcy case, prior to a court determination establishing debtor's obligation to provide adequate protection for creditor's interest in vehicle. 11 U.S.C.A. §§ 362(a)(3), 542.

2 Cases that cite this headnote

[7] **Bankruptcy**⇐Collection and Recovery for Estate; Turnover

Turnover of estate property by creditor in possession thereof is compulsory. 11 U.S.C.A. § 542(a).

2 Cases that cite this headnote

[8] **Bankruptcy**⇐Acts excepted from stay

City which, prior to commencement of debtors' Chapter 13 cases, had impounded motor vehicles belonging to debtors based on their unpaid parking and moving tickets improperly exercised control over property of the estate, in violation of automatic stay, by refusing to return vehicles postpetition in order to avoid losing its possessory lien interests in vehicles; while city argued that its passive retention of motor vehicles that it had lawfully impounded was not an "act" to exercise control over property of the stay, of kind barred by automatic stay, city's argument ignored fundamental purpose of bankruptcy, to allow debtors to regain their financial foothold and repay their creditors, something for which motor vehicle was necessary. 11 U.S.C.A. § 362(a)(3).

1 Cases that cite this headnote

[9] **Bankruptcy**⇐Collection and Recovery for Estate; Turnover

Turnover statute compels the return of estate property, including property in which debtor did not have a possessory interest at the time the bankruptcy proceedings commenced. 11 U.S.C.A. § 542(a).

[10] **Bankruptcy**⇐Adequate Protection

It is obligation of creditor with possessory lien interest in debtor's property to come to court and ask for adequate protection of its interest,

not the debtor's obligation to file adversary proceeding against every creditor holding her property at the time that she files for bankruptcy.

1 Cases that cite this headnote

[11] **Bankruptcy**⇐Construction and Operation

Courts construe the Bankruptcy Code liberally in favor of debtors and strictly against creditors. 11 U.S.C.A. § 101 et seq.

[12] **Bankruptcy**⇐Automatic Stay

Automatic stay is one of the fundamental debtor protections provided by bankruptcy laws, and courts therefore narrowly construe exceptions to the stay in order to give the stay its intended broad application. 11 U.S.C.A. § 362(a).

[13] **Bankruptcy**⇐Acts excepted from stay

Stay exception for "any act to perfect, or to maintain or continue the perfection of, an interest in property" did not permit city to continue to retain possession of motor vehicles that it had impounded prepetition for Chapter 13 debtors' unpaid parking and moving tickets; involuntary turnover of vehicles by city solely to comply with its obligations under the Bankruptcy Code would not result in loss of its possessory lien interest in vehicles. 11 U.S.C.A. § 362(b)(3).

[14] **Bankruptcy**⇐Acts excepted from stay

By enacting stay exception for "any act to perfect, or to maintain or continue the perfection of, an interest in property," and by limiting trustee's power to avoid an unperfected lien by making that power subject to any nonbankruptcy law that permits perfection to relate back, Congress sought to prevent a trustee from avoiding the lien of creditor when only the intervening bankruptcy stopped creditor from perfecting or continuing perfection of its lien; purpose of these provisions is to prevent creditors from losing their lien rights due to debtor's bankruptcy filing, not to permit creditors to retain possession of debtors' property. 11 U.S.C.A. §§ 362(b)(3), 546(b).

[15] **Bankruptcy**⇐Administrative Proceedings and Governmental Action

"Police or regulatory power" exception to automatic stay is narrowly construed to apply to the enforcement of state laws affecting health, welfare, morals and safety, but not to regulatory laws that directly conflict with control of the res or property by bankruptcy court. 11 U.S.C.A. § 362(b)(4).

[16] **Bankruptcy**⇐Administrative Proceedings and Governmental Action

City's retention of possession of motor vehicles which it had impounded prepetition for unpaid parking tickets and other monetary penalties assessed against Chapter 13 debtors, the vehicles' owners, and not against offending drivers, until such time as tickets and penalties were paid in full, was focused on debtors' financial obligations, not on public safety matters, and did not come within "police or regulatory power" exception to automatic stay. 11 U.S.C.A. § 362(b)(4).

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[17] **Bankruptcy**⇨Administrative Proceedings and Governmental Action

Courts apply two tests to determine whether a state's actions fall within the "police or regulatory power" exception to automatic stay, the "pecuniary purpose" test and the "public policy" test, and the satisfaction of either test is sufficient for the stay exception to apply. 11 U.S.C.A. § 362(b)(4).

[18] **Bankruptcy**⇨Administrative Proceedings and Governmental Action

"Pecuniary purpose" test for whether an action comes within the "police or regulatory power" exception to automatic stay requires court to look to what specific acts the government wishes to carry out and determine if such execution will result in an economic advantage over third parties in relation to debtor's estate. 11 U.S.C.A. § 362(b)(4).

[19] **Bankruptcy**⇨Administrative Proceedings and Governmental Action

If focus of the State's alleged exercise of its police power is directed at debtor's financial obligations, rather than at the State's health and safety concerns, then automatic stay is applicable. 11 U.S.C.A. § 362(b)(4).

[20] **Bankruptcy**⇨Administrative Proceedings and Governmental Action

"Public policy" test for whether an action comes within the "police or regulatory power" exception to automatic stay considers whether the State's action is principally to effectuate public policy or to adjudicate private rights. 11 U.S.C.A. § 362(b)(4).

[21] **Bankruptcy**⇨Administrative Proceedings and Governmental Action

Even if court assumed that city's adjudication of parking and minor moving violations against Chapter 13 debtors was result of city's exercise of its police and regulatory powers, city could not enforce these final determinations of liability, which were in nature of money judgments, by retaining possession of debtors' vehicles until it was paid in full, without violating automatic stay; city had to seek satisfaction of any prepetition debts owed to it by debtors through bankruptcy process, just like any other creditor. 11 U.S.C.A. § 362(b)(4).

3 Cases that cite this headnote

***919** Appeal from the United States Bankruptcy Court for the Northern District of Illinois, Eastern Division. No. 18-02860—**Jack B. Schmetterer**, *Bankruptcy Judge.*

Appeal from the United States Bankruptcy Court for the Northern District of Illinois, Eastern Division. No. 17-25141—**Jacqueline P. Cox**, *Bankruptcy Judge.*

Appeal from the United States Bankruptcy Court for the Northern District of Illinois, Eastern Division. No. 18-16544—**Deborah Lee Thorne**, *Bankruptcy Judge.*

Appeal from the United States Bankruptcy Court for the Northern District of Illinois, Eastern Division. No. 18-04116—**Carol A. Doyle**, *Chief Bankruptcy Judge.*

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John A. Haderlein, Attorney, JOHN HADERLEIN, ATTORNEY AT LAW, Libertyville, IL, for Appellee JASON S. HOWARD (Case No. 18-2793).

Marilyn O. Marshall, OFFICE OF THE CHAPTER 13 TRUSTEE, for Trustee MARILYN O. MARSHALL (Case No. 18-2835).

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Before Flaum, Kanne, and Scudder, Circuit Judges.

Opinion

Flaum, Circuit Judge.

***920** In this consolidated appeal of four Chapter 13 bankruptcies, we consider whether the City of Chicago may ignore the Bankruptcy Code's automatic stay and continue to hold a debtor's vehicle until the debtor pays her outstanding parking tickets. Prior to the debtors' filing for bankruptcy, the City impounded each of their vehicles for failure to pay multiple traffic fines. After the debtors filed their Chapter 13 petitions, the City refused to return their vehicles, claiming it needed to maintain possession to continue perfection of its possessory liens on the vehicles and that it would only return the vehicles when the debtors paid in full their outstanding fines. The bankruptcy courts each held that the City violated the automatic stay by "exercising control" over property of the bankruptcy estate and that none of the exceptions to the stay applied. The courts ordered the City to return debtors' vehicles and imposed sanctions on the City for violating the stay.

This is not our first time addressing this issue: in *Thompson v. General Motors Acceptance Corp.*, 566 F.3d 699 (7th Cir. 2009), we held that a creditor must comply with the automatic stay and return a debtor's vehicle upon her filing of a bankruptcy petition. We decline the City's request to overrule *Thompson*. We therefore affirm the bankruptcy courts' judgments relying on *Thompson*, and we also agree with the bankruptcy courts that none of the exceptions to the stay apply.

I. Background

The Chicago Municipal Code permits creditor-appellant the City of Chicago to immobilize and then impound a vehicle if its owner has three or more "final determinations of liability," or two final determinations that are over a year old, "for parking, standing, compliance, automated traffic law enforcement system, or automated speed enforcement system violation[s]." Municipal Code of Chicago ("M.C.C.") § 9-100-120(b); *see also id.* § 9-80-240(a) (providing for impoundment of vehicles "operated by a person with a suspended or revoked driver's license"). The fines for violations of the City's Traffic Code range from $ 25 (*e.g.*, parallel parking violation) to $ 500 (*e.g.*, parking on a public street without displaying a wheel tax license emblem). *Id.* § 9-100-020(b)–(c). Failure to pay the fine within twenty-five days automatically doubles the penalty. *Id.* § 9-100-050(e). After a vehicle is impounded, the owner is further subjected to towing and storage fees, *see id.* § 9-64-250(c), and to the City's costs and attorney's fees for collection activity. *Id.* §§ 1-19-020, 2-14-132(c)(1)(A). To retrieve her vehicle, an owner may either pay the fines, towing and storage fees, and collection costs and fees in full, *id.* § 2-14-132(c)(1)(A), or pay the full amount via an installment plan over a period of up to thirty-six months,

provided she makes an initial payment of half the fines and penalties plus all of the impoundment, towing, and storage charges. *Id.* § 9-100-101(a)(2)–(3).

In 2016, the City amended the Code to include: "Any vehicle impounded by the City or its designee shall be subject to a possessory lien in favor of the City in the amount required to obtain release of the vehicle." *Id.* § 9-92-080(f). Based on this provision, the City began refusing to release impounded vehicles to debtors who had filed Chapter 13 petitions. That is just what occurred in these four cases.

A. *In re Fulton*

Debtor-appellee Robbin Fulton uses a vehicle to commute to work, transport her ***921** young daughter to day care, and care for her elderly parents on weekends. On December 24, 2017, three weeks after she purchased a 2015 Kia Soul, the City towed and impounded the vehicle for a prior citation of driving on a suspended license. Fulton filed a Chapter 13 bankruptcy petition on January 31, 2018 and filed a plan on February 5, treating the City as a general unsecured creditor. The City filed a general unsecured proof of claim on February 23 for $ 9,391.20. After the court confirmed Fulton's plan on March 21, she requested the City turn over her vehicle. The City then amended its proof of claim to add impound fees, for a total of $ 11,831.20, and to assert its status as a secured creditor; it did not return Fulton's vehicle.

On May 2, Fulton filed a motion for sanctions arguing the City was required to turn over her vehicle pursuant to *Thompson* and that its failure to do so was sanctionable conduct. The City countered that Fulton must seek turnover through an adversary proceeding. It asserted it was retaining possession to perfect its possessory lien and was thus excepted from the automatic stay pursuant to 11 U.S.C. § 362(b)(3).

On May 25, the bankruptcy court held that the City was required to return Fulton's vehicle under *Thompson* and that the City was not excepted from the stay under § 362(b)(3). The court ordered the City to turn over Fulton's vehicle no later than May 29, imposed a sanction of $ 100 for every day the City failed to comply, and sustained Fulton's objection to the City's claim as a secured creditor. The City moved to stay the order in the district court pending appeal; the district court denied the stay request on September 10. Eventually, the City returned Fulton's vehicle. At no point did the City initiate proceedings to protect its rights under § 363(e).

B. *In re Shannon*

The City impounded debtor-appellee Timothy Shannon's 1997 Buick Park Avenue on January 8, 2018 for unpaid parking tickets. Shannon filed a Chapter 13 petition on February 15. On February 27, the City filed an unsecured proof of claim for $ 3,160 in fines dating back to 1999. Shannon, in turn, filed a proposed plan that did not include the City as a secured creditor, to which the City did not object, and the court confirmed the plan on May 1. When Shannon sought the return of his vehicle, the City amended its proof of claim, adding fines, storage, and towing fees for a total of $ 5,600, and stated the claim was secured by its possession of Shannon's vehicle.

Shannon filed a motion for sanctions on June 12, asserting the stay required the City to turn over his vehicle. The court granted his motion on September 7; it held the City's claim was unsecured because it did not object to the plan that characterized the debt as such. It also determined the City violated the stay by failing to return Shannon's vehicle, that the §§ 362(b)(3) and (b)(4) exceptions to the stay did not apply, and that the City further violated § 362(a)(4) and (a)(6) by retaining the vehicle. The court noted the City was free to file a motion seeking adequate protection of its lien. The City returned Shannon's car and did not file any such motion.

C. *In re Peake*

Debtor-appellee George Peake relies on his car to travel approximately forty-five miles from his home to work. The City impounded his 2007 Lincoln MKZ for unpaid fines on June 1, 2018. Peake filed a Chapter 13 petition on June 9. In response, the City filed a secured proof of claim for $ 5,393.27 and asserted a possessory lien on his vehicle. After the City ***922** refused Peake's request to return his vehicle, he filed a motion for sanctions and for turnover. On August 15, the bankruptcy court granted the motion; it held that neither § 362(b)(3) nor (b)(4) applied, so the City's retention of Peake's vehicle violated the stay, and it ordered the City to release his vehicle immediately. The City filed a motion to stay the order pending appeal, which the court denied on August 22. The same day, Peake filed a motion for civil contempt based on the City's refusal to release his vehicle. The

court granted the motion and entered an order requiring the City to pay monetary sanctions—$ 100 per day from August 17 through August 22 and $ 500 per day thereafter until the City returned his vehicle. The City filed an emergency motion for a stay pending appeal in our Court, which we denied. Finally, the City released Peake's vehicle. At no point did the City file a motion to protect its interest in the vehicle.

D. *In re Howard*

The City immobilized debtor-appellee Jason Howard's vehicle on August 9, 2017 and impounded it soon after. Howard filed a Chapter 13 petition on August 22. The City filed a secured proof of claim on August 23 for $ 17,110.80. The court confirmed Howard's plan on October 16, which included a nonpriority unsecured debt of $ 13,000 owed to the City for parking tickets. Though the Code did not impose an automatic stay when Howard filed his petition due to his prior dismissed bankruptcy petitions, *see* 11 U.S.C. § 362(c)(4)(A), the court granted Howard's motion to impose a stay when it confirmed his plan on October 16. The City did not object to its treatment as unsecured under the plan and did not appeal the confirmation order; rather, it simply refused to release Howard's vehicle unless he paid 100% of its claim.

On January 22, 2018, the court issued a rule to show cause to the City why it should not be sanctioned for refusing to release Howard's vehicle in accordance with *Thompson*. The court rejected the City's argument that it was excepted from the stay under § 362(b)(3) and, on April 16, 2018, ordered sanctions of $ 50 per day beginning August 22, 2017 for the City's violation of the stay.

[1] [2]After the City filed its opening appellate brief, Howard filed notice of his intention not to participate in the appeal. His counsel explained Howard's bankruptcy case had been dismissed and the City disposed of his vehicle. He has since filed a new bankruptcy case to address his parking tickets but has abandoned interest in the vehicle that was the subject of the relevant Chapter 13 petition in the bankruptcy court below. However, "issues related to an alleged violation of the automatic stay" are not mooted by dismissal of a bankruptcy petition, *Denby-Peterson v. Nu2u Auto World*, 595 B.R. 184, 188 (D.N.J. 2018); a court "must have the power to compensate victims of violations of the automatic stay and punish the violators, even after the conclusion of the underlying bankruptcy case." *In re Johnson*, 575 F.3d 1079, 1083 (10th Cir. 2009) (citing *In re Davis*, 177 B.R. 907, 911–12 (B.A.P. 9th Cir. 1995)).

* * *

In each of these four cases, the City appealed the bankruptcy courts' orders finding the City violated the stay. These cases have been consolidated for appeal.

II. Discussion

[3]The main question before us is whether the City is obligated to return a debtor's vehicle upon her filing of a Chapter 13 bankruptcy petition, or whether the City is entitled to hold the debtor's vehicle until she pays the fines and costs or until she obtains a court order requiring the City to turn over the vehicle. We review a ***923** bankruptcy court's factual findings for clear error and conclusions of law de novo. *In re Jepson*, 816 F.3d 942, 945 (7th Cir. 2016).

A. The Automatic Stay

Section 362(a)(3) of the Bankruptcy Code provides that a Chapter 13 bankruptcy petition "operates as a stay, applicable to all entities, of ... any act to obtain possession of property of the estate or of property from the estate or to *exercise control* over property of the estate." 11 U.S.C. § 362(a)(3) (emphasis added). We applied this provision to a very similar factual situation in *Thompson v. General Motors Acceptance Corp.* There, a creditor seized a debtor's car after he defaulted on payments. 566 F.3d at 700. The debtor filed a Chapter 13 petition and attempted to retrieve his car, but the creditor refused. *Id.* We considered two issues relating to § 362(a)(3): whether the creditor "exercised control" of property of the bankruptcy estate by failing to return the vehicle after the debtor filed for bankruptcy, and whether the creditor was required to return the vehicle prior to a court determination establishing the debtor could provide adequate protection for the creditor's interest in the vehicle. *Id.* at 701.

1. "Exercise Control"

[4]First, we observed in *Thompson* there was no debate the debtor has an equitable interest in his vehicle, and "as such, it is property of his bankruptcy estate." 566 F.3d at 701 (citing *United States v. Whiting Pools, Inc.*, 462 U.S. 198, 203, 103 S.Ct. 2309, 76 L.Ed.2d 515 (1983)); *see* 5 Collier on Bankruptcy ¶ 541.01 (16th ed. 2019) ("Congress's intent to define property of the estate in the broadest possible sense is evident from the language of the statute which, in section 541(a)(1), initially defines the scope of estate property to be all legal or equitable interests of the debtor in property as of the commencement of the case, wherever located and by whomever held."). We then rejected the creditor's argument that passively holding the asset did not satisfy the Code's definition of exercising control: "Holding onto an asset, refusing to return it, and otherwise prohibiting a debtor's beneficial use of an asset all fit within th[e] definition, as well as within the commonsense meaning of the word." *Thompson*, 566 F.3d at 702. As we explained, limiting the reach of "exercising control" to "selling or otherwise destroying the asset," as the creditor proposed, did not fit with bankruptcy's purpose: "The primary goal of reorganization bankruptcy is to group *all* of the debtor's property together in his estate such that he may rehabilitate his credit and pay off his debts; this necessarily extends to all property, even property lawfully seized pre-petition." *Id.* (citing *Whiting Pools*, 462 U.S. at 203–04, 103 S.Ct. 2309).

Additionally, Congress amended § 362(a)(3) in 1984 to prohibit conduct that "exercise[d] control" over estate assets. We determined this addition suggested congressional intent to make the stay more inclusive by including conduct of "creditors who seized an asset pre-petition." *Id.*; *see* *In re Javens*, 107 F.3d 359, 368 (6th Cir. 1997) ("The fact that 'to obtain possession' was amended to 'to obtain possession ... or to exercise control' hints [ ] that this kind of 'control' might be a broadening of the concept of possession ... It could also have been intended to make clear that [§ 362](a)(3) applied to property of the estate that was not in the possession of the debtor." (first alteration in original)); *In re Del Mission Ltd.*, 98 F.3d 1147, 1151 (9th Cir. 1996) (The 1984 amendment "broaden[ed] the scope of § 362(a)(3) to proscribe the mere knowing retention of estate property."). We therefore held that in retaining possession of the car, the creditor violated the automatic stay in § 362(a)(3). *Thompson*, 566 F.3d at 703.

*924 *2. Compulsory Turnover*

[5]Next, we concluded § 362(a)(3) becomes effective immediately upon filing the petition and is not dependent on the debtor first bringing a turnover action. *Id.* at 707–08. In so concluding, we relied on a plain reading of §§ 363(e) and 542(a) and the Supreme Court's decision in *Whiting Pools.*

[6]Section 363(e) provides:

> [O]n request of an entity that has an interest in property used, sold, or leased, or proposed to be used, sold, or leased ... by the trustee, the court, with or without a hearing, shall prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of such interest.

11 U.S.C. § 363(e). The creditor acknowledged, and we agreed, that it has the burden of requesting protection of its interest in the asset under § 363(e). "However, if a creditor is allowed to retain possession, then this burden is rendered meaningless—a creditor has no incentive to seek protection of an asset of which it already has possession." *Thompson*, 566 F.3d at 704. For § 363(e) to have meaning then, the asset must be returned to the estate prior to the creditor seeking protection of its interest. *Id.*; *cf.* *In re Sharon*, 234 B.R. 676, 684 (B.A.P. 6th Cir. 1999) ("[T]he Bankruptcy Code does not elevate [the creditor's] adequate protection right above the Chapter 13 debtor's right to possession and use of a car.").

[7]Moreover, § 542(a) "indicates that turnover of a seized asset is compulsory." *Thompson*, 566 F.3d at 704. Section 542(a) requires that a creditor in possession of property of the estate "*shall deliver* to the trustee, and account for, such property or the value of such property,

unless such property is of inconsequential value or benefit to the estate." 11 U.S.C. § 542(a) (emphasis added). We observed that a majority of courts had found § 542(a) worked in conjunction with § 362(a) "to draw back into the estate a right of possession that is claimed by a lien creditor pursuant to a pre-petition seizure; the Code then substitutes 'adequate protection' for possession as one of the lien creditor's rights in the bankruptcy case." *Thompson*, 566 F.3d at 704 (quoting *Sharon*, 234 B.R. at 683). Because "[t]he right of possession is incident to the automatic stay," *id.*, the creditor must first return the asset to the bankruptcy estate. Only then is "the bankruptcy court [ ] empowered to condition the right of the estate to keep possession of the asset on the provision of certain specified adequate protections to the creditor." *Id.*; *see also* 11 U.S.C. § 362(d)(1) ("On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under [§ 362](a) ... for cause, including the lack of adequate protection of an interest in property ...."). The Supreme Court indicated as much in *Whiting Pools* when it explained that a "creditor with a secured interest in property included in the estate must look to [§ 363(e)] for protection, *rather than to the nonbankruptcy remedy of possession*." 462 U.S. at 204, 103 S.Ct. 2309 (emphasis added).

3. Thompson *Controls*

[8]Applying *Thompson* to the facts before us, we conclude, as each bankruptcy court did, that the City violated the automatic stay pursuant to § 362(a)(3) by retaining possession of the debtors' vehicles after they declared bankruptcy. *See In re Shannon*, 590 B.R. 467, 477 (Bankr. N.D. Ill. 2018), ECF No. 64 ("*Thompson* [ ] requires any secured creditor in possession of a debtor's vehicle to return it immediately and seek adequate protection ...."); *In re Peake*, 588 B.R. 811, 816 (Bankr. N.D. Ill. 2018), ECF No. 40 ("[T]he City's conduct in retaining possession of the vehicle violates [§] 362(a)(3) as that section ***925** has been interpreted ... in *Thompson* ...."); *In re Fulton*, 18-bk-02860, Mem. Op. at 2, 2018 WL 2392854 (Bankr. N.D. Ill. May 25, 2018), ECF No. 39 ("[T]he City is circumventing entirely the procedural burden imposed on it by *Thompson* and the protections provided to debtors by the automatic stay."); *In re Howard*, 17-bk-25141, Mem. Op. at 10, 2018 WL 1830910 (Bankr. N.D. Ill. Apr. 16, 2018), ECF. No. 63 ("[Section 362(a)] does not authorize continued possession of impounded vehicles in contravention of the *Thompson* ruling."). The City was required to return debtors' vehicles and seek protection within the framework of the Bankruptcy Code rather than through "the nonbankruptcy remedy of possession." *Whiting Pools*, 462 U.S. at 204, 103 S.Ct. 2309.

The City acknowledges *Thompson* controls but asks us to overrule *Thompson* for three reasons: (1) property impounded prior to bankruptcy is not property of the bankruptcy estate because the debtors did not have a possessory interest in their vehicles at the time of filing; (2) the stay requires creditors to maintain the status quo and not take any action, such as returning property to the debtor, so the onus is on the debtor to move for a turnover action to retrieve her vehicle; and (3) the plain language of § 362(a)(3) requires an "act" to exercise control, and passive retention of the vehicle is not an "act."

[9]We decline the City's request; *Thompson* considered and rejected these arguments. More fundamentally, the City's arguments ignore the purpose of bankruptcy—"to allow the debtor to regain his financial foothold and repay his creditors." *Thompson*, 566 F.3d at 706; *see also* 5 Collier on Bankruptcy ¶ 541.01 ("[The] central aggregation and protection of property [ ] promote[s] the fundamental purposes of the Bankruptcy Code: the breathing room given to a debtor that attempts to make a fresh start, and the equality of distribution of assets among similarly situated creditors according to the priorities set forth within the Code."). To effectively do so, a debtor must be able to use his assets "while the court works with both debtor and creditors to establish a rehabilitation and repayment plan." *Thompson*, 566 F.3d at 707; *see also* *Whiting Pools*, 462 U.S. at 203, 103 S.Ct. 2309 ("[T]o facilitate the rehabilitation of the debtor's business, all the debtor's property must be included in the reorganization estate."). This is why § 542 compels the return of property to the estate, including "property in which the debtor did not have a possessory interest at the time the bankruptcy proceedings commenced." *Whiting Pools*, 462 U.S. at 205, 103 S.Ct. 2309; *see* *In re Weber*, 719 F.3d 72, 79 (2d Cir. 2013) ("*Whiting Pools* teaches that the filing of a petition will generally transform a debtor's equitable interest into a bankruptcy estate's possessory right in the vehicle."). Thus, contrary to the City's argument, the

status quo in bankruptcy is the return of the debtor's property to the estate. In refusing to return the vehicles to their respective estates, the City was not passively abiding by the bankruptcy rules but actively resisting § 542(a) to exercise control over debtors' vehicles.

What's more, the position we took in *Thompson* brought our Circuit in line with the majority rule, held by the Second, Eighth, and Ninth Circuits. *See Weber*, 719 F.3d 72; *Del Mission* 98 F.3d 1147; *In re Knaus*, 889 F.2d 773 (8th Cir. 1989). Although the Tenth Circuit recently adopted the City's view, *see In re Cowen*, 849 F.3d 943 (10th Cir. 2017), that position is still the minority rule. Our reasoning in *Thompson* continues to reflect the majority position and we believe it is the appropriate reading of the bankruptcy statutes. At bottom, the City wants to maintain possession of the vehicles not because it wants the vehicles but to put pressure on ***926** the debtors to pay their tickets. That is precisely what the stay is intended to prevent.[1]

The City, though, pleads necessity; it claims that, without retaining possession, it is helpless to prevent the loss or destruction of the vehicles. It did not attempt in any of these cases, however, to seek adequate protection of its interests through the methods available under the Bankruptcy Code, and at oral argument, the City asserted it did not have "the opportunity" to request such protection before the bankruptcy courts ordered it to return the vehicles. The record belies this statement. In each case, the parties engaged in motion practice, often over the course of months, before the courts held the City to be in violation of the stay. At any point the City could have sought adequate protection of its interests, but it chose not to avail itself of the Code's available procedures. *See, e.g.*, 11 U.S.C. § 362(d)(1) (court may relieve creditor from the stay if debtor cannot adequately protect creditor's interest in the property); *id.* § 362(f) (court may relieve creditor from stay "as is necessary to prevent irreparable damage to the interest of an entity in property"); *id.* § 363(e) (creditor may request court to place limits or conditions on trustee's power to use, sell, or lease property to protect creditor's interest).

[10]We recognize that once the City complies with the automatic stay and immediately turns over vehicles, it will need to seek protection on an expedited basis. Though we leave it to the City and the bankruptcy courts to fashion the precise procedure for doing so, we note the following: The City will have notice of the bankruptcy petition when the debtor requests her vehicle, if not sooner. At that time, the City may immediately file an emergency motion for adequate protection of its interest in a debtor's vehicle, which may be heard within a day or so, and the City can even file such motions ex parte if necessary. *See id.* § 363(e); Fed. R. Bankr. P. 4001(a)(2); *see also* 11 U.S.C. § 362(d)(1), (f); Bankr. N.D. Ill. R. 9013-9(B)(9)(d) (motion for relief from stay under § 362 where movant alleges security interest in vehicle "ordinarily [ ] granted without hearing"). It will be the rare occasion where a single day's delay will have lost the City the value of its security. Regardless, the Code is clear that it is the creditor's obligation to come to court and ask for protection, not, as the City advocates, the debtor's obligation to file an adversary proceeding against every creditor holding her property at the time she files for bankruptcy. *Cf. In re Lisse*, 921 F.3d 629, 639 (7th Cir. 2019) ("The basic premise [of Chapter 13] is to facilitate the debtor's ability to pay his creditors ....").

The City's argument that it will be overburdened with responding to Chapter 13 petitions is ultimately unavailing; any burden is a consequence of the Bankruptcy Code's focus on protecting debtors and on preserving property of the estate for the benefit of *all* creditors. It perhaps also reflects the importance of vehicles to residents' everyday lives, particularly where residents need their vehicles to commute to work and earn an income in order to eventually pay off their fines and other debts.[2] It is not a reason to permit the ***927** City to ignore the automatic stay and hold captive property of the estate, in contravention of the Bankruptcy Code.

Furthermore, if a debtor files a bankruptcy petition in bad faith and immediately dismisses her case, as the City claims many debtors do solely to retrieve their impounded vehicles, the City has recourse: it may file a bad faith motion against the debtor. If the court finds bad faith, it may immediately dismiss the case and may even sanction the debtor. 11 U.S.C. § 1307(c); *see, e.g.*, *Lisse*, 921 F.3d at 639–41 (affirming sanctions and dismissal of Chapter 13 petition filed in bad faith to collaterally attack state court judgment); *In re Bell*, 125 F. App'x 54, 57 (7th Cir. 2005) (affirming dismissal of Chapter 13 petition with prejudice where debtors filed multiple petitions "solely to impede the foreclosure sale" of their home).

B. Exceptions to the Stay

[11] [12]The City next argues that even if the stay applies, it is excepted under § 362(b)(3) and (b)(4). "We construe the Bankruptcy Code 'liberally in favor of the debtor and strictly against the creditor.' " *Village of*

San Jose v. McWilliams, 284 F.3d 785, 790 (7th Cir. 2002) (quoting *In re Brown*, 108 F.3d 1290, 1292 (10th Cir. 1997)). The automatic stay is "one of the fundamental debtor protections provided by the bankruptcy laws." *Midlantic Nat'l Bank v. N.J. Dep't of Envtl. Prot.*, 474 U.S. 494, 503, 106 S.Ct. 755, 88 L.Ed.2d 859 (1986) (quoting S. Rep. No. 95–989, at 54 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5840). We therefore narrowly construe exceptions "to give the automatic stay its intended broad application." *In re Grede Foundries, Inc.*, 651 F.3d 786, 790 (7th Cir. 2011); *see In re Stringer*, 847 F.2d 549, 552 (9th Cir. 1988) ("Congress clearly intended the automatic stay to be quite broad. Exemptions to the stay, on the other hand, should be read narrowly to secure the broad grant of relief to the debtor." (footnotes omitted)).

1. Section 362(b)(3)

[13] Section 362(b)(3) provides that a Chapter 13 bankruptcy petition does not operate as a § 362(a) automatic stay:

> of any act to perfect, or to maintain or continue the perfection of, an interest in property to the extent that the trustee's rights and powers are subject to such perfection under section 546(b) of [the Bankruptcy Code] or to the extent that such act is accomplished within the period provided under section 547(e)(2)(A) of [the Bankruptcy Code].

11 U.S.C. § 362(b)(3). Section 546(b) limits a trustee's power to avoid a nonperfected lien by making that power subject to any ***928** nonbankruptcy law that "permits perfection of an interest in property to be effective against an entity that acquires rights in such property before the date of perfection," or "provides for the maintenance or continuation of perfection of an interest in property to be effective against an entity that acquires rights in such property before the date on which action is taken to effect such maintenance or continuation." 11 U.S.C. § 546(b)(1). The classic example of this exception is for a creditor who has a grace period for perfecting its interest, such as under the Uniform Commercial Code. *See* 3 Collier on Bankruptcy ¶ 362.05 (explaining § 362(b)(3) permits a purchase-money secured creditor to retroactively perfect under the twenty-day grace period provided in Article 9 of the U.C.C. and permits the filing of continuations of financing statements under U.C.C. § 9-515).

[14]As the *In re Shannon* court explained, through §§ 362(b)(3) and 546(b), "Congress sought only to prevent a trustee from avoiding the lien of a creditor when only the intervening bankruptcy stopped the creditor from perfecting or continuing perfection of its lien." Thus, the purpose of these sections is to prevent creditors from losing their lien rights because of the bankruptcy; they do not permit creditors to retain possession of debtors' property. Indeed, if the nonbankruptcy law requires a creditor to seize property after the filing of a bankruptcy petition to perfect or maintain the perfection of a lien, § 546(b)(2) replaces the seizure requirement with the giving of notice. *See* 3 Collier on Bankruptcy ¶ 362.05. "This assures that the trustee's right to maintain possession of the property will be unaffected by the creditor's right to perfect its interest." *Id.* And the (b)(3) exception permits a creditor to give notice under § 546(b)(2) without violating the automatic stay.

Here, the City argues the Chicago Municipal Code (a nonbankruptcy law) gives it the right to retain possession of a debtor's vehicle until the debt is paid, thereby creating a possessory lien on the vehicle. *See, e.g.*, M.C.C. §§ 9-92-080(f), 9-100-120(b)–(c). It further asserts it must retain the vehicle to maintain perfection of its lien.

First, as to perfection, it is commonly understood that an interest in property is perfected when it is valid against other creditors who have an interest in the same property. *See Perfection*, Black's Law Dictionary (11th ed. 2019). The City's continued possession of a debtor's vehicle is one way to perfect its lien because it can demand the amount owed to it from any holder of an interest in the vehicle before it gives up possession, be that the debtor or another lienholder asserting its right to possession of the vehicle. *See* M.C.C. § 9-92-080(a), (c). However, possession is not the only way to perfect; the City can also perfect its lien by filing notice of its interest in the vehicle, such as with the Secretary of State or the Recorder of Deeds. And the Chapter 13 plan, itself, provides a public record of secured liens. *See* 11 U.S.C. § 1325(a)(5) (regarding the rights of secured

creditors related to confirmation of the plan). Thus, the City does not need to retain possession of the vehicle to maintain perfection of its lien.

Second, despite its arguments to the contrary, the City's possessory lien is not destroyed by its involuntary loss of possession due to forced compliance with the Bankruptcy Code's automatic stay. The City did not indicate any intent to abandon or release its lien, so its possessory lien survives its loss of possession to the bankruptcy estate. *See In re Estate of Miller*, 197 Ill.App.3d 67, 144 Ill.Dec. 890, 556 N.E.2d 568, 572 (1990) ("The law respecting common law retaining liens is that the involuntary relinquishment of retained property pursuant to a court order does not result in the loss of the lien."); *see also* ***929** *In re Borden*, 361 B.R. 489, 495 (B.A.P. 8th Cir. 2007) ("[I]nvoluntary loss of possession does not defeat the [ ] lien."); Restatement (First) of Security § 80 cmt. c (1941) ("The lien is a legal interest dependent upon possession. Where the lienor voluntarily gives up the possession, his lien, at least so far as it is a legal interest, is gone. The lienor ... does not lose his legal interest if he is deprived without his consent of his possession.").[3]

Because the City does not lose its perfected lien via the involuntary loss of possession of the debtors' vehicles to the bankruptcy estates, § 362(b)(3) does not apply to except it from the stay. To the extent the City has any doubt about the continuation of its lien, when it requests relief from the automatic stay and adequate protection, it could also ask the bankruptcy court to include in its order a notation of the City's continuing lien on the property.

2. *Section 362(b)(4)*

[15] [16]Alternatively, the City looks to § 362(b)(4) to except it from the stay. That section provides that a Chapter 13 bankruptcy petition does not operate as a § 362(a) automatic stay:

> of the commencement or continuation of an action or proceeding by a governmental unit ... to enforce such governmental unit's or organization's police and regulatory power, including the enforcement of a judgment other than a money judgment, obtained in an action or proceeding by the governmental unit to enforce such governmental unit's ... police or regulatory power.

11 U.S.C. § 362(b)(4). "This exception has been narrowly construed to apply to the enforcement of state laws affecting health, welfare, morals and safety, but not to 'regulatory laws that directly conflict with the control of the res or property by the bankruptcy court.' " *In re Cash Currency Exch., Inc.*, 762 F.2d 542, 555 (7th Cir. 1985) (quoting *In re Missouri*, 647 F.2d 768, 776 (8th Cir. 1981)). The City asserts its impoundment of vehicles is an exercise of its police power to enforce traffic regulations as a matter of public safety. The debtors respond that the impoundment of vehicles enhances the City's revenue collection rather than protects public safety, and it is therefore an enforcement of a money judgment which § 362(b)(4) does not permit.

[17]Courts apply two tests to determine whether a state's actions fall within the scope of § 362(b)(4)—the pecuniary purpose test and the public policy test. *Chao v. Hosp. Staffing Servs., Inc.*, 270 F.3d 374, 385–86 (6th Cir. 2001); *In re First All. Mortg. Co.*, 263 B.R. 99, 107–08 (B.A.P. 9th Cir. 2001). Satisfying either test is sufficient for the exception to apply. *See First All. Mortg.*, 263 B.R. at 108; *see also* 3 Collier on Bankruptcy ¶ 362.05.

[18] [19]The pecuniary purpose test requires the court to "look to what specific acts the government wishes to carry out and determine if such execution would result in an economic advantage over third parties in relation to the debtor's estate." *Solis v. Caro*, No. 11-cv-6884, 2012 WL 1230824, at *5 (N.D. Ill. Apr. 12, 2012) (quoting ***930** *In re Emerald Casino, Inc.*, No. 03-cv-05457, 2003 WL 23147946, at *8 (N.D. Ill. Dec. 24, 2003)). "[I]f the focus of the police power is directed at the debtor's financial obligations rather than the [government's] health and safety concerns, the automatic stay is applicable." *In re Ellis*, 66 B.R. 821, 825 (N.D. Ill. 1986) (quoting *In re Sampson*, 17 B.R. 528, 530 (Bankr. D. Conn. 1982)). Though the City says its impoundment laws are "designed to further the safety and welfare of Chicago residents" with just an "ancillary pecuniary benefit," we disagree. In retaining possession of the vehicles until it is paid in full, the City is "attempting to satisfy a debt outside the bankruptcy process," which would give it an advantage over other parties interested in the debtors' estates.

Emerald Casino, 2003 WL 23147946, at *9. The City's act is focused on the debtor's financial obligation, not its safety concerns, and thus fails the pecuniary purpose test.

[20]Alternatively, the public policy test considers whether the state action is principally to effectuate public policy or to adjudicate private rights. *Hosp. Staffing Servs.*, 270 F.3d at 385–86; *Caro*, 2012 WL 1230824, at *4. The public policy the City highlights is enforcing its traffic ordinances against repeat offenders "for the safety and convenience of the public." It explains the traffic ordinance system gradually escalates, beginning with the issuance of fines then intensifying to immobilization and impoundment only after an individual ignores repeat citations. Without impoundment as a general deterrence, the City argues, it cannot enforce its traffic regulations. *See* *Emerald Casino*, 2003 WL 23147946, at *6.

The debtors argue the balance between revenue collection and public safety weighs heavily toward the former. Additionally, prior to the 2016 Municipal Code amendment imposing a possessory lien on impounded vehicles, the City released impounded vehicles to Chapter 13 debtors. When the City recently amended the Code, it did not mention public safety concerns but rather stated the amendment was "in response to a growing practice of individuals attempting to escape financial liability for their immobilized or impounded vehicles." Chi., Ill., Ordinance, Amendment of M.C.C. § 9-100-120 (July 6, 2017).

We are persuaded that, on balance, this is an exercise of revenue collection more so than police power. As debtors observe, a not insignificant portion of the City's annual operating fund comes from its collection of parking and traffic tickets. *See* City of Chicago, 2019 Budget Overview 29, 192 (2018), https://chicago.legistar.com/View.ashx?M=F&ID=6683992&GUID=CAEFBC7F-7C1A-4B2E-9F8B-0CB931B3EE88 (fines, forfeitures, and penalties—primarily from parking tickets—constitute approximately nine percent of the 2019 fund). Moreover, the kind of violations the City enforces are not traditional police power regulations; these fines are for parking tickets, failure to display a City tax sticker, and minor moving violations. Even tickets for a suspended license, a seemingly more serious offense, are often the result of unpaid parking tickets and are thus not related to public safety. And the City impounds vehicles regardless of what violations the owner has accrued, without distinguishing between more serious violations that could affect public safety versus the mere failure to pay for parking. Most notably, the City imposes the monetary penalty on the owner of the vehicle, not the driver, which signals a seeming disconnect if the City actually has safety concerns about the offending driver. As the ordinance amending M.C.C. § 9-100-120 demonstrates, the City's focus is on the financial liability of vehicle owners, not on public safety.

[21]But even if we assume that the adjudication of these violations is the result ***931** of the City's exercise of police and regulatory power, the City cannot enforce these final determinations of liability if they are "money judgment[s]" as the term is used in § 362(b)(4). *See* S. Rep. No. 95-989, at 52 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5838 ("Since the assets of the debtor are in the possession and control of the bankruptcy court, and ... constitute a fund out of which all creditors are entitled to share, enforcement by a governmental unit of a money judgment would give it preferential treatment to the detriment of all other creditors."). A judgment is a "money judgment" that cannot be enforced without violating the automatic stay if it requires payment. 3 Collier on Bankruptcy ¶ 362.05 ("[T]he governmental unit still may commence or continue any police or regulatory action, including one seeking a money judgment, but *it may enforce only those judgments and orders that do not require payment.*" (emphasis added)); *First All. Mortg.*, 263 B.R. at 107 (same); *see also* 3 Collier on Bankruptcy ¶ 362.05 ("Although a governmental unit may obtain a liability determination, *it may not collect* on any monetary judgment received." (emphasis added)); *SEC v. Brennan*, 230 F.3d 65, 71 (2d. Cir. 2000) ("[Section] 362(b)(4) permits the *entry* of a money judgment against a debtor ... [but] *anything beyond the mere entry of a money judgment* against a debtor is prohibited by the automatic stay.").

The City claims it did not have money judgments "because it did not pursue the additional steps required to turn the citations into money judgments in the circuit court." We disagree. A "money judgment" is simply an order that identifies "the parties for and against whom judgment is being entered" and "a *definite* and *certain* designation of the amount ... owed." *Penn Terra Ltd. v. Dep't of Envtl. Res.*, 733 F.2d 267, 275 (3d Cir. 1984). Prior to impounding a vehicle, the City must administratively adjudicate the debtor's violations, *see* M.C.C. § 9-100-010, and those adjudications result in a determination of final liability—*i.e.*, a judgment. Only after a debtor has two or three judgments against it does the Municipal Code authorize the City to impound the vehicle until the debtor pays the judgments and related costs and fees. *See id.* §§ 2-14-132(c)(1)(A), 9-92-080, 9-100-120(b). So, without any additional steps, the City had final determinations of liability requiring these

particular debtors to pay it specific sums.

The City does not contest that it conditioned the release of the debtors' vehicles on payment of the amount specified in the final determinations of liability. *Cf. id.* § 9-100-100(b) ("Any fine and penalty ... remaining unpaid after the notice of final determination of liability is sent shall constitute a debt due and owing the city ...."). The continued possession of the vehicles is the City's attempt to short-circuit the state court collection process and to enforce final judgments requiring monetary payment from the debtors. As such, the City is not excepted from the stay under § 362(b)(4). That the City is not excepted under § 362(b)(4) does not "permit[ ] debtors to park for free wherever they like, or to drive without a risk of fines for moving violations ...." *In re Steenes*, 918 F.3d 554, 558 (7th Cir. 2019). This just means the City needs to satisfy the debts owed to it through the bankruptcy process, as do all other creditors.

III. Conclusion

For the foregoing reasons, we AFFIRM the judgments of the bankruptcy courts.

All Citations

926 F.3d 916, 67 Bankr.Ct.Dec. 100, Bankr. L. Rep. P 83,412

Footnotes

1 The *In re Shannon* court further found that § 362(a)(4) and (a)(6) also prohibit the City's continued retention of debtors' vehicles. Because the City is bound by the stay under § 362(a)(3), we do not reach the applicability of the additional stay provisions.

2 We additionally note that the "flood" of Chapter 13 filings is evidence of the disproportionate effect of the City's traffic fines and fees on its low-income residents, an issue that is not unique to Chicago. *See, e.g.*, Maura Ewing, *Should States Charge Low-Income Residents Less for Traffic Tickets?*, The Atlantic (May 13, 2017), https://www.theatlantic.com/politics/archive/2017/05/traffic-debt-california-brown/526491/ (California); Sam Sanders, *Study Finds The Poor Subject To Unfair Fines, Driver's License Suspensions*, NPR: The Two-Way (Apr. 9, 2015), https://www.npr.org/sections/thetwo-way/2015/04/09/398576196/study-find-the-poor-subject-to-unfair-fines-drivers-license-suspensions (Missouri and California); Melissa Sanchez & Sandhya Kambhampati, *How Chicago Ticket Debt Sends Black Motorists Into Bankruptcy*, ProPublica Illinois (Feb. 27, 2018), https://features.propublica.org/driven-into-debt/chicago-ticket-debt-bankruptcy/ ("[African-American] neighborhoods account for 40 percent of all debt, though they account for only 22 percent of all the tickets issued in the city over the past decade—suggesting how the debt burdens the poor."); *see also* Torie Atkinson, Note, *A Fine Scheme: How Municipal Fines Become Crushing Debt in the Shadow of the New Debtors' Prisons*, 51 Harv. C.R.-C.L. L. Rev. 189, 217–22 (2016) ("The consequences of fines and fees can be dramatic and unforgiving: unemployment, loss of transportation, homelessness, loss of government or community services, and poor credit. And without the ability to accumulate wealth or capture even the smallest windfall for themselves, the poor become poorer, unable to climb out of an economic chasm.").

3 The City's attempt to distinguish between loss of possession due to compliance with a court order versus compliance with the automatic stay is in vain. Section 362 provides for the imposition of punitive damages for willful violations of the automatic stay. *See* 11 U.S.C. § 362(k)(1). This demonstrates that failure to comply with the stay may be punished even more severely than failure to comply with a court order and, correspondingly, there is no question the stay *compels* the City to return the vehicles.

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KeyCite Blue Flag – Appeal Notification
Petition for Certiorari Docketed by JOY DENBY-PETERSON v. NU2U AUTO WORLD, ET AL., U.S., February 26, 2020

941 F.3d 115
United States Court of Appeals, Third Circuit.

IN RE: Joy DENBY-PETERSON, Appellant

No. 18-3562
|
Argued May 23, 2019
|
Filed: October 28, 2019

Synopsis
Background: Chapter 13 debtor whose vehicle had been repossessed prepetition filed motion to compel turnover, and also sought to recover for creditor's alleged violations of automatic stay. The United States Bankruptcy Court for the District of New Jersey, Andrew B. Altenburg, J., 576 B.R. 66, denied motion in part. Debtor appealed. The United States District Court for the District of New Jersey, Noel L. Hillman, J., 595 B.R. 184, affirmed. Debtor appealed.

Holdings: The Court of Appeals, Fuentes, Senior Circuit Judge, held that:

[1] as matter of first impression, stay provision had to be interpreted as prohibiting only postpetition affirmative act to exercise control over property of the estate;

[2] creditors that lawfully repossessed the motor vehicle securing their claim prior to commencement of debtor's Chapter 13 case, and that, once bankruptcy petition was filed, passively retained possession of vehicle did not thereby violate automatic stay;

[3] turnover provision of the Bankruptcy Code is not self-executing, and creditor's obligation to turn over estate property in its possession is not automatic; and

[4] even assuming that turnover provision was self-executing, creditors' alleged violation of turnover statute, in failing to promptly turn over motor vehicle, was not also in nature of willful violation of automatic stay.

Affirmed.

Procedural Posture(s): On Appeal; Motion for Damages, Contempt, or Sanctions for Violation of Automatic Stay.

West Headnotes (22)

[1] **Bankruptcy**⇐Conclusions of law; de novo review
Bankruptcy⇐Clear error

On appeal from district court's decision in its bankruptcy appellate capacity, the Court of Appeals reviews district court's determinations de novo, reviewing the legal conclusions of the bankruptcy court de novo and its factual determinations for clear error. Fed. R. Bankr. P. 8013.

1 Cases that cite this headnote

[2] **Bankruptcy**⇐Automatic Stay

Automatic stay serves twofold purpose: (1) of protecting debtor by stopping all collection efforts, harassment and foreclosure actions, thereby giving debtor a respite from creditors; and (2) of protecting creditors as whole by preventing particular creditors from acting unilaterally in their self-interest to obtain payment from a debtor to the detriment of other creditors. 11 U.S.C.A. § 362(a).

[3] **Bankruptcy**⇐Proceedings, Acts, or Persons Affected

Automatic stay, by barring any act to obtain possession of property of the estate or to exercise control over property of the estate, prevents dismemberment of estate, and enables

an orderly distribution of debtor's assets. 11 U.S.C.A. § 362(a)(3).

[4] **Bankruptcy**⇒Damages and attorney fees

Creditor's violation of automatic stay is a "willful violation," of kind supporting damages award against creditor, when the creditor violates the stay with knowledge that bankruptcy petition has been filed. 11 U.S.C.A. § 362(k).

[5] **Bankruptcy**⇒Damages and attorney fees

"Willful violation" of automatic stay, of kind supporting a damages award against the offending creditor, does not require the creditor to intend to violate the stay; rather, it requires that the acts which violate the stay must be intentional. 11 U.S.C.A. § 362(k).

[6] **Statutes**⇒Language

Statutory interpretation must begin with the language of the statute itself.

[7] **Bankruptcy**⇒Construction and Operation

In interpreting provision of the Bankruptcy Code, court is not guided by a single sentence or member of a sentence, but looks to the provisions of the whole law, and to its object and policy. 11 U.S.C.A. § 101 et seq.

[8] **Statutes**⇒What constitutes ambiguity; how determined
Statutes⇒Context

To determine the plainness or ambiguity of statutory language, court, in addition to considering the statutory language itself, may also engage in a studied examination of the statutory context.

[9] **Bankruptcy**⇒Construction and Operation

If court ultimately determines that the provision of the Bankruptcy Code in question is clear and unambiguous, court must simply apply it as written; however, if court finds that the provision is ambiguous, then it must turn to pre-Code practice and legislative history to find its meaning.

[10] **Statutes**⇒Undefined terms

When statutory terms are left undefined, court must look to their ordinary meaning.

[11] **Bankruptcy**⇒Proceedings, Acts, or Persons Affected

Provision of automatic stay that prohibits any party from taking "any act to obtain possession of property of the estate ... or to exercise control over property of the estate" prohibits only "acts to exercise control," and not the actual "exercise of control" itself, and must be interpreted as prohibiting only postpetition affirmative act to exercise control over property of the estate.

11 U.S.C.A. § 362(a)(3).

[12] **Bankruptcy**⇒Proceedings, Acts, or Persons Affected

Language of bankruptcy statute imposing an automatic stay to prohibit anyone from taking "any act to obtain possession of property of the estate ... or to exercise control over property of the estate" is prospective in nature. 11 U.S.C.A. § 362(a)(3).

[13] **Bankruptcy**⇒Repossession

Creditors that lawfully repossessed motor vehicle securing their claim prior to commencement of debtor's Chapter 13 case, and that, once bankruptcy petition was filed, passively retained possession of the vehicle pending an order by bankruptcy court, did not "act to exercise control" over property of the estate in violation of automatic stay and were not liable to debtor in damages for failing to immediately return vehicle once notified of debtor's bankruptcy filing. 11 U.S.C.A. § 362(a)(3), (k).

3 Cases that cite this headnote

[14] **Bankruptcy**⇒Automatic Stay

One of the automatic stay's primary purposes is to maintain the status quo between the debtor and his creditors, thereby affording the parties and the bankruptcy court an opportunity to appropriately resolve competing economic interests in orderly and effective way. 11 U.S.C.A. § 362(a).

[15] **Bankruptcy**⇒Proceedings, Acts, or Persons Affected

Given that bankruptcy statute imposing an automatic stay to prohibit anyone from taking "any act to obtain possession of property of the estate ... or to exercise control over property of the estate" was clear and unambiguous in prohibiting only affirmative, postpetition acts to obtain possession of, or to exercise control over, estate property, there was no need to resort to legislative history to uncover the statute's meaning. 11 U.S.C.A. § 362(a)(3).

[16] **Bankruptcy**⇒Collection and Recovery for Estate; Turnover

Turnover provision of the Bankruptcy Code is not self-executing, and creditor's obligation to turn over estate property in its possession is not automatic. 11 U.S.C.A. § 542(a).

[17] **Bankruptcy**⇒Form and nature; adversary proceeding or application or motion

In order to obtain turnover of property allegedly included in bankruptcy estate, debtor must bring an adversary proceeding in bankruptcy court in order to give the court an opportunity to determine whether the property is subject to turnover. 11 U.S.C.A. § 542(a).

[18] **Bankruptcy**⇒Proceedings

Debtor's right to turnover is subject to substantive and procedural requirements that

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must be evaluated by the bankruptcy court; it is only after bankruptcy court has determined whether those requirements are met that debtor's right to turnover is triggered. 11 U.S.C.A. § 542(a).

[19] **Bankruptcy**⇨Nature and form; adversary proceedings

"Adversary proceeding," as that term is used in the Bankruptcy Rules, is essentially a self-contained trial within the original bankruptcy case itself, in which a panoply of additional procedures apply. Fed. R. Bankr. P. 7001.

[20] **Bankruptcy**⇨Proceedings

Turnover provision does not placing the onus on creditors to immediately surrender property in their possession which the debtor claims is an estate asset and is subject to turnover, without regard to any affirmative defenses that they might have to turnover, and then immediately file a motion in bankruptcy court asserting their rights. 11 U.S.C.A. § 542(a).

[21] **Bankruptcy**⇨Form and nature; adversary proceeding or application or motion

While the word "shall," as used in turnover provision stating that any entity in possession, custody or control of any property that trustee can use, sell, or lease "shall deliver" that property to trustee, might be mandatory in nature, it was mandatory only in context of adversary proceeding presided over by bankruptcy court. 11 U.S.C.A. § 542(a).

[22] **Bankruptcy**⇨Damages and attorney fees

Even assuming that turnover provision of the Bankruptcy Code was self-executing, lack of any cross-references between turnover and automatic stay provisions prevented court from finding that creditors' alleged violation of turnover statute, in failing to promptly turn over motor vehicle that they had lawfully repossessed prepetition upon being notified of debtor's Chapter 13 filing, was also in nature of willful violation of automatic stay, for which debtor was entitled to award of damages. 11 U.S.C.A. §§ 362(k), 542(a).

***118** Appeal from the United States District Court for the District of New Jersey (D.C. No. 1-17-cv-09985), District Judge: Hon. Noel L. Hillman

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Before: McKEE, SHWARTZ, and FUENTES, Circuit Judges.

OPINION OF THE COURT

FUENTES, Circuit Judge.

At the center of this bankruptcy appeal is "America's first sports car": the Chevrolet Corvette.[1] Joy Denby-Peterson

purchased a Chevrolet Corvette in July 2016. Several months later, the Corvette was repossessed by creditors after Denby-Peterson defaulted on her car payments. Denby-Peterson subsequently filed an emergency voluntary Chapter 13 petition in the Bankruptcy Court for the District of New Jersey. She then notified the creditors of the bankruptcy filing and demanded that they return the Corvette to her.

After the creditors did not comply with her demand, Denby-Peterson filed a motion for turnover in the Bankruptcy Court. She sought an order (1) compelling the creditors to return the Corvette to her, and (2) imposing sanctions for the creditors' alleged violation of the Bankruptcy Code's automatic stay.[2] The Bankruptcy Court entered an order mandating turnover of the Corvette to Denby-Peterson but denying Denby-Peterson's request for sanctions. The Bankruptcy Court denied the sanctions request on the basis that the creditors did not violate the automatic stay by failing to return the repossessed Corvette to Denby-Peterson upon receiving notice of the bankruptcy filing. Denby-Peterson ***119** appeals from an order of the District Court affirming the Bankruptcy Court.

We are now presented with an issue of first impression for our Court: whether, upon notice of the debtor's bankruptcy, a secured creditor's failure to return collateral that was repossessed pre-bankruptcy petition is a violation of the automatic stay. We answer in the negative, and thus join the minority of our sister courts—the Tenth and D.C. Circuits—in holding that a secured creditor does not have an affirmative obligation under the automatic stay to return a debtor's collateral to the bankruptcy estate immediately upon notice of the debtor's bankruptcy because failure to return the collateral received pre-petition does not constitute "an[ ] act ... to exercise control over property of the estate."[3] We will therefore affirm the order of the District Court affirming the Bankruptcy Court.

I.

A. Facts

On July 21, 2016, Debtor Joy Denby-Peterson purchased a used yellow 2008 Chevrolet Corvette from a car dealership named Pine Valley Motors. To finance her purchase, Denby-Peterson entered into a retail installment contract with Pine Valley Motors, which, in turn, assigned its rights under the contract to its affiliate company, NU2U Auto World.[4] Under the contract, Denby-Peterson agreed to pay (1) a $3,000 cash down payment; (2) a deferred down payment of $2,491 by August 11, 2016 to pay sales taxes and registration fees to obtain permanent license plate tags; and (3) weekly installment payments of $200 for 212 weeks. Between July 2016 and February 2017, Denby-Peterson made payments totaling $9,200 under the contract, including the $3,000 down payment applied on the day of the sale. She never made the required down payment of $2,491. As a result, the creditors repossessed the Corvette in February or March 2017.[5] The Corvette was never titled or registered in Denby-Peterson's name.

B. Bankruptcy Court Proceedings

i. Denby-Peterson's Chapter 13 Bankruptcy Petition

After the Corvette was repossessed, Denby-Peterson filed a voluntary petition for relief under Chapter 13 of the Bankruptcy Code on March 21, 2017. Under Section 362 of the Code, the filing of the petition triggered an automatic stay of "any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate."[6]

***120** Within two days, the creditors received notice of Denby-Peterson's bankruptcy filing. Counsel for Denby-Peterson had notified them of the filing and demanded that they return the Corvette to Denby-Peterson. Counsel also maintained that the creditors' failure to return the Corvette would result in a violation of the automatic stay. He faxed a letter to the creditors which stated, in relevant part:

> **BE ADVISED** your failure to release the vehicle to Ms. Denby-Peterson is a violation of the Automatic Stay. If the vehicle has not been released before 5pm today, this firm will seek damages, costs, and attorneys' fees against your company for willful violations of the automatic stay.[7]

The creditors did not comply with Denby-Peterson's demand and thus remained in possession of the Corvette.

ii. Denby-Peterson's Motion for Turnover and Sanctions

Denby-Peterson then filed a motion[8] for turnover in Bankruptcy Court, asking the Bankruptcy Court to (1) order the creditors to return the Corvette to her, and (2) impose sanctions for the creditors alleged violation of the automatic stay. Denby-Peterson sought costs and attorneys' fees for filing the motion; compensation for "non-economic damages"; punitive damages; and "all other relief the Court deem[ed] just and equitable."[9]

The creditors opposed the motion. They also filed a proof of claim, asserting a security interest in the Corvette in the amount of $28,773.[10]

iii. The Bankruptcy Court's Decision

Following a two-day hearing, the Bankruptcy Court issued a written decision and order granting the motion in part and denying it in part. The Bankruptcy Court, *inter alia*, granted Denby-Peterson's request for turnover and thus ordered the creditors to return the Corvette to Denby-Peterson within seven days, but denied Denby-Peterson's sanctions request.

The Bankruptcy Court held, *inter alia*, that (1) the creditors must return the Corvette under the Bankruptcy Code's turnover provision in Section 542(a),[11] and (2) the creditors did not violate the automatic stay by retaining possession of the Corvette ***121** upon receiving notice of the bankruptcy filing. Thus, the Bankruptcy Court determined that the creditors were not liable for sanctions based on an alleged violation of the automatic stay.

In reaching its holdings, the Bankruptcy Court found that Denby-Peterson had an equitable interest in the Corvette at the time of the bankruptcy filing, and therefore, the Corvette was property of the estate subject to turnover.[12]

Next, the Bankruptcy Court considered whether the creditors violated the automatic stay by failing to return the Corvette after learning of the bankruptcy filing. It identified the split among our sister circuits on this issue, pointing out that the Second, Seventh, Eighth, and Ninth Circuits ("the majority") have held that the Bankruptcy Code's turnover provision requires immediate turnover of estate property that was seized pre-petition and that failure to do so violates the automatic stay.[13] However, the Tenth and D.C. Circuits ("the minority") "have instead held that a creditor does not violate the stay in regard to property of the estate if it merely maintains the status quo."[14] The Bankruptcy Court noted that the minority was critical of the majority's rule that Section 542(a)'s turnover provision "is self-effectuating" because "it does not allow for the possibility of defenses to turnover."[15]

The Bankruptcy Court ultimately adopted the minority position, describing it as "particularly persuasive"[16] and pointing out that "[f]rom the inception of this case there was an issue regarding exactly what ... [Denby-Peterson]'s interest in ... [the Corvette] was."[17] Accordingly, the Bankruptcy Court concluded that the creditors did not violate the automatic stay by failing to turn over the Corvette to Denby-Peterson "prior to adjudication of ... [her] right to redeem the [Corvette]," and thus, sanctions were not warranted.[18]

C. Denby-Peterson's Appeal to the District Court

Denby-Peterson appealed the Bankruptcy Court's order denying her sanctions request. Similar to the Bankruptcy Court, the District Court found "the minority position more persuasive."[19] The District Court thus affirmed the Bankruptcy Court's order denying Denby-Peterson's sanctions request.[20]

***122** [1]Denby-Peterson now appeals to our Court.[21] Because the creditors are not participating in this appeal, we appointed Craig Goldblatt as *amicus curiae* to defend the judgment of the District Court.[22]

II.

On appeal, Denby-Peterson renews her argument that the creditors violated the automatic stay by not returning the repossessed Corvette upon learning of the bankruptcy filing. To provide context for the issue before us, we will discuss the Bankruptcy Code's automatic stay before addressing the merits of this appeal.

Under Section 362 of the Bankruptcy Code, entitled "[a]utomatic stay," the filing of a bankruptcy petition automatically triggers a stay.[23] Of particular relevance to this appeal, subsection (a)(3) provides that a bankruptcy petition "operates as a stay, applicable to all entities, of ... any act to obtain possession of property of the estate ... or to exercise control over property of the estate."[24] Property of the bankruptcy estate, in turn, generally includes "all legal or equitable interests of the debtor in property as of the commencement of the case,"[25] "wherever located and by whomever held."[26]

[2] [3]The automatic stay imposed by the Bankruptcy Code has a "twofold" purpose:

> (1) to protect the debtor, by stopping all collection efforts, harassment, and foreclosure actions, thereby giving the debtor a respite from creditors and a chance 'to attempt a repayment or reorganization plan or simply be relieved of the financial pressures that drove him [or her] into bankruptcy;' and (2) to protect 'creditors by preventing particular creditors from acting unilaterally in self-interest to obtain payment from a debtor to the detriment of other creditors.'[27]

***123** In furtherance of the automatic stay's overarching purpose, Section 362(a)(3) "prevent[s] dismemberment of the estate," and enables an "orderly" distribution of the debtor's assets.[28]

[4] [5]The consequences for willful violations of the automatic stay are set forth in Section 362(k) which provides that, subject to one exception, "an individual injured by any willful violation" of the automatic stay is entitled to "actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages."[29] We have explained that "[i]t is a willful violation of the automatic stay when a creditor violates the stay with knowledge that the bankruptcy petition has been filed. Willfulness does not require that the creditor intend to violate the automatic stay provision, rather it requires that the acts which violate the stay be intentional."[30]

III.

With the foregoing statutory background in mind, we now turn our attention to the issue of first impression before our Court: whether, upon receiving notice of a bankruptcy petition, a secured creditor violates the automatic stay by maintaining possession of collateral that it lawfully repossessed pre-petition. Specifically, we must decide whether the creditors' failure to return the Corvette to Denby-Peterson upon learning of her bankruptcy filing was a violation of the automatic stay.[31]

As we previously acknowledged, there is a circuit split on this issue, which we have not yet joined. Under the majority position, held by the Second, Seventh, Eighth, Ninth, and Eleventh Circuits, a secured creditor, upon learning of the bankruptcy filing, must return the collateral to the debtor and failure to do so violates the automatic stay.[32] However, both the Tenth and D.C. Circuits disagree with the majority's interpretation of the automatic stay provision.[33] Under their view, a secured creditor is not obligated to return the collateral to the debtor until the debtor obtains a court order from the Bankruptcy Court requiring the creditor to do so. Thus, according to the minority, a creditor does not violate the automatic stay by retaining possession of the collateral after being notified of the bankruptcy filing.

Here, Denby-Peterson urges us to adopt the view of the majority of our sister circuits, advancing two theories in support of her position that the creditors violated the automatic stay. First, she maintains that the creditors' failure to return the Corvette violated the plain language of Section 362(a)(3)'s automatic stay provision by being "an[ ] act ... to exercise control over ***124** property of the estate."[34] Second, Denby-Peterson asserts that Section 362(a)(3)'s automatic stay provision and Section 542(a)'s turnover provision operate together such that a violation of the turnover provision results in a violation of the automatic stay. Thus, according to Denby-Peterson, the creditors were required to immediately turn over the Corvette, and by not doing so, they violated the automatic stay. For the reasons that follow, we are not persuaded by those arguments and thus hold that the creditors in this case did not violate the automatic stay. In so holding, we join the minority of our sister circuits.

IV.

A.

[6]We begin our interpretation of Section 362(a)(3) of the Bankruptcy Code "where all such inquiries must begin: with the language of the statute itself."[35]

[7] [8] [9]In examining the Bankruptcy Code, we are not "guided by a single sentence or member of a sentence, but look to the provisions of the whole law, and to its object and policy."[36] Thus, to determine the plainness or ambiguity of Section 362(a)(3)'s statutory language, in addition to considering the statutory language itself, we may also engage in "a studied examination of the statutory context."[37] If we ultimately determine that a provision "is clear and unambiguous, [we] must simply apply it."[38] However, if we find that a provision is ambiguous,[39] "we then turn to pre-Code practice and legislative history to find meaning."[40]

With these principles of construction in mind, we will now examine the language of Section 362(a)(3). To reiterate, Section 362(a)(3) provides, in relevant part, that the filing of a bankruptcy petition "operates as a stay ... of ... any act to ... exercise control over property of the estate."[41] According to Denby-Peterson, under the plain language of the automatic stay, a creditor who does not turn over property of the estate after a debtor demands its return exercises control over that property, thereby violating the automatic stay. While we agree that Section 362(a)(3) is unambiguous, we decline to hold that a plain reading of that Section compels the conclusion that the creditors in this case violated the automatic stay by failing to turn over the Corvette to Denby-Peterson.

***125** [10]The operative terms and phrases of Section 362(a)(3) are "stay," "act," and "exercise control." Because the Bankruptcy Code does not define them, we must look to their ordinary meanings.[42]

We start with the meaning of the word "stay." *Black's Law Dictionary* defines "stay" as "[t]he postponement or halting of a proceeding, judgment, or the like" or "[a]n order to suspend all or part of a judicial proceeding or a judgment resulting from that proceeding."[43] Moreover, *Webster's Third New International Dictionary* defines "stay" as a noun (as it is used in Section 362) as: (1) "a bringing to a stop," (2) "the action of halting," and (3) "the state of being stopped."[44]

Next, the noun "act" means, among other things, "[s]omething done; the action or process of achieving this."[45] *Black's Law Dictionary* similarly defines "act," in relevant part, as "[s]omething done or performed," or "[t]he process of doing or performing."[46]

Finally, as to the phrase "exercise control," we will separately consider the verb "exercise" and the noun "control." The relevant definition of "exercise" is "[t]o put in action or motion."[47] *Webster's Third New International Dictionary* also defines "exercise," in relevant part, as "to ... make effective in action."[48] Additionally, "control," as a noun, means, among other things, "[t]he fact or power of directing and regulating the actions of people or things; direction, management; command."[49]

[11] [12]From these definitions, we gather that Section 362(a)(3) prohibits creditors from taking any affirmative act to exercise control over property of the estate. As correctly pointed out by the District Court, the statutory language "is prospective in nature ... the *exercise* of control is not stayed, but the *act to* exercise control is stayed."[50] Therefore, we agree with the minority position held by two of our sister courts—the text of Section 362(a)(3) requires a post-petition affirmative ***126** act to exercise control over property of the estate.[51]

B.

[13]Here, a post-petition affirmative act to exercise control over the Corvette is not present. The creditors repossessed the Corvette before Denby-Peterson had filed for bankruptcy. Accordingly, pre-bankruptcy petition, the creditors had possession and control of the Corvette, and post-bankruptcy petition, the creditors merely passively retained that same possession and control. Although the creditors exercised control over the Corvette by keeping it in their possession after learning of the bankruptcy filing, the requisite post-petition affirmative "act ... to exercise control over" the Corvette is not present in this case.[52] An application of the plain language of the statute to the facts of this case thus shows that the creditors did not violate the automatic stay.[53]

[14]Our conclusion is bolstered by the legislative purpose and underlying policy goals of the automatic stay. It is well-established that one of the automatic stay's primary purposes is " '*to maintain the status quo* between the debtor and [his] creditors, thereby affording the parties and the [Bankruptcy] Court an opportunity to appropriately resolve competing economic interests in an orderly and effective way.' "[54] Here, the creditors had

possession of the Corvette both before and after the bankruptcy filing. Thus, by keeping possession of the Corvette after learning of the bankruptcy filing, the creditors preserved the pre-petition status quo. To hold that such a retention of possession violates the automatic stay would directly contravene the status-quo aims of the automatic stay.

In sum, the plain language of the automatic stay provision in § Section 362(a)(3) and the automatic stay's legislative purpose indicate that Congress did not intend passive retention to qualify as "an act to ... exercise control over property of the estate."[55] In light of our interpretation of § Section 362(a)(3), we thus hold that the creditors did not engage in a post-petition "act to ... exercise control" over the Corvette and thus did not violate the automatic stay.[56]

C.

Denby-Peterson, on the other hand, disregards the automatic stay's legislative purpose and instead relies on § Section 362(a)(3)'s scarce legislative history to support her position. She maintains that her ***127** "plain language reading of § Section 362 is bolstered by the 1984 Amendments to the Bankruptcy Code."[57] We disagree.

[15]Given § Section 362(a)(3)'s unambiguous text, we need not resort to legislative history to uncover its meaning.[58] In any event, we point out that the relevant legislative history fails to shed light on Congress's intent behind the 1984 addition of the "exercise control over property of the estate" clause. The legislative history reveals that, as originally enacted in 1978, § Section 362(a)(3) only stayed "any act to obtain possession of property of the estate or of property from the estate."[59] Thereafter, in 1984, Congress amended § Section 362(a)(3) by inserting the "or to exercise control over property of the estate" clause.[60] Congress, however, "gave no explanation of its intent."[61]

Denby-Peterson nevertheless urges us to follow the Seventh Circuit's view that "the mere fact that Congress expanded the provision to prohibit conduct above and beyond obtaining possession of an asset suggests that it intended to include conduct by creditors who seized an asset pre-petition."[62] We will not do so because the legislative history would be pertinent only to the extent that Congress clearly expressed an intent to interpret § Section 362(a)(3) contrary to its plain language. Here, Congress did not express any intent, much less an intent to include creditors' passive retention of property that was seized pre-petition.[63] Moreover, even assuming that § Section 362(a)(3) is ambiguous, thereby warranting consideration of legislative history, the legislative history's silence provides no guidance regarding Congress's rationale for adding the "or to exercise control over property of the estate" clause. Accordingly, the interpretation that Denby-Peterson urges us to adopt is unsupported by § Section 362(a)(3)'s legislative history as well as its statutory language.

V.

We now consider Denby-Peterson's final attempt to overcome the plain language of § Section 362(a)(3). Denby-Peterson asserts that § Section 362's automatic stay should be read in conjunction with Section 542(a)'s allegedly self-effectuating turnover provision. We are not persuaded.

Under Section 542(a), creditors who are in possession of property of the estate ***128** must turn over such property to the debtor "during the [Bankruptcy] case."[64] The turnover provision states, in relevant part, that "an entity, other than a custodian," such as a creditor,[65]

> in possession, custody, or control, during the case, of property that the [debtor] may use, sell, or lease under section 363 ..., or that the debtor may exempt under section 522 ... shall deliver to the [debtor], and account for, such property or the value of such property, unless such property is of inconsequential value or benefit to the estate.[66]

Denby-Peterson contends that we should join the majority of our sister circuits and conclude that: (1) Section 542(a)'s turnover provision is self-executing; (2) therefore, the creditors had a mandatory duty to return the Corvette to Denby-Peterson upon receiving notice of the bankruptcy filing; and (3) when the creditors rejected Denby-Peterson's demand for turnover, they violated the automatic stay.[67] We respectfully disagree with the

majority. For the following reasons, we conclude that Denby-Peterson's threefold argument is unpersuasive.

A.

[16] [17]First, in our view, Section 542(a)'s turnover provision is not self-executing; in other words, a creditor's obligation to turn over estate property to the debtor is not automatic.[68] Rather, the turnover provision requires the debtor to bring an adversary proceeding in Bankruptcy Court in order to give the Court the opportunity to determine whether the property is subject to turnover under Section 542(a).

[18]Both the Federal Rules of Bankruptcy Procedure and the text of the turnover provision support our conclusion by demonstrating that the debtor's right to turnover is subject to substantive and procedural requirements that must be evaluated by the Bankruptcy Court.[69] It is only after the Bankruptcy Court determines whether those requirements are met that the debtor's right to turnover is triggered.

i.

[19]We start with the procedure behind turnover. Denby-Peterson argues that a creditor's duty to turn over collateral is automatically triggered when a creditor receives notice of the bankruptcy petition. ***129** In other words, procedurally, says Denby-Peterson, all the debtor must do to initiate turnover is file a bankruptcy petition and notify the creditor of the filing. However, Federal Rule of Bankruptcy Procedure 7001(1) explicitly indicates otherwise. Under that Rule, the debtor must bring a request for turnover in an adversary proceeding before a Bankruptcy Court.[70] Accordingly, contrary to Denby-Peterson's claim, the debtor must not only file a bankruptcy petition, he or she must also initiate a turnover proceeding by (1) filing a complaint in Bankruptcy Court and (2) serving a creditor with a copy of the complaint.[71] This procedural requirement negates any possibility that a creditor's duty to turn over property is automatic.[72]

ii.

Moreover, the plain language of the Bankruptcy Code's turnover provision also shows that the provision is not self-effectuating. Section 542(a) provides that only property of the estate, as defined in Section 541, that is either (1) "property that the [debtor] may use, sell, or lease under section 363" or (2) property "that the debtor may exempt under section 522," is subject to turnover.[73] The turnover provision also explicitly limits the right to turnover to estate property that (1) is in the possession, custody or control of a creditor, and (2) is not "of inconsequential value or benefit to the estate."[74] Thus, on its face, the turnover provision includes numerous explicit conditions that must be satisfied before a property is subject to turnover.

[20]In the case before us today, Denby-Peterson asks us to essentially ignore Section 542(a)'s statutory prerequisites and find that a creditor must immediately turn over any collateral that a debtor deems to be subject to turnover. We will not do so. We further note that mandating creditors to automatically turn over any property that the debtor deems worthy of turnover would allow debtors to temporarily strip creditors of their rights to assert affirmative defenses such as laches,[75] or to ***130** claim that the property is not property of the estate. While it is true that creditors would presumably be able to assert these defenses in Bankruptcy Court after turning over the collateral to the debtor, we do not read the turnover provision as placing the onus on creditors to surrender the collateral and then immediately file a motion in Bankruptcy Court asserting their rights.

In sum, in light of the plain language of Section 542(a)'s turnover provision, and the procedural and substantive requirements underlying turnover, it would be illogical for us to interpret the turnover provision as imposing an automatic duty on creditors to turn over collateral to the debtor upon learning of a bankruptcy petition. We therefore reject Denby-Peterson's claim that the turnover provision is self-effectuating.[76] Instead, we conclude that the turnover provision is effectuated by virtue of judicial action. The Chapter 13 debtor must first seek court intervention, such as through an adversary proceeding, and then the Bankruptcy Court, not the debtor, must ultimately decide whether certain property must be turned over to the debtor.[77]

B.

[21]Additionally, we point out that our interpretation of the turnover provision is not changed by the turnover provision's use of the phrase "shall deliver to the [debtor]."[78] As argued by Denby-Peterson, it may well be so that the word "shall" ***131** strongly suggests that turnover is mandatory.[79] However, turnover is mandatory only in the context of an adversary proceeding presided over by the Bankruptcy Court. Under Rule 7001(1), the debtor must bring an adversary proceeding seeking turnover. True, the turnover provision states: "shall deliver," but the question before us is when must a creditor deliver? The answer is when the Bankruptcy Court says so in the context of an adversary proceeding brought under Rule 7001(1). We view the statutory and procedural framework as: (1) the Chapter 13 debtor must seek court relief, such as by initiating an adversary proceeding requesting turnover; (2) the Bankruptcy Court then determines whether the property is subject to turnover; and (3) if it is, in accordance with that determination, the Bankruptcy Court issues a court order compelling a creditor to turn over property to the debtor.

Our conclusion is further supported by the United States Supreme Court's reasoning in *Citizens Bank of Maryland v. Strumpf*.[80] In that case, the Court considered the interplay between the automatic stay[81] and the turnover provision in Section 542(b). Notably, notwithstanding the word "shall" in that turnover provision, the *Strumpf* Court did not interpret the provision as self-executing.

Section 542(b)'s turnover provision states: "an entity that owes a debt that is property of the estate ... *shall* pay such debt to ... the trustee."[82] However, an entity is excused from that obligation "to the extent that such debt may be offset under section 553 ... against a claim against the debtor."[83] Thus, similar to the turnover provision at issue in this case, the turnover provision in subsection (b) includes the word "shall" as well as a defense to turnover.

In *Strumpf*, the Supreme Court held that a bank's temporary withholding of funds in a debtor's bank account, pending resolution of the bank's setoff right,[84] did not violate the automatic stay. In reaching that holding, the Court reasoned, among other things, that interpreting Section 542(b)'s turnover provision as self-executing would "eviscerate" the provision's exceptions to the duty to pay.[85] Here, we likewise decline to interpret Section 542(a)'s "shall deliver" clause in a way that would disregard the provision's explicit defenses.[86]

***132 C.**

[22]Even assuming the turnover provision is self-executing, as pointed out by the Tenth Circuit, "there is still no textual link between [Section] 542 and [Section] 362."[87] The language of the automatic stay provision and the turnover provision do not refer to each other. The absence of an express textual link between the two provisions indicates that they should not be read together, so violation of the turnover provision would not warrant sanctions for violation of the automatic stay provision.

VI.

Guided by the plain language of the Bankruptcy Code's automatic stay and turnover provisions, the legislative purpose and policy goals of the automatic stay, and the reasoning of the Supreme Court and our two sister circuits, we hold that a creditor in possession of collateral that was repossessed before a bankruptcy filing does not violate the automatic stay by retaining the collateral post-bankruptcy petition.

We will thus affirm the order of the District Court affirming the Bankruptcy Court's order denying Denby-Peterson's request for sanctions.

All Citations

941 F.3d 115, 67 Bankr.Ct.Dec. 236, Bankr. L. Rep. P 83,459

Footnotes

1 H.R. Res. 970, 110th Cong. (2008).

2 *See* 11 U.S.C. §§ 362(a)(3), (k).

3 *Id.* § 362(a)(3).

4 For the sake of brevity, we will collectively refer to Pine Valley Motors and NU2U Auto World as "the creditors."

5 The retail installment contract's "repossession" clause states, in relevant part: "[i]f you are in default, we may take the vehicle from you after we give you any notice required by law." Bankr. Petition No. 17-15532-ABA, Doc. No. 17-5 at 3. "Default," in turn, is defined as including, among other things: (1) "failure to pay any installment when due"; (2) "failure to perform or breach of any section of th[e] contract"; and (3) "failure to obtain and maintain the insurance required by th[e] contract." *Id.*
Before the Bankruptcy Court, the parties disputed the date of repossession. Denby-Peterson claimed that the Corvette was repossessed on March 13, 2017, while the creditors claimed that it was repossessed one month earlier, in February 2017. All parties nevertheless agree that the repossession occurred before Denby-Peterson filed for bankruptcy.

6 11 U.S.C. § 362(a)(3).

7 Bankr. Petition No. 17-15532-ABA, Doc. No. 5-3 at 3. *See* 11 U.S.C. § 362(k)(1).

8 The motion was entitled "motion for return of repossessed auto and seeking sanctions against creditor for violat[ing] the automatic stay." Bankr. Petition No. 17-15532-ABA, Doc. No. 5 (original in uppercase and bold).

9 Bankr. Petition No. 17-15532-ABA, Doc. No. 5-7 at 3. *See* 11 U.S.C. § 362(k)(1) (stating, in relevant part, that "an individual injured by any willful violation of a stay ... shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages"); *see also* *In re Lansaw*, 853 F.3d 657, 667 (3d Cir. 2017), *cert. denied sub nom. Zokaites v. Lansaw*, —— U.S. ——, 138 S. Ct. 1001, 200 L.Ed.2d 253 (2018) ("expressly concluding that 'actual damages' under § 362(k)(1) include damages for emotional distress resulting from a willful violation of the automatic stay.").

10 The retail installment contract's "security interest" clause provides that (1) Denby-Peterson gave the creditors a security interest in, *inter alia*, the Corvette, and (2) the security interest "cover[ed] all amounts [she] owe[d]." Bankr. Petition No. 17-15532-ABA, Doc. No. 17-5 at 3.

11 *See* 11 U.S.C. § 542(a) (stating, in relevant part, that "an entity, other than a custodian, in possession, custody, or control, during the case, of property that the [debtor] may use, sell, or lease under section 363 of this title ... shall deliver to the [debtor], and account for, such property or the value of such property, unless such property is of inconsequential value or benefit to the estate").

12 *See id.* § 541(a) (defining "property of the estate," in relevant part, as "all legal or equitable interests of the debtor in property as of the commencement of the case").

13 *See* *In re Fulton*, 926 F.3d 916 (7th Cir. 2019); *In re Weber*, 719 F.3d 72 (2d Cir. 2013); *In re Del Mission Ltd.*, 98 F.3d 1147 (9th Cir. 1996); *In re Knaus*, 889 F.2d 773 (8th Cir. 1989); *see also* *In re Rozier*, 376 F.3d 1323, 1324 (11th Cir. 2004) (per curiam) (holding that the "district court did not err by affirming the bankruptcy court's order holding [the creditor] in willful contempt of the automatic stay ... by refusing to return the vehicle").

14 *In re Denby-Peterson*, 576 B.R. 66, 80 (Bankr. D.N.J. 2017) (citing *In re Cowen*, 849 F.3d 943 (10th Cir. 2017); *United States v. Inslaw, Inc.*, 932 F.2d 1467 (D.C. Cir. 1991)).

15 *Denby-Peterson*, 576 B.R. at 82.

16 *Id.*

17 *Id.*

18 *Id.* at 83.

19 *Denby-Peterson v. Nu2u Auto World*, 595 B.R. 184, 190 (D.N.J. 2018).

20 While Denby-Peterson's appeal to the District Court was pending, the Bankruptcy Court dismissed the underlying bankruptcy case based on Denby-Peterson's failure to make all required pre-confirmation payments to the Trustee. Before addressing the merits of the appeal, the District Court concluded that Denby-Peterson's appeal was not mooted by the dismissal because the automatic-stay-related issue "is an ancillary issue not closely intertwined with the underlying bankruptcy." *Denby-Peterson*, 595 B.R. at 188.

21 The District Court had jurisdiction under 28 U.S.C. § 158 (a). We have jurisdiction under 28 U.S.C. § 158(d)(1). Because the District Court acted as an appellate court, we review its determinations *de novo*. *In re Bocchino*, 794 F.3d 376, 379 (3d Cir. 2015). We review the legal conclusions of the Bankruptcy Court *de novo* and its factual determinations for clear error. *Id.* at 380.
Generally, "[t]he imposition or denial of sanctions is subject to abuse-of-discretion review." *In re Miller*, 730 F.3d 198, 203 (3d Cir. 2013). We have not, however, addressed our standard of review for the imposition or denial of sanctions for violations of the automatic stay. We nevertheless need not do so now given that (1) the Bankruptcy Court denied sanctions based on its conclusion that the creditors did not violate the automatic stay, and (2) we now hold that both the Bankruptcy Court and the District Court correctly concluded that there was no such violation.

22 We thank Mr. Goldblatt for his excellent briefing and oral advocacy in this matter.

23 11 U.S.C. § 362.

24 *Id.* § 362(a)(3). *See* H.R. Rep. No. 95-595, at 340 (1977) (stating that "[s]ubsection (a) defines the scope of the automatic stay, by listing the acts that are stayed by the commencement of the case").

25 11 U.S.C. § 541(a)(1).

26 *Id.* § 541(a). In a Chapter 13 case, such as this case, the concept of property of the estate is broader. *See id.* § 1306 (a)(1) (providing that the Chapter 13 estate includes, in addition to the property specified in Section 541, property "that the debtor acquires after the commencement of the bankruptcy case" but before the case is either closed, dismissed, or converted).

27 *Constitution Bank v. Tubbs*, 68 F.3d 685, 691 (3d Cir. 1995) (quoting *Maritime Elec. Co. v. United Jersey Bank*, 959 F.2d 1194, 1204 (3d Cir. 1991)). *See* *Taggart v. Lorenzen*, —— U.S. ——, 139 S. Ct. 1795, 1804, 204 L.Ed.2d 129 (2019) (explaining that the automatic stay "aims to prevent damaging disruptions to the administration of a bankruptcy case in the short run"); *Inslaw*, 932 F.2d at 1473 ("The object of the automatic stay provision is essentially to solve a collective action problem—to make sure that creditors do not destroy the bankrupt estate in their scramble for relief.").

28 H.R. Rep. No. 95-595, at 341.

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29 11 U.S.C. § 362(k)(1). *See* *id.* § 362(k)(2) (providing a "good faith" exception to Section 362(k)(1)).

30 *In re Lansdale Family Rests., Inc.*, 977 F.2d 826, 829 (3d Cir. 1992) (internal citations omitted).

31 It is undisputed here that the creditors repossessed the Corvette before Denby-Peterson had filed for bankruptcy and that the Corvette was property of Denby-Peterson's bankruptcy estate.

32 *See* *Fulton*, 926 F.3d 916; *Weber*, 719 F.3d 72; *Del Mission*, 98 F.3d 1147; *Knaus*, 889 F.2d 773; *Rozier*, 376 F.3d 1323.

33 *See* *Cowen*, 849 F.3d 943; *Inslaw*, 932 F.2d 1467.

34 11 U.S.C. § 362(a)(3).

35 *Ransom v. FIA Card Servs., N.A.*, 562 U.S. 61, 69, 131 S.Ct. 716, 178 L.Ed.2d 603 (2011) (internal quotation marks omitted).

36 *Kelly v. Robinson*, 479 U.S. 36, 43, 107 S.Ct. 353, 93 L.Ed.2d 216 (1986) (internal quotation marks omitted). *See* *In re Price*, 370 F.3d 362, 369 (3d Cir. 2004) (emphasizing that "in interpreting the Bankruptcy Code, the Supreme Court has been reluctant to declare its provisions ambiguous, preferring instead to take a broader, contextual view"); *Official Comm. of Unsecured Creditors of Cybergenics Corp., ex rel. Cybergenics Corp. v. Chinery*, 330 F.3d 548, 559 (3d Cir. 2003) ("Statutory construction is a holistic endeavor, and this is especially true of the Bankruptcy Code." (quotation marks, alterations and citations omitted)).

37 *Price*, 370 F.3d at 369.

38 *In re KB Toys Inc.*, 736 F.3d 247, 251 (3d Cir. 2013) (citing *Roth v. Norfalco L.L.C.*, 651 F.3d 367, 379 (3d Cir. 2011)).

39 *See* *Price*, 370 F.3d at 369 (explaining that "a provision is ambiguous when, despite a studied examination of the statutory context, the natural reading of a provision remains elusive").

40 *In re Friedman's Inc.*, 738 F.3d 547, 554 (3d Cir. 2013).

41 11 U.S.C. § 362(a)(3).

42 *See* *Lamar, Archer & Cofrin, LLP v. Appling*, —— U.S. ——, 138 S. Ct. 1752, 1759, 201 L.Ed.2d 102 (2018).

43 Stay, *Black's Law Dictionary* (11th ed. 2019). Black's Law Dictionary further defines "automatic stay" as "[a] bar to all judicial and extrajudicial collection efforts against the debtor or the debtor's property, subject to specific statutory exceptions." *Id.*

44 *Webster's Third New International Dictionary* 2231 (1993); *see* Stay, Oxford English Dictionary Online, https://www.oed.com/view/Entry/189408?rskey=uCJBz6& result=3& isAdvanced=false (including, among its definitions of "stay," "[t]he action of stopping or bringing to a stand or pause") (last visited Aug. 15, 2019).

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45 Act, Oxford English Dictionary Online, https://www.oed.com/view/Entry/1888?rskey=eprROF& result=4 (last visited Aug. 15, 2019).

46 Act, *Black's Law Dictionary* (11th ed. 2019).

47 Exercise, Oxford English Dictionary Online, https://www.oed.com/view/Entry/66089?rskey=QNVdyF& result=2& isAdvanced=false (last visited Aug. 15, 2019); *see* Exercise, *Black's Law Dictionary* (11th ed. 2019) (describing "exercise" as meaning, in relevant part, "[t]o make use of; to put into action").

48 *Webster's Third New International Dictionary* 795.

49 Control, Oxford English Dictionary Online, https://www.oed.com/view/Entry/40562?rskey=qZlHZj& result=1 (last visited Aug. 15, 2019); *see* Control, *Black's Law Dictionary* (11th ed. 2019) (identifying "the power or authority to manage, direct, or oversee" as one of the definitions of "control").

50 *Denby-Peterson*, 595 B.R. at 190.

51 *See* *Cowen*, 849 F.3d at 949 (concluding that Section 362(a)(3) "stays entities from *doing* something to ... exercise control over the estate's property"); *Inslaw*, 932 F.2d at 1474 ("The automatic stay, as its name suggests, serves as a restraint only on acts to gain possession or control over property of the estate.").

52 11 U.S.C. § 362(a)(3).

53 Denby-Peterson's characterization of the creditors' post-petition behavior as a refusal to return the Corvette upon request does not alter our conclusion. A creditor's refusal to comply with a debtor's turnover request is not an affirmative act; rather, it is inaction. Denby-Peterson's attempt to reframe creditors' failure to act as an affirmative act is unavailing as it does not alter the passive nature of the creditors' post-petition role in relation to the Corvette. *See* *Nat'l Fed'n of Indep. Bus. v. Sebelius*, 567 U.S. 519, 555, 132 S.Ct. 2566, 183 L.Ed.2d 450 (2012) (recognizing "the distinction between doing something and doing nothing").

54 *Taylor v. Slick*, 178 F.3d 698, 702 (3d Cir. 1999) (quoting *Zeoli v. RIHT Mortg. Corp.*, 148 B.R. 698, 700 (D.N.H. 1993)) (emphasis and alteration in original).

55 11 U.S.C. § 362(a)(3).

56 *Id.*

57 Appellant's Br. at 13.

58 *See Doe v. Hesketh*, 828 F.3d 159, 167 (3d Cir. 2016).

59 Bankruptcy Reform Act of 1978, Pub. L. 95-598, § 362 (a)(3), 92 Stat. 2549, 2570 (1978).

60 Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 362(a)(3), 98 Stat. 333, 371 (1984).

61 *In re Young*, 193 B.R. 620, 623 (Bankr. D.D.C. 1996).

62 *Thompson v. Gen. Motors Acceptance Corp., LLC*, 566 F.3d 699, 702 (7th Cir. 2009). *See* *Fulton*, 926 F.3d at 923 (declining to overrule *Thompson* and reiterating that the amendment "suggested

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congressional intent to make the stay more inclusive by including conduct of 'creditors who seized an asset pre-petition' " (quoting *Thompson*, 566 F.3d at 702)); *see also* *Weber*, 719 F.3d at 80 (describing the amendment as a "significant textual enlargement" that supports the view that "Congress intended to prevent creditors from retaining property of the debtor in derogation of the bankruptcy procedure ... without regard to what party was in possession of the property in question when the petition was filed").

63 *See* *Consumer Prod. Safety Comm'n v. GTE Sylvania, Inc.*, 447 U.S. 102, 108, 100 S.Ct. 2051, 64 L.Ed.2d 766 (1980) ("Absent a clearly expressed legislative intention to the contrary, th[e] [statutory] language must ordinarily be regarded as conclusive.").

64 11 U.S.C. § 542(a). In a Chapter 13 case, such as this case, the debtor retains control over property of the estate. *See id.* § 1306(b). Accordingly, a Chapter 13 trustee does not take possession or liquidate property of the estate, except with respect to money collected for the purpose of making distributions to creditors under a plan. *See id.* §§ 1302, 1303.

65 *See id.* § 101(10)(A).

66 *Id.* § 542(a). *See id.* § 1303 (providing the Chapter 13 debtor "the rights and powers of a trustee under sections 363(b), 363(d), 363(e), 363(f), and 363(l)"); *id.* § 1306(b) (stating, in relevant part, that "the [Chapter 13] debtor shall remain in possession of all property of the estate").

67 *See* *Fulton*, 926 F.3d 916; *Weber*, 719 F.3d 72; *Del Mission*, 98 F.3d 1147; *Knaus*, 889 F.2d 773.

68 *But see* *Fulton*, 926 F.3d at 924 (reaffirming that Section 362(a)(3) "becomes effective immediately upon filing the petition and is not dependent on the debtor first bringing a turnover action"); *Weber*, 719 F.3d at 79 ("Section 542 requires that any entity in possession of property of the estate deliver it to the trustees, without condition or any further action: the provision is self-executing." (internal quotation marks omitted)).

69 *See* 4 Norton Bankr. L. & Prac. 3d § 62:3 (2019) (stating that "several [Bankruptcy] Code provisions play a role in determining whether a turnover will be ordered pursuant to Code § 542(a)").

70 *See* Fed. R. Bankr. P. 7001(1) (identifying, in relevant part, "a proceeding to recover money or property" as an adversary proceeding).

71 "An adversary proceeding is essentially a self-contained trial—still within the original bankruptcy case—in which a panoply of additional procedures apply," *In re Mansaray-Ruffin*, 530 F.3d 230, 234 (3d Cir. 2008) (citing Fed. R. Bankr. P. 7001-7087), including the requirement that a complaint must be filed to commence such a proceeding, *see* Fed. R. Bankr. P. 7003 (stating that Federal Rule of Civil Procedure 3 "applies in adversary proceedings").

72 Here, as noted by the Bankruptcy Court, Denby-Peterson did not initiate an adversary proceeding. Instead, she filed a motion for turnover entitled, in relevant part, "Motion for Return of Repossessed Auto." *Denby-Peterson*, 576 B.R. at 69.
Faced with this procedural posture, the Bankruptcy Court concluded that the parties waived their right to an adversary proceeding. *See* *In re Village Mobile Homes, Inc.*, 947 F.2d 1282, 1283 (5th Cir. 1991) ("Compliance with the requisites of an adversary proceeding may be excused by waiver of the parties."). Treating the matter as a contested motion, the Court then addressed the merits of the turnover request. This difference in the procedural mechanism used to achieve turnover does not change our conclusion because, regardless of the form, a debtor must initiate a procedural event before the Bankruptcy Court in order for turnover to occur, if applicable, under the Bankruptcy Court's supervision.

73 11 U.S.C. § 542(a).

74 *Id.*

75 *See* *In re Mushroom Transp. Co., Inc.*, 382 F.3d 325, 337 (3d Cir. 2004); *see also In re Stancil*, 473 B.R. 478, 484 (Bankr. D.D.C. 2012) ("The plain language of section 542(a) demonstrates that establishing inconsequential value or benefit to the estate is an affirmative defense to a turnover action.").

76 Denby-Peterson's reliance on the Supreme Court's decision in *United States v. Whiting Pools, Inc.* is misplaced. 462 U.S. 198, 201, 103 S.Ct. 2309, 76 L.Ed.2d 515 (1983). Contrary to Denby-Peterson's claim that *Whiting Pools* implicitly supports the proposition that the turnover provision is self-effectuating, *Whiting Pools* suggests the opposite: that the turnover provision is not self-effectuating because adequate protection can serve as a condition precedent before turnover. *See* 11 U.S.C. § 542(a) (providing that "property that the [debtor] may use, sell, or lease under section 363" may be subject to turnover); *id.* § 363(e) (stating, in relevant part, that "the court, with or without a hearing, shall prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of such interest"); *id.* § 361 (providing examples of "adequate protection").

In *Whiting Pools*, the Bankruptcy Court, not the Chapter 11 debtor, ordered the creditor to turn over property to the debtor. 462 U.S. at 201, 103 S.Ct. 2309. Moreover, it did so only "on the condition that [the Chapter 11 corporate-debtor] provide the [creditor] with specified [adequate] protection for its interests." *Id. See* *id.* at n.7 ("Pursuant to [Section 363(e) of the Bankruptcy Code], the Bankruptcy Court set the following conditions to protect the tax lien: [the debtor] was to pay the [creditor] $20,000 before the turnover occurred; [the debtor] also was to pay $1,000 a month until the taxes were satisfied; the [creditor] was to retain its lien during this period; and if [the debtor] failed to make the payments, the stay was to be lifted."). *Whiting Pools* thus suggests that turnover is required upon (1) the debtor's filing of a motion for turnover, and (2) the issuance of a court order.

77 We also note that under pre-Code practice, turnover was not viewed as self-effectuating. Before the Bankruptcy Code was enacted, a secured creditor, who had repossessed collateral pre-bankruptcy, retained possession pending the Bankruptcy Court's entry of a turnover order, *see* Ralph Brubaker, *Turnover, Adequate Protection, and the Automatic Stay (Part I): Origins and Evolution of the Turnover Power*, 33 Bankr. L. Letter No. 8, at 4-7 (Aug. 2013), and "[n]othing in the legislative history evinces a congressional intent to depart from that [pre-Code] practice." *Whiting Pools*, 462 U.S. at 208, 103 S.Ct. 2309. *See* *In re VistaCare Grp., LLC*, 678 F.3d 218, 227-28 (3d Cir. 2012) (recognizing that "courts should be 'reluctant to accept arguments that would interpret the Code ... to effect a major change in pre-Code practice,' absent at least some suggestion in the legislative history that such a change was intended" (quoting *Dewsnup v. Timm*, 502 U.S. 410, 419, 112 S.Ct. 773, 116 L.Ed.2d 903 (1992))).

78 11 U.S.C. § 542(a).

79 *See* *Alabama v. Bozeman*, 533 U.S. 146, 153, 121 S.Ct. 2079, 150 L.Ed.2d 188 (2001) ("The word 'shall' is ordinarily the language of command." (internal quotation marks omitted)); *Dessouki v. Att'y Gen. of United States*, 915 F.3d 964, 966 (3d Cir. 2019) (recognizing that "the word 'shall' imposes a mandatory requirement"); *see also* Shall, *Black's Law Dictionary* (11th ed. 2019) (defining "shall," in relevant part, as "[h]as a duty to; more broadly, is required to," and characterizing that usage as "the mandatory sense that drafters typically intend and that courts typically uphold").

80 516 U.S. 16, 116 S.Ct. 286, 133 L.Ed.2d 258 (1995).

81 As relevant to *Strumpf*, the filing of a bankruptcy petition stays "the setoff of any debt owing to the debtor that arose before the commencement of the [bankruptcy] case ... against any claim against the debtor." 11 U.S.C. § 362(a)(7).

82 *Id.* § 542(b) (emphasis added).

83 *Id.*

84 *See* *Strumpf*, 516 U.S. at 19, 116 S.Ct. 286 ("Petitioner refused to pay its debt, not permanently and absolutely, but only while it sought relief under § 362(d) from the automatic stay.").

85 *Id.* at 20, 116 S.Ct. 286.

86 *See* *Smith v. City of Jackson*, 544 U.S. 228, 233, 125 S.Ct. 1536, 161 L.Ed.2d 410 (2005) ("[W]hen Congress uses the same language in two statutes having similar purposes ... it is appropriate to presume that Congress intended that text to have the same meaning in both statutes.").

87 *Cowen*, 849 F.3d at 950.

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COVID 19 AND CHAPTER 13

CARES ACT PASSED MARCH 27, 2020

Passed by Congress in response to the COVID 19 pandemic.

Section. 4022. Foreclosure moratorium and consumer right to request forbearance.

Sec. 4023. Forbearance of residential mortgage loan payments for multifamily properties with federally backed loans.

Sec. 4024. Temporary moratorium on eviction filings. Sec. 4025. Protection of collective bargaining agreement.

CARES ACT Section 4022 provides foreclosure relief for federally backed mortgages on 1 to 4 family residential homes. Federally backed mortgages include those that are insured, owned, guaranteed, or purchased by FNMA, FHLMC, FHA or the VA. (4022(a)(2). This Act does not apply to private investors.

Section 4022(c)(2) states that a servicer of a federally backed mortgage may not initiate a foreclosure, more for a foreclosure judgment, schedule a sale or execute a foreclosure related eviction. NY state has imposed a moratorium on all evictions and foreclosures until August 20 which extends beyond the timeframe imposed by Congress.

In order to take advantage of the CARES ACT, you must demonstrate a financial hardship as a result of COVID 19. This hardship can be direct or indirect. Loss of a job, reduction in income, are examples of a direct impact. However, the hardship can result from an indirect impact as well. For example, an adult child loses their job and moves back home. While the parent's income may remain the same, the expenses have increased as the parent has to now support another individual.

MORTGAGES AND FORBEARANCES

The purpose of the forbearance is to provide short term relief to debtors. A Forbearance Plan is defined as a written agreement defining whether the Borrower may make either reduced or no monthly payments for a specified time. The Forbearance Plan provides a solution for borrowers experiencing hardships such as illness, unemployment, reduction in income, etc. Depending on the investor, different solutions will be available. Many secured creditors offer 90 to 180 day forbearances. Homeowners may request additional 180 days. During forbearance period no fees, interest, penalties shall accrue beyond the amounts borrowers are contractually obligated to pay. The period seems to extend until 12/31/20 or the emergency ends, whichever is earlier.

To receive a forbearance the debtor must contact the servicer and advise that they are experiencing a financial hardship as a result of COVID 19. No additional documentation is required. This does not preclude the trustee from requesting documentation however.

These forbearances do not waive the payments but rather provide the debtor with a period of time in which payments are not required to be made. It does not defer the payments to a future date. Payments must resume at the end of the forbearance period. Further the amount which was forborne must be repaid. A forbearance is not a modification and regular payments are required to resume at the end of the forbearance term.

Options for repayment:

1. Pay in full at end of deferment period
2. Enter into Extended Agreed Order
3. Loss Mitigation
4. Capitalization of payments or adding to end of loan

Bankruptcy Issues

1. Forbearances – Notices filed. Do we need court approval for these? We have been filing the Notices without obtaining court approval. The Southern District and Northern District have forms for these forbearances
2. Impact of Forbearances on future payment changes
   For ex. Escrow changes ..how will that be calculated, may result in escrow shortages and increased payments
3. Motions for Relief not automatically stopped. Lenders may proceed with Motions for Relief. If debtor is on forbearance a MFR will not be filed but may be filed if no repayment plan is worked out.

MODIFICATION OF CONFIRMED PLANS

1329(d)(1) – Modification of Plans Confirmed Prior to 3/27/2020

Plans confirmed prior to 3/27/2020 may be extended for 2 years provided the debtor can demonstrate a material financial hardship due directly or indirectly as a result of COVID 19.

Can a debtor add the post petition payments into the plan modification?

This provision terminates one year after the 3/27/20 so if you are intending to take advantage of this provision it must be done by 3/27/21

WHAT HAPPENS AFTER FORBEARANCE

CARES requires that the lender/servicer work with the debtor to enter into a plan to pay the arrears. This includes:

1. Loss Mitigation
2. Payment through the Chapter 13 Plan
3. Payment through an Agreed Order

REMEMBER LENDERS HAVE THE RIGHT TO FILE A MOTION FOR RELIEF AFTER THE FORBEARANCE SO IT IS IMPORTANT TO WORK OUT SOME TYPE OF REPAYMENT PRIOR TO THE FORBEARANCE PERIOD ENDS.

SEC. 4022. FORECLOSURE MORATORIUM AND CONSUMER RIGHT TO REQUEST FORBEARANCE.

(a) DEFINITIONS.—In this section:

(1) COVID–19 EMERGENCY.—The term "COVID–19 emergency" means the national emergency concerning the novel coronavirus disease (COVID–19) outbreak declared by the President on March 13, 2020 under the National Emergencies Act (50 U.S.C. 1601 et seq.).

(2) FEDERALLY BACKED MORTGAGE LOAN.—The term "Federally backed mortgage loan" includes any loan which is secured by a first or subordinate lien on residential real property (including individual units of condominiums and cooperatives) designed principally for the occupancy of from 1- to 4- families that is—

(A) insured by the Federal Housing Administration under title II of the National Housing Act (12 U.S.C. 1707 et seq.);

(B) insured under section 255 of the National Housing Act (12 U.S.C. 1715z–20);

(C) guaranteed under section 184 or 184A of the Housing and Community Development Act of 1992 (12 U.S.C. 1715z–13a, 1715z–13b);

(D) guaranteed or insured by the Department of Veterans Affairs;

(E) guaranteed or insured by the Department of Agriculture;

(F) made by the Department of Agriculture; or

(G) purchased or securitized by the Federal Home Loan Mortgage Corporation or the Federal National Mortgage Association.

(b) FORBEARANCE.—

(1) IN GENERAL.—During the covered period, a borrower with a Federally backed mortgage loan experiencing a financial hardship due, directly or indirectly, to the COVID–19 emergency may request forbearance on the Federally backed mortgage loan, regardless of delinquency status, by—

(A) submitting a request to the borrower's servicer; and

(B) affirming that the borrower is experiencing a financial hardship during the COVID–19 emergency.

(2) DURATION OF FORBEARANCE.—Upon a request by a borrower for forbearance under paragraph (1), such forbearance shall be granted for up to 180 days, and shall be extended for an additional period of up to 180 days at the request of the borrower, provided that, at the borrower's request, either the initial or extended period of forbearance may be shortened.

(3) ACCRUAL OF INTEREST OR FEES.—During a period of forbearance described in this subsection, no fees, penalties, or interest beyond the amounts scheduled or calculated as if the borrower made all contractual payments on time and in full under the terms of the mortgage contract, shall accrue on the borrower's account.

(c) REQUIREMENTS FOR SERVICERS.—

(1) IN GENERAL.—Upon receiving a request for forbearance from a borrower under subsection (b), the servicer shall with no additional documentation required other than the borrower's attestation to a financial hardship caused by the COVID–19 emergency and with no fees, penalties, or interest (beyond the amounts scheduled or calculated as if the borrower made all contractual payments on time and in full under the terms of the mortgage contract) charged to the borrower in connection with the forbearance, provide the forbearance for up to 180 days, which may be extended for an additional period of up to 180 days at the request of the borrower, provided that, the borrower's request for an extension is made during the covered period, and, at the borrower's request, either the initial or extended period of forbearance may be shortened.

(2) FORECLOSURE MORATORIUM.—Except with respect to a vacant or abandoned property, a servicer of a Federally backed mortgage loan may not initiate any judicial or non-judicial foreclosure process, move for a foreclosure judgment or order of sale, or execute a foreclosure-related eviction or foreclosure sale for not less than the 60-day period beginning on March 18, 2020.

CASE SUMMARIES OF RECENT CASE DECISIONS FROM THE BANKRUPTCY COURT FOR THE EASTERN DISTRICT OF NEW YORK, CENTRAL ISLIP

Adam P. Wofse, Esq.
LaMonica Herbst & Maniscalco, LLP

Judge Alan S. Trust

1. In re Lynch, 2019 WL 4584146 (U.S. Bankr. E.D.N.Y. Sept. 20, 2019).

Court Converts Defendant's Motion to Dismiss to a Motion for Summary Judgment

This is a case that was brought by LaMonica Herbst & Maniscalco, LLP, on behalf of R. Kenneth Barnard, as Chapter 7 Trustee (the "Trustee") of the Estate of Maura E. Lynch, against Patricia M. Frank, the purchaser of the Debtor's real property located on Harbor Drive in Sag Harbor, NY. Debtor was the sole fee owner of the Harbor Drive property ("Harbor Drive") on the date the Contract of Sale was executed. The Contract of sale scheduled a closing for June 4, 2014, but it did not proceed on that date due to a stay granted to the debtor by NYS Supreme Court. The Defendant moved into the house and took possession without the consent of the Receiver or the Debtor, and she continued to be in possession of the house through March 24, 2016, at which time she closed on the purchase of Harbor Drive as the highest bidder at a public auction for the Real Property. The contract of sale did not provide Defendant with a pre-closing right of possession. The Trustee brought an adversary proceeding alleging 2 causes of action for recovery of use and occupancy by Ms. Frank of Harbor Drive for that time period of June 4, 2014 through March 24, 2016, over 1 year and 9 months, in an amount not less than $150,000.00 and 2 causes of action for disallowance of the Frank Proofs of Claims. Thereafter, Ms. Frank filed a Motion to Dismiss the Complaint, the Trustee filed an opposition to the motion, and Ms. Frank replied. Both Frank and the Trustee relied on documents that were not attached to nor incorporated into the Complaint.

Defendant asserted: (1) that the Complaint fails to allege a landlord-tenant relationship existing between the parties in connection with Ms. Frank's possession of Harbor Drive, which she asserted is a requirement for acclaim for relief for use and occupancy under NY law; and (2) the disallowance causes of action should be dismissed because Debtor's alleged breach of the contract by her action which prevented the closing from going forward pre-petition amounts to a rejection of the executory contract which allows Defendant to seek allowance of her claim under Section 502. Plaintiff argued, however, that a landlord-tenant relationship existed because Frank took possession of Harbor Drive for temporary occupancy in exchange for repairs she was making to Harbor Drive. Plaintiff asserted that Frank's request for

rejection damages was already addressed by the Court in connection with the sale of Harbor Drive in that Frank actively participated in the auction process by increasing her offer for more money, thereby waiving her claims. Judge Trust held that for the Court to consider the fact-based assertions made by both parties which are not attached to or incorporated into the Complaint, the Court must convert the Motion to Dismiss into a motion for summary judgment, and afford all parties the opportunity to present pertinent material to the motion, citing to FED. R. CIV. P .12(d); FED. R. BANKR. P. 7012(b); *Cole v. Bourke*, 2016 US Dist. LEXIS 16517 at *9-10 (E.D.N.Y. Jan. 27, 2016)("[t]he essential inquiry in determining whether it is appropriate to convert a motion to dismiss into a motion for summary judgment is whether the non-movant should reasonably have recognized the possibility that the motion might be converted into one for summary judgment or was taken by surprise and deprived of reasonable opportunity to meet facts outside the pleadings."); *In re Gadsen*, 128 B.R. 45, 48 (Bankr. EDNY 1991) (the bankruptcy court may treat a motion to dismiss as a motion for summary judgment if it gives both parties notice and a reasonable opportunity to submit affidavits and extraneous evidence so as to avoid taking a party by surprise). Judge Trust further stated that because many, but not all, of the disputes in this adversary proceeding were matters of law and not issues of fact, they may be susceptible to determination under Rule 7056 (Summary Judgment).

The parties submitted additional materials pursuant to a briefing schedule, and the summary judgment motion matter is now before the Court.

2. In re Atkinson, 2019 WL 4438963 (Bankr. E.D.N.Y. 2019)

Multiple bankruptcy filings in a short span deemed a scheme to delay, hinder or defraud.

Following Section 362(d)(4) of the Bankruptcy Code, Judge Trust concluded that the Creditor met its burden of proof showing debtor's multiple bankruptcy filings regarding real property was a scheme to hinder, delay and defraud Creditor.

Debtor filed two Chapter 7 cases in 2018 to stave off foreclosure sales of real property. In each case, the Creditor filed a motion for relief from the automatic stay, and the court granted stay relief. In the first case, the court entered a notice closing the case without Debtor receiving a discharge, due to Debtor's failure to timely file a certification of financial management course or official form 423, as required by Interim Bankruptcy Rules 1007(b)(7) and 1007(c). In Debtor's second filing, the Court granted Debtor a Chapter 7 discharge.

However, the following February, Debtor, acting *pro se*, filed for bankruptcy again, but under Chapter 13 of the Bankruptcy Code. Again the Creditor moved for stay relief but, this time also sought relief from the co-debtor stay pursuant to 11 U.S.C. § 1301(c) and in rem relief pursuant to § 362(d)(4). In support of the motion for in rem relief under § 362(d)(4), the Creditor provided to the court a Judgment of Foreclosure and Sale in favor of the Creditor from 2017. Additionally, the Creditor asserted that no payments had been made on the note in the original amount of $400,000 since 2012, and the amount outstanding had subsequently swelled to $806,069.84. The Creditor further provided that the property was worth only $400,000 and argued that each bankruptcy filing happened within approximately one week of a scheduled foreclosure sale of the property.

The Court conditionally granted the motion pursuant to 11 U.S.C. §§ 362(d)(1), (4) and 1301(c) and directed the Creditor to settle the order. The Court provided Debtor with the opportunity to file an objection to the proposed order and established that Debtor had the burden to show that Debtor could adequately protect the Creditor's interest in the Property, and that Debtor's proposed Chapter 13 plan had a viable chance of being confirmed.

Marianne DeRosa, the Chapter 13 Trustee (the "Trustee") filed a motion to dismiss Debtor's case, and the Creditor filed the notice of settlement of proposed order. The Debtor retained counsel and filed a letter in opposition to the notice of settlement along with a counter order. The Debtor did not challenge the factual allegations concerning the defaults, the loan balance, the property value, or the scheduled foreclosure sales, nor did she claim the Creditor lacked standing to seek relief to the

stay. Debtor's opposition did not address how Debtor could adequately protect the Creditor's interest in the property nor why the proposed plan was viable The sole objection made by Debtor was to granting in rem relief. The Court held a hearing on the motion to dismiss which was granted and reserved the issue of in rem relief.

In his decision, Judge Trust began by observing that Congress added Section 362(d)(4) to the Bankruptcy Code in 2005 to address perceived abuses in the bankruptcy process by repeat filers. The Creditor has the burden of proof to establish relief under Section 362(d)(4). Section 362(d)(4) provides that "the Court can Order that any and all future filings by any person or entity with an interest in the subject property will not operate as an automatic stay against the creditor and its successors and/or assigns for a period of two years after the date of the entry of such an order, if the Court finds that the filing of the bankruptcy filing 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." *Id.* at 2-3 (citing *In re Montalvo*, 416 B.R. 381, 386 (Bankr. E.D.N.Y. 2009).

The Court relied on *In re Montalvo*, which had established that "the mere timing and filing of several bankruptcy cases is an adequate basis from which a court can draw a permissible inference that the filing of a subsequent case was part of a scheme to hinder, delay, and defraud creditors." *Id* at 3; *see also Montalvo*, 416 B.R. 386. The Court also took into consideration that "[T]he extent of the efforts by a debtor to prosecute [their] bankruptcy case and '[t]he timing and sequencing of the filings' are important factors in determining whether a debtor has engaged in 'a scheme to delay, hinder, and defraud'" *Id.* at 3 (citing *See In re Richmond*, 513 B.R. 34, 38 (Bankr. E.D.N.Y. 2014)).

Judge Trust determined that the Creditor met its burden of proof. The Court took into consideration that even though multiple filings do not alone justify relief under 11 U.S.C. § 362(d)(4)(B), "had Debtor's goal been just to obtain a discharge she could have avoided a second filing by simply completing her post-petition financial management education course in her First Case or by filing after the foreclosure sale was complete and any deficiency determined." *Id.* at 3. Moreover, "Debtor has not provided evidence of any payments she made to U.S. Bank during or after any of the three bankruptcy filings, and she did not have a viable Chapter 13 plan in this case. Debtor's mortgage was nearly seven years in default, had been under a foreclosure judgment for nearly two years prior to filing this case, and the Property value was substantially under the mortgage debt." *Id.* at 3.

Therefore, Judge Trust ultimately concluded that Debtor's actions, and inactions, were indicative of a multiple case filing scheme for which Congress enacted Section 362(d)(4).

3. In re Norton, 2020 WL 717411 (Bankr. E.D.N.Y. 2020)

Scam Loan Modification Attorney Cannot Escape his Judgment Creditors

In an Order Granting Plaintiffs Motion for Summary Judgment, Judge Trust opined on whether damages awarded from a certain previous state court judgment should be deemed nondischargeable based upon collateral estoppel and/or res judicata.

In this case, Debtor voluntarily filed Chapter 7. Subsequently, the Plaintiffs filed an adversary complaint against Debtor under Section 523 of the Bankruptcy Code. Plaintiffs had previously litigated a civil suit in 2014 against Debtor. Plaintiffs alleged they were low income/middle income New York homeowners who suffered financial hardship and fell behind on mortgage payments, and that when they sought help, they became victims of false advertising and a fraudulent loan modification scheme run by Debtor. Debtor was an attorney who advertised he had an extremely high success rate, charged a fixed upfront fee between $2,500 2to $5,000, and often told clients and Plaintiffs that he anticipated his fees would end up totaling less. Upon signing up with Norton, Plaintiffs were prohibited under their retainer agreements from speaking with their lenders. Once Norton received Plaintiffs' fees, he ceased communications with them. In most cases, Norton never communicated with the lenders either, but still badgered Plaintiffs for additional fees approaching double the amounts initially charged. The state court ultimately found for the Plaintiffs after Debtor failed to comply with a Motion to Compel regarding certain withheld documents in response to a document discovery request and awarded judgment in favor of each of the Plaintiffs, aggregating $204,100.63. Judgment enforcement efforts were stayed upon the Debtor's bankruptcy filing.

Plaintiffs argued that the damages awarded to them in the Judgment were nondischargeable under Section 523(a)(2) for actual fraud and false representations, and under Section 523(a)(4) for fraud while acting in a fiduciary capacity as an attorney. After Debtor answered Plaintiffs' Complaint, Plaintiffs moved for a judgment on the pleadings ("MJP"), which the Court determined, and converted into a motion for summary judgment. Through the MJP as converted to a motion for summary judgment, Plaintiffs assert that they should prevail as a matter of law based upon collateral estoppel and/or res judicata.

The first main issue Judge Trust addressed was whether issue preclusion should be applied. The Court cited both Supreme Court Cases and Second Circuit cases which had established that Bankruptcy Courts can give preclusive effect to each other's judgments, as well as to give preclusive effect to judgments of the state courts, and vice versa. *Id.* at 3. Therefore, because Norton's liability was decided under state law, the court applied New York's rules of preclusion.

The Court then applied the rules from the 2nd Circuit in (*In re Snyder*), 939 F.3d 92 (2d Cir. 2019), which states, "[A] party seeking to invoke collateral estoppel must establish that "(1) the identical issue was raised in a previous proceeding; (2) the issue was actually litigated and decided in the previous proceeding; (3) the party had a full and fair opportunity to litigate the issue; and (4) the resolution of the issue was necessary to support a valid and final judgment on the merits." *Id.* at 4. First, the court addressed if the Plaintiffs' § 523(a)(2) claim for fraud in connection with the loan modification scam was necessarily decided in the state court action. After analyzing the allegations raised by Plaintiffs in the state court action, the court concluded that the claims did not bare an identical issue to the § 523(a)(2) false pretense claim, and did not analyze the false pretenses claim for issue preclusion purposes.

Next the Court addressed if the underlying fraud claim was actually ligated, and decided in the state court. The court concluded that the underlying issue was indeed actually litigated and decided in the state court action because judgment was entered as a result of Debtor repeatedly failing to comply with Plaintiffs' discovery requests by withholding responsive documents for nearly a year, and failing to comply with the Order to Compel, thus, qualifying as bad conduct, and the Debtor had the opportunity to participate in the underlying litigation.

Moreover, the Court determined the third and fourth elements were satisfied because Debtor had a full and fair opportunity to litigate the fraud claim and the state court's resolution of the properly pleaded fraud claim was necessary to the Judgment it entered.

Therefore, the Court concluded that the state law fraud claim and the § 523(a)(2) actual fraud claim are essentially the same and therefore collateral estoppel should apply. As such the liability established under the Judgment was deemed nondischargeable.

Judge Robert E. Grossman

4. In re Joe's Friendly Service & Son, Inc., d/b/a Thatched Cottage at the Bay, Chapter 7 case no. 14-70001-REG, Adv. Pro. 16-8035-REG (6/11/20)

Not so fast. Defendants can't have it both ways.

Judge Grossman issued this decision just a few days ago. In the above adversary proceeding filed by non-debtors Bethpage Federal Credit Union ("BFCU") and Business Services Group, LLC ("BSG") (together, the "Plaintiffs") against non-debtors the Town of Huntington, Joseph Cline, Richard Vacchio, and Terence McNally (collectively, the "Defendants"), the Defendants filed a motion seeking a determination that the Court lacked subject matter jurisdiction over the adversary proceeding. The Debtors and the Trustee (R. Kenneth Barnard) are not parties to the adversary proceeding.

Earlier in the main case, the Court approved an auction sale of substantially all of the Debtors' assets under Section 363 of the Bankruptcy Code. The assets consisted of real property together with the widely known catering hall in Centerport, New York. The approved buyer defaulted on the sale, and the Plaintiffs, as backup bidder, were required to buy the property from the bankruptcy estate. In the underlying adversary proceeding, the Plaintiffs asserted that the Defendants' "placarding" of the catering hall establishment (essentially, condemnation of the property due to alleged structural deficiencies with signage posted at the property that stated the property was "unfit for human habitation" under the Code of the Town of Huntington, without notice to the Trustee)--smack in the middle of the Trustee's sale process--contributed toward the high bidder's default. It was further asserted by the Plaintiffs that such actions by Defendants ultimately caused Plaintiffs economic loss and damages when it sold the property nearly two years later, and at a much reduced price (than the original price) and deep discount from the bank's lien.

The Plaintiffs initially brought an action for damages against Defendants in state court. The Defendants sought and achieved removal to the Bankruptcy Court. The Plaintiffs then sought to remand the case back to state court, however, a stipulation was negotiated by the parties, which was approved by the Bankruptcy Court in July 2016. The stipulation expressly provided that the Plaintiffs withdrew their remand request and that they submitted to the entry of final orders by the Bankruptcy Court. The So Ordered stipulation was not appealed and became a final non-appealable order.

Surprisingly, the Defendants later asserted that the Bankruptcy Court lacked subject matter jurisdiction! Recall that it was the Defendants who initially argued that the Bankruptcy Court had jurisdiction. It was the Plaintiffs who wanted to be in the state court forum. The Defendants voluntarily entered the Bankruptcy Court-approved stipulation consenting to its jurisdiction, which became a final order of the Bankruptcy

Court. *It is the opinion of the author of this case summary that a reading of this case and other case history reveals that the Defendants likely tried to reverse their position, unjustifiably, based upon the fact that they did not like the way the case was shaping up in the Bankruptcy Court and preferred their chances in a different forum.* The trial on the merits will, however, occur in the Bankruptcy Court in the future.

In deciding the motion seeking a determination that the Bankruptcy Court lacked subject matter jurisdiction, the Court rejected the Defendants' arguments. The Court held that not only had the Defendants made representations in pleadings and to the Bankruptcy Court that the Court indeed possessed subject matter jurisdiction, but the Defendants likewise consensually negotiated and entered a stipulation consenting to jurisdiction, which became a final non-appealable order of the Bankruptcy Court. Further, even in the absence of these findings, the Court held that it also had subject matter jurisdiction over a suit between non-debtors because it concerned damages resulting from an effort to interfere with and/or sabotage a Bankruptcy Court-sanctioned sale of estate property, and thus, was a core proceeding under 28 U.S.C. § 157(b). Matters that "arise" from a bankruptcy case are core matters; asserted interference with the integrity of a bankruptcy sale of assets under Section 363 was implicated here. Unequivocally, a bankruptcy sale process is fundamental to the jurisdiction of the Bankruptcy Court.

5. In re Ventura, 2020 WL 1867898 (Bankr. E.D.N.Y. 2020).

The Debtor indeed can proceed as a Subchapter V Debtor

In a memorandum decision, Judge Grossman decided a series of legal issues of first impression involving questions of law resulting from amendments to the Bankruptcy Code pursuant to the Small Business Reorganization Act of 2019 (the "SBRA").

In this case, Debtor, an operator of a bed and breakfast, filed for Chapter 11. Prior to filing, Debtor had not designated herself as a small business debtor. While in the throes of the bankruptcy process, one day before the plan confirmation hearing, the SBRA became effective. At the Confirmation Hearing, the Court advised the parties of the SBRA and offered the Debtor the opportunity to proceed with the hearing as scheduled or the option to adjourn the hearing for a short time to allow the Debtor to determine whether she wished to amend her petition.

Debtor decided she would amend her petition to designate herself as a "small business debtor" and to proceed as such under subchapter V of Chapter 11, a newly amended provisions added to the Bankruptcy Code pursuant to the SBRA. The Mortgagee and United States Trustee ("UST"), filed objections to the Debtor's election to be treated as a subchapter V case, raising timing and technical issues amongst other objections.

The overall issues discussed by the court were (1) Does the SBRA apply to the Debtor's case?; (2) Does the Debtor fit within the definition of a "small business debtor"?; (3) Does judicial estoppel apply to preclude the Debtor from claiming that the Mortgage debt arose from commercial or business activities?; and, (4) Is the Debtor entitled to utilize 11 U.S.C. § 1190(3)?

Judge Grossman, in review of the objections by the UST and Mortgagee, began by addressing the New SBRA modifications to the existing Bankruptcy Code Sections. The SBRA defines a small business debtor in part, as "...a person engaged in commercial or business activities ... that has aggregate noncontingent liquidated secured and unsecured debts as of the date of the filing of the petition ... in an amount not more than $2,725,625... not less than 50 percent of which arose from the commercial or business activities of the debtor. *Id*. at 6 (citing 11 U.S.C. § 101(51D)(A)). The new changes allow small business debtors under subchapter V, (1) the power to modify the rights of the holder of a claim secured only by a security interest in real

property that is the principal residence of the debtor if the new value received in connection with the granting of the security interest was not used primarily to acquire the real property; and used primarily in connection with the small business of the debtor, (2) small business debtors under subchapter V to be appointed a trustee who will act as a fiduciary for creditors, in lieu of an appointed creditors' committee, and also facilitate the small business reorganization and monitor the subchapter V debtor's consummation of its plan of reorganization,(3) subchapter V debtors the exclusive right to file a plan of reorganization, which must be filed within 90 days after entry of the order for relief.

Further, the Court went on to decide if the SBRA applied to the Debtor's case. Judge Grossman held, as matters of first impression, procedural and timing issues did not bar the debtor from amending her petition to take advantage of the benefits of the SBRA. The Court first based this decision on a Debtor's ability to amend their schedule at any time before the case is closed. Second, the Court opined that the UST's argument, that the Debtor should have complied with the procedural requirements of the new law before the law came was in effect, was the "height of absurdity" *id.* at 8. Additionally, the lack of prohibition provided by Congress conferred Judge Grossman no reason to bar the Debtor from amending her petition to take advantage of the benefits of the SBRA.

Next, the Court held, a debtor could amend their petition to designate themselves as a "small business debtor" notwithstanding prior court orders allowing a creditor to file its own proposed plan of reorganization, scheduling a confirmation hearing, and approving mortgagee's disclosure statement. Mortgagee argued that the retroactive application of the SBRA to the Debtor's case would be prejudicial because of the prior authorization and decisions permitting the Mortgagee to file it's own plan, from the court approving the Mortgagees disclosure statement and from the court deeming Debtor's proposed disclosure statement unconfirmable. Judge Grossman distinguished that the correct question to ask was whether if the designation of the Debtor as a subchapter V debtor would impair Mortgagee's rights as they existed prior to the effective date of the SBRA. Judge Grossman based this question from prior Supreme Court decisions which considered the issue of retroactivity in the context of a newly enacted bankruptcy statutes. Judge Grossman determined that "[T]he SBRA merely amends the definition of small business debtor to ensure that certain debtors can avail themselves of a less costly and time-consuming path to reorganization that befits the family – owned businesses and other "Main Street" businesses that are currently in such dire need of relief." *Id.* at 10.

Further, the Court determined the exception to the anti-modification provision permits a debtor to modify the rights of certain mortgagees by allowing the debtor to bifurcate a claim into a secured and unsecured claim based on the value of the underlying collateral. *See* 11 U.S.C.S. § 1190(3). Judge Grossman noted the Bankruptcy Code works to abrogate contractual rights, but does not affect the vested property rights of mortgagees. Further, the contractual right of a secured creditor to obtain repayment of debt may be quite different in legal contemplation from the property right of the same creditor in the collateral.

Moreover, Judge Grossman indicated, the fact that a debtor incurs mortgage debt to buy a residence does not automatically mean that the debt is consumer debt. Under the Bankruptcy Code, "The test for determining whether a debt should be classified as a business debt, rather than as a consumer debt, is whether it was incurred with an eye toward profit. Courts must look at the substance of the transaction and the borrower's purpose in obtaining the loan, rather than merely looking at the form of the transaction. A debt incurred with an eye toward profit is a business debt, rather than consumer debt. *Id. at 12*

Next, the Court addressed the issue of Judicial estoppel. The Court quoted precedent stating "A debtor may be judicially estopped from changing its legal position when a court has adopted and relied on it and the party claiming judicial estoppel suffers an unfair detriment as a result, unless mistake or inadvertence is an applicable defense. Inadvertence can be shown where the party in question either lacks sufficient knowledge of the undisclosed claims or would have no motive for their concealment.

The circumstances under which judicial estoppel may be invoked are not reducible to any general formulation of principle. However, a general test for determining when judicial estopped may be invoked has been developed, as follows: (i) a party's later position is clearly inconsistent with its earlier position, (ii) the party's former position has been accepted in some way by the court in the earlier proceeding, such that judicial acceptance of an inconsistent position in a later proceeding would create the perception that either the first or the second court was misled, and (iii) the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped. Judicial estoppel has been applied in the bankruptcy context where a debtor changes its designation on the petition. Therefore, Judge Grossman held the Debtor was not judicially estopped from claiming that her mortgage debt arose from commercial or business activities.

The Court is charged with interpreting all federal and state statutes according to their plain meaning. In determining its degree of ambiguity or clarity, courts cannot examine statutory language in isolation. The Court must determine the specific context in which the language appears, and the statutory scheme's broader framework in order to preserve the coherence and consistency of the statutory scheme. In matters of statutory interpretation, the plain meaning of statutory language is often illuminated by considering not only the particular statutory language at issue, but also the structure of the section in which the key language is found, and the design of the statute as a whole and its object.

Unlike 11 U.S.C.S. § 1123(b)(5), which precluded modifications of claims secured by mortgages on the debtor's principal residence, 11 U.S.C.S. § 1190(3) specifically permits the modification of claims secured by mortgages on the debtor's principal residence. Starting with subparagraph (A), the statute reads that the mortgage proceeds cannot have been used primarily to acquire the real property. As a matter of common usage, the word "primarily" means for the most part. The phrase "real property" refers back to the real property that is the debtor's residence. Unlike 11 U.S.C.S. § 1123(b)(5) which took an all-or-nothing approach to loans securing the debtor's residence, 11 U.S.C.S. § 1190(3) asks the Court to determine whether the primary purpose of the mortgage was to acquire the debtor's residence. Subparagraph (B) requires the Court to determine whether the mortgage proceeds were used primarily in connection with the debtor's business. Both of these subparagraphs direct the Court to conduct a qualitative analysis to determine whether the principal purpose of the debt was not to provide the debtor with a place to live, and whether the mortgage proceeds were primarily for the benefit of the debtor's business activities.

With respect to 11 U.S.C.S. § 1190(3), the Court established the following factors be considered to determine whether a mortgage in question is subject to modification under 11 U.S.C.S. § 1190(3): 1. Were the mortgage proceeds used primarily to further the debtor's business interests; 2. Is the property an integral part of the debtor's business; 3. The degree to which the specific property is necessary to run the business; 4. Do customers need to enter the property to utilize the business; and 5. Does the business utilize employees and other businesses in the area to run its operations.

The court concluded that the Debtor is considered a “small business debtor” within the purview of 11 U.S.C. § 101(51D)(A) and is eligible to proceed as a subchapter V debtor. Moreover, the Court overruled the UST and Mortgagee’s objections. *Presently, a direct appeal of the Decision and Order to the Second Circuit has been sought by the mortgage servicer.*

6. In re Telles, 2020 WL 2121254 (Bankr. E.D.N.Y. 2020)

Nunc pro tunc relief cannot cure an otherwise void foreclosure sale

In a Memorandum Decision, Judge Grossman denied Creditor's Motion for Relief from the automatic stay, *nunc pro tunc*, to the day before Debtor's foreclosure sale on his property. This decision was issued following the Supreme Court's decision concerning *nunc pro tunc* relief in *Roman Catholic Archdiocese of San Juan v. Acevedo Feliciano*, 140 S. Ct. 696, 206 L. Ed. 2d 1 (2020).

Here, Creditor held a Judgment of foreclosure and sale with respect to the property owned by Debtor. Previously, Debtor resided at a property but had no legal interest in the property. The property was owned by a non-debtor mortgagor. A judgment of foreclosure and sale was entered in March with a sale scheduled 2 months later. Two days before the sale the non-debtor mortgagor deeded a ten percent interest in the property to the Debtor. Debtor then filed Chapter 13 but was denied. The foreclosure sale was rescheduled. The day before the rescheduled foreclosure sale, Debtor filed Chapter 13 again. The sale was not canceled. Unaware of the bankruptcy filing, Creditor purchased the property. Creditor was unaware of the Debtor's bankruptcy filing at the time of the foreclosure sale because Debtor failed to notify the state court referee of the bankruptcy.

Creditor aware of Debtor's shenanigans, fearful the case would be dismissed, sought an emergency hearing. Creditor argued that the Court should not permit such an obvious abuse of the bankruptcy laws to benefit the Debtor and asked the Court to utilize its power to grant the requested relief in the interest of fairness and in keeping with the purpose of the bankruptcy laws.

The E.D.N.Y. had never granted relief from the automatic stay *nunc pro tunc* to put its imprint on an otherwise void foreclosure sale, and often denied such motion without issuing a written decision. Nevertheless, Judge Grossman took it upon himself to explain the reasoning behind the denial.

The Court relied heavily on the Supreme Court's ruling in *Acevedo*, which held, "[f]ederal courts may issue *nunc pro tunc orders*, or 'now for then' orders, . . . to 'reflect [] the reality' of what has already occurred . . . . 'Such a decree presupposes a decree allowed, or ordered, but not entered, through inadvertence of the court.' . . . Put colorfully, '[n]unc pro tunc orders are not some Orwellian vehicle for revisionist history — creating 'facts' that never occurred in fact.'"*See Acevedo*, 140 S. Ct. at 700-01. In other words, *nunc pro tunc* relief could not cure the jurisdictional defect and therefore the state court orders were void and of no force and effect. Moreover, a *nunc pro tunc*

order may not be used to cure the absence of a decree on a prior date and instead is properly used to correct the record to "reflect the reality of what has already occurred.

Judge Grossman took into consideration and understood Creditor's argument, but pointed out a critical flaw. Creditor seemed like a strong candidate for retroactive relief. They bolstered their argument with two previous cases from the E.D.N.Y. where *nunc pro tunc* relief was granted. In the first case creditor never received notice of the bankruptcy filing, and in the second case where debtor filed for bankruptcy 20 minutes prior to a foreclosure sale. *see In re Cunningham,* 506 BR 334, 346 (Bankr. E.D.N.Y. 2014); *see In re Jean-Francois*, 516 B.R. 699, 704-07 (E.D.N.Y. 2014). However, Creditor failed to take into consideration the newer rule set forth in *Acevedo.* According to *Acevedo*, "Once a debtor files for bankruptcy, the state court is divested of jurisdiction over property of the estate, and any action taken by the state court with respect to the debtor's property is void." *id.* at 700. Therefore, *nunc pro tunc relief* cannot be used to change the outcome of a void foreclosure sale.

Judge Grossman added that if the Court were to grant the Motion, the ruling would contradict *Acevedo,* and therefore, be subject to reversal on appeal. Based upon the Supreme Court's decision that *nunc pro tunc* relief cannot be granted to confer jurisdiction on a state court where none existed, the Court denied creditor's motion in its entirety.

7. In re Hector Benitez, 68 Bankr.Ct.Dec. 140, 2020 WL 1272258 (Bankr. E.D.N.Y. 2020)

The Bankruptcy Court will no longer require or grant *nunc pro tunc* retentions--they are not necessary

In this decision, Judge Grossman denied, without prejudice, Chapter 7 Trustee's motion made for an order approving the retention of general counsel to the Trustee *nunc pro tunc* to 2/02/2019.

Here, Marc Pegament, the Chapter 7 Trustee (the "Trustee") asked the court to approve his counsel's retention *nunc pro tunc* to approximately eleven months prior to filing a Motion to Retain. Debtor had been asked to turn over several documents by the Trustee following the date of the petition. After 11 months had passed, the Trustee filed a Motion to Retain contemporaneously with a Motion to Compel the Debtor to turn over documents, the sum of $1,579.28, and the Debtor's 2018 income tax refunds. Trustee provided 2 letters 10 months apart asking for documents, but did not get a response from Debtor. As a result, Trustee sought *nunc pro tunc* approval for counsel retention to one-month post-petition.

The Court began by discussing that *nunc pro tunc* retentions are common practice in bankruptcy matters largely resulting from the statutory framework for compensation of estate professionals set forth in 11 U.S.C.S. §§ 327 and 330 and Fed. R. Bankr. P. 2014; that is, professionals seeking compensation from the estate, such as general counsel retained by a Chapter 7 trustee, may not be compensated under 11 U.S.C.S. § 330 unless they have been retained under 11 U.S.C.S. § 327. Further, Judge Grossman points out that the delay between commencement of services to the estate, the filing of a motion for court approval and the entry of the order approving the retention may take several weeks. In most cases it is impractical and possibly detrimental to the estate for the professional to delay providing what may be critical services until entry of the order approving their retention. Courts have addressed this situation by, in specific cases, approving *nunc pro tunc* retentions so that the date of approval of the professional's retention dates back to the date of the trustee's application, or in some cases to the date of commencement of the professional's services.

However, in *Acevedo,* as previously mentioned, federal courts may issue *nunc pro tunc* orders, or "now for then" orders, to reflect the reality of what has already

occurred. Judge Grossman's and the Bankruptcy Court for the Eastern District of New York's reading of *Acevedo*, holds that utilizing *nunc pro tunc* orders to approve the retention of estate professionals retroactive to some date prior to the actual date of court approval is inappropriate.

It is this Court's determination that retroactive approval of the retention of an estate professional, whether it be *nunc pro tunc*, *post-facto* or any similar nomenclature, is not mandated under the Bankruptcy Code or Rules. Therefore, according to this Court, a professional must be retained as required by 11 U.S.C.S. § 327 but once having been retained, the Bankruptcy Court is free to compensate him for services rendered to the estate at any time, pre and post-court approval, in accordance with 11 U.S.C.S. § 330.

Subsequently, Judge Grossman determined that the United States Bankruptcy Court for the Eastern District of New York will no longer require or grant *nunc pro tunc* retentions. A late applicant runs the risk that court approval under 11 U.S.C.S. § 327 may be withheld on the basis of disinterestedness or some other statutory infirmity, which will preclude compensation under 11 U.S.C.S. § 330. In addition, the Court also establishes that late-filed retention applications should be subject to heightened scrutiny. Such applications must contain a detailed recitation of: the reasons for the delay in seeking court approval; the services already performed by the proposed professional, and the approximate amount billed up to the date of the application; the results obtained; and any future services that are contemplated. The late applicant runs the risk that court approval may be withheld on the basis that, in hindsight, the services performed by the proposed professional did not benefit the estate.

Furthermore, the court held that there is no per se prohibition, in the statute or precedential caselaw, against awarding reasonable compensation to an estate professional for actual and necessary services rendered to the estate prior to the date of court approval of retention. However, the longer an estate professional waits to seek court approval of its retention, the more the particular facts and circumstances surrounding the case develop, allowing a court to broaden its analysis to include hindsight consideration of the services already rendered and the professionals who rendered those services. Seeking court approval after-the-fact subjects the professional to the possibility that approval of retention may be denied considering the lack of benefit to the estate thus precluding any possibility of compensation under 11 U.S.C.S. § 330. Where services rendered ultimately provide little or no benefit to the estate, court approval obtained prior to the rendering of the services would at least allow the professional to seek compensation and prove the compensation was reasonable and necessary in light of the facts and circumstances of the case.

Therefore, the Court concluded that the Trustee's delay of nearly a full year in filing the Motion to Retain would actually permit the Court to review the work already performed and determine whether the retention of Trustee's counsel should be approved considering what had happened in this specific case. The Court, however, was unable to evaluate the actual value provided by counsel and the Court was disappointed with the limited information provided by the Trustee contained in the Motion to Retain. Ultimately, the Court decided given the particular facts and circumstances surrounding the case and the proposed retention, there was no basis to retain Trustee's counsel at the time.

Judge Louis A. Scarcella

8. In re Hlady, Adv. Pro. 16-8181-LAS (4/24/20)

Undue Hardship, Hardly!

In a Memorandum Decision After Trial, Judge Scarcella denied Debtor's Motion for Discharge of her student loan debt. In his opinion, Judge Scarcella acknowledged that although it has received criticism for being overly harsh, the Second Circuit maintains that the three prong Brunner test remains binding precedent. Chief Justice Morris stated the Brunner test should be applied by the courts "as it was originally intended." Clavell v. U.S. Department of Education, 611 B.R. 504 (Bankr. S.D.N.Y. 2020).

Here, the plaintiff asserted she satisfied the three prong test set forth by the Second Circuit Court of Appeals in Brunner v. N.Y. Higher Educ. Servs. Corp., 831 F.2d 395 (2d Cir. 1987) for determining the existence of "undue hardship", thus establishing that the student loan debt at issue is dischargeable. In re Hlady, No. 8-16-74011-las, Adv. Pro. No. 8-16-08181-las. at *1 (E.D.N.Y. Apr. 24, 2020).

Under the three-prong Brunner test, a claim of "undue hardship" turns on the following questions:

(i) whether a debtor, based on her current finances, can repay her student loan obligation and still maintain a minimal standard of living,

(ii) if she does not have the present ability to repay her student loan obligation and, at the same time, maintain a minimal standard of living, whether that inability will persist for a significant portion of the repayment period, and

(iii) whether the debtor has made a good faith effort to repay her student loan obligation. Additionally, under existing Second Circuit precedent, a debtor bears the burden of proving each element of the Brunner test by a preponderance of the evidence. Id.

A. Minimal Standard of Living

While the court cannot impose a certain standard of living on the debtor, it is required to assess the reasonableness of the Debtor's budget — particularly the allocation of projected expenses in relation to projected income as it determines his capabilities to pay the instant obligations without undue hardship.'" Lozada v. Educ. Credit Mgmt. Corp. (In re Lozada), 594 B.R. 212, 222 (Bankr. S.D.N.Y. 2018) (emphasis in original), aff'd, 604 B.R. 427 (S.D.N.Y. 2019) (quoting Pincus, 280 B.R. at 317).

Additionally, courts consider whether a debtor has sought to maximize her ability to earn adequate income to pay for expenses and student loans while minimizing certain

discretionary expenses. Burton v. Educ. Credit Mgmt. Corp. (In re Burton), 339 B.R. 856, 870-71 (Bankr. E.D. Vir. 2006) (finding that courts must look at the debtor's income and expenses to determine what is the minimally necessary amount to ensure that the debtor's needs, such as food, shelter, clothing, and medical treatment are met and then look to see whether the debtor has additional funds to make student loan repayments).

Here, Plaintiff made no effort to obtain a loan requiring a payment of $0 for 25 years but did buy an Apple watch for $432.33, a Kate Spade purse for $214, and stayed at the Fairmont Hotel in Montreal at a cost of $1,115.77. Judge Scarcella held that the Plaintiff made no effort to minimize these discretionary expenses. Further, her stated intention to retire at 58 is a worthy goal, but not one the Court is willing to consider as part of a repayment plan. Moreover, Plaintiff's intention to retire early (page 16) and her unwillingness to e.g. advertise her business beyond word of mouth referrals, despite allocating over $1,000 towards a conference in Montreal about an area of business she does not engage in nor has made any affirmative steps towards.

The Court concluded the Plaintiff failed to meet her burden of proof for the first prong of the Brunner test because she spent lavishly and made no effort to expand her business.
Since the Plaintiff did not meet her burden of proof as to the first prong of the Brunner test, the Court did not need to continue its analysis but decided to for the sake of completeness.

B. Persistence of Inability to Pay

The second prong of the Brunner test requires a debtor to show that `additional circumstances exist indicating that [the debtor's present economic duress] is likely to persist for a significant portion of the repayment period' for the student loans, and that inability to pay is because of factors beyond the debtor's control." In re Lozada, 604 B.R. 427, 436 (S.D.N.Y. 2019) (quoting In re Crawley, 460 B.R. 421, 438 (Bankr. E.D. Pa. 2011)). "Under this factor, debtors must demonstrate `unique or exceptional circumstances in their current situations that would clearly limit their future abilities to earn a living, support themselves, and repay their loans.'" Id. (citations omitted). In evaluating this factor, courts may consider a debtor's medical condition, disability, or responsibility for his or her dependents. King v. Vt. Student Assistance Corp. (In re King), 368 B.R. 358, 370 (Bankr. D. Vt. 2007). However, the debtor's testominoy alone is not sufficient. Lozada at 436-437.

Courts have rejected arguments that age alone satisfies the second prong of the Brunner test. Chance, 600 B.R. at 59 (rejecting age as a factor where the debtors are in their late fifties); Tuttle v. Educ. Credit Mgmt. Corp. (In re Tuttle), 600 B.R. 783, 801 (Bankr. E.D. Wis. 2019) (rejecting argument that 46 years of age is an "exceptional circumstance" equating to unemployability and a persistent inability to pay). The fact that repayment of plaintiff's student loan obligation will last into her later years in life is a by-product of plaintiff's choice to obtain her law degree in her mid-30's, and it is not a

unique or exceptional circumstance that is beyond plaintiff's control. Little v. U.S. Dep't. of Educ. (In re Little), 607 B.R. 853, 861 (Bankr. N.D. Tex. 2019).

The Plaintiff cannot claim that her inability to pay is because of factors beyond her control. Here, the debtor relied exclusively on her own testimony that her physical capacity to work was reduced by a 2011 injury. She has continued to work as an attorney and shovel snow ever since then.

The Plaintiff cannot claim that her arbitrary decision to retire at 58 will create a burden preventing her from making payment. The Plaintiff claimed that payment of $0 for a period of 25 years would unduly burden her because in 25 years she would be 74 years old and intends to retire at 58. However, the Plaintiff did not proffer any medical testimony stating that she needed to stop working at 58.

The Plaintiff cannot rely on her own testimony alone to prove she is physically incapable of working and cannot arbitrarily decide to retire early.

C. Good Faith Effort

The third prong of the Brunner test considers whether "the debtor has made good faith efforts to repay the loans." Brunner, 831 F.2d at 396. Courts look to factors such as a debtor's "efforts to obtain employment, maximize income and minimize expenses, and to undertake all other reasonable efforts to ensure repayment." Pobiner v. Educ. Credit Mgmt. Corp. (In re Pobiner), 309 B.R. 405, 420 (Bankr. E.D.N.Y. 2004) (citation omitted); Pincus, 280 B.R. at 316. Repayment efforts can include (1) actual payments made on the loans and (2) attempts by the debtor to seek alternative remedies to discharge, such as deferment of payment. Id.

Plaintiff cannot establish good faith effort. Plaintiff made no attempt to curtail her spending and could have expanded her business beyond word of mouth referrals. Further, while Plaintiff is not required to enter into an income-based repayment program, her basis for declining to pursue such an option, where her future monthly payment under any of the program options would be $0 based upon her 2016 income, is simply the inconvenience of having to annually report her income for 25 years. Plaintiff's unwillingness to be inconvenienced by having to report her annual income for the next 25 years does not provide sufficient justification to discharge her student loan obligation.

The Second Circuit mandates the application of the Brunner test, despite ongoing criticism of the standard. Judge Scarcella's application of the test focused on the fact that the Plaintiff qualified for a loan repayment program wherein she would pay nothing for 25 years (assuming her current income level remains similar). Where a debtor is eligible to enroll in an income-based repayment program, the debtor must demonstrate how she will be unable to make the limited payments required under the formula and still maintain a minimal standard of living. Chance, 600 B.R. at 58 (noting

that a court can consider whether the debtor is able to make payments under an income-based repayment plan and still maintain a minimum standard of living); Lewellen v. Access Group, Inc. (In re Lewellen), Case No. 07-31666 TEC, Adv. Proc. No. 08-3119 TC, 2010 WL 4975903, at *1 (Bankr. N.D. Cal. Dec. 1, 2010). Thus, the Court held that Plaintiff failed to demonstrate by a preponderance of the evidence that she would be unable to maintain a minimum standard of living if required to make payments of $0 for a period of 25 years (based upon her present income).

9. In re Grinspan, 597 B.R. 725 (Bankr. E.D.N.Y. 2019)

Automatic Stay Exception for Domestic Support Obligations Does Not Include Post-Petition Contempt Motion to Enforce Debtor's Fee Obligation

Isaac Grinspan brought an adversary proceeding against his ex-wife and her attorney to recover for their willful violations of the automatic stay imposed under 11 U.S.C. section 362(a), alleging that Defendants violated the automatic stay when they continued to litigate in state court a motion to hold Plaintiff in contempt in the parties' state court matrimonial action, after Grinspan filed his Chapter 7 petition. Plaintiff alleged that a contempt motion which sought to enforce a money judgment consisting of attorneys' fees awarded to the ex-wife as a result of Plaintiff's alleged default under their divorce agreement is not exempt from the automatic stay as a domestic support obligation. In turn, Defendants, represented by LaMonica Herbst & Maniscalco, LLP, argued that even if their post-petition actions in the state court proceedings are construed as a demand for payment of a money judgment, those actions sought to collect upon a domestic support obligation and are exempt under section 362(b)(2)(B). The parties' Judgment of Divorce incorporated a Stipulation of Settlement that provided that if either party failed to comply with their respective obligations under the Settlement, the defaulting party would reimburse the non-defaulting party for legal fees incurred in connection with enforcing the Settlement, so long as the non-defaulting party prevailed. Plaintiff defaulted under a Consent Order entered in Supreme Court, Nassau County and his ex-wife obtained a judgment against him in the amount of $18,372.61, which consisted of attorneys' fees owed to the ex-wife plus accrued interest (the "Money Judgment"). The Court was faced with three primary issues: (1) whether defendants violated the automatic stay; (2) if so, whether the Money Judgment is a domestic support obligation and Defendants' conduct is exempt from the automatic stay under section 362(b)(2)(B); and (3) if Defendants' conduct is not allowed under section 362(b)(2)(B) whether the conduct was a willful violation of the automatic stay.

Judge Scarcella noted that the prudent approach would have been for Defendants to seek declaratory relief from the Bankruptcy Court before taking any action with regard to the pending contempt motion, but they did not. Judge Scarcella ruled that Plaintiff established that Defendants had violated the automatic stay by continuing to prosecute the motion. The Court held that the Defendants' actions were not exempt from the automatic stay under section 362(b)(2)(B). Defendants took the position that the Money Judgment is a "domestic support obligation" as that term is defined under section 101(14A), so any action by them to collect the Money Judgment is allowed by section 362(b)(2)(B). Plaintiff, on the other hand, contended that the Money Judgment was not entered for the purpose of awarding support to the ex-wife and/or to their children, and it was not a domestic support obligation and was not exempt from the constraints of the automatic stay. Rather, it was a penalty for not complying with the Settlement. Plaintiff also asserted that even if the Court were to find

that the Money Judgment constitutes a domestic support obligation, Defendants conduct is still not permitted because Defendants sought to enforce, not collect, the money judgment, and while collection is a protected activity, enforcement is not.

In rendering his decision, Judge Scarcella focused on the basis for the award of attorneys' fees. The Court agreed that the default provision in the parties' Stipulation of Settlement was not designed to support the ex-wife and/or their children, but was instead designed to provide both parties with an incentive to timely perform their respective obligations under the Settlement. Accordingly, Plaintiff's obligation to pay attorneys' fees awarded by the Money Judgment is not a domestic support obligation as defined in section 101(14A), but is instead a debt incurred by the Debtor in the course of a divorce or separation agreement (following Judge Eisenberg's rationale in *In re Golio,* 393 B.R. 56 (Bankr. E.D.N.Y. 2008)). The Court also found that even if the Money Judgment constitutes a domestic support obligation, which it did not, Defendants violated the automatic stay because litigating the Contempt Motion was the "enforcement" of a DSO, which is not excepted pursuant to section 362(b)(2)(B) as a "collection". Finally, the Court found that since Defendants willfully violated the automatic stay, an award of actual damages incurred by Plaintiff was mandated by section 362(k)(1). The Court reserved judgment of actual damages pending submission of supplemental briefing. Punitive damages were not warranted as there was no malice or bad faith.

10. In re Joseph Yerushalmi, Chapter 7 case no. 07-72816-LAS (6/5/19)

Bankruptcy Court's decision on IRS tax obligation would receive preclusive effect in Tax Court.

The Debtor filed a Chapter 11 case in July 2007, which was converted to a Chapter 7 case in October 2007, and Marc Pergament was appointed as Chapter 7 Trustee. In December 2007, the IRS issued a statutory notice of deficiency to the Debtor-Taxpayer, which provided the Debtor with a 90 day period to petition the Tax Court for a redetermination of the deficiency. However, due to the automatic stay imposed under § 362(a), the Debtor was barred from petitioning the Tax Court unless the stay was lifted (and since an additional 60 days was provided after the automatic stay ends, the Debtor would have 150 days to petition the IRS after the stay was lifted or ended).

The Debtor's ex-wife filed a petition with the Tax Court in March 2008, which was halted by the Debtor's refusal to seek relief from the automatic stay and participate. Prompted by the delay in the administration of debtor's bankruptcy case (due to a pending state court action), the IRS sought relief from the automatic stay in July 2013. A Stay Relief Stipulation was entered, but was limited to the ex-wife's petition. The IRS then filed a second motion for relief from stay in May 2014 to allow the Debtor to petition on his own tax liability. The Bankruptcy Court entered a Conditional Order in July 2014, allowing the IRS to commence proceedings in Tax Court unless the Debtor filed a complaint against the IRS in the Bankruptcy Court or otherwise challenged the IRS' proof of claim. The Debtor timely filed his objection to the IRS' proof of claim, and the IRS argued that the Debtor did not have standing to object. The Debtor argued that the determination of his tax liability should be heard by the Bankruptcy Court pursuant to the Stay Relief Stipulation and the Conditional Order. The IRS filed a third motion seeking relief from the automatic stay in February 2015 to permit the 150-day period to run regardless of whether the Debtor decided to petition the Tax Court or the Bankruptcy Court decided the objection to the IRS claim (arguing that continuing to stay running of the 150 day period would be prejudicial).

Judge Scarcella first determined that the Stay Relief Stipulation did not confer exclusive jurisdiction on the Bankruptcy Court to determine the tax dispute. Judge

Scarcella held that under 28 U.S.C.S. § 157(a), the Bankruptcy Court did not have exclusive jurisdiction over the tax dispute, as the Tax Court also had jurisdiction under I.R.C. § 7442, and the parties by agreement could not confer exclusive jurisdiction on the Bankruptcy Court. Instead, Judge Scarcella agreed with the IRS' interpretation of the terms of the Stay Relief Stipulation, *i.e.*, that the Bankruptcy Court retained exclusive jurisdiction to interpret and enforce the Stay Relief Stipulation only. Judge Scarcella further determined that the Conditional Order did not mandate that the tax dispute be heard and determined by the Bankruptcy Court, as argued by the Debtor. Judge Scarcella found that the Debtor's choice of the Bankruptcy Court to hear the tax dispute, by filing of the claim objection, did not preclude the IRS from asking the Bankruptcy Court to abstain in favor of the Tax Court (nor did it so infer), since there was nothing to abstain from until the objection was filed.

Judge Scarcella next determined that the Debtor had standing to object to the IRS' proof of claim. The IRS argued that the Debtor was not a party in interest under § 502(a) because he did not have a pecuniary interest in the Chapter 7 bankruptcy case. Judge Scarcella found that the Debtor had standing to object to the IRS' nondischargeable and priority claim because reduction would maximize the distribution of estate assets and reduce the Debtor's personal liability (and further noted that pecuniary interest would also exist where the objection would result in a surplus to a debtor).

Next, Judge Scarcella determined that the IRS' request for abstention of the hearing of the outstanding tax dispute in deference to the Tax Court was premature because there was no parallel proceeding in Tax Court to determine the Debtor's tax liability. Judge Scarcella analyzed permissive or discretionary abstention under 28 U.S.C.S. § 1334(c)(1), and weighed various factors to determine that abstention would be appropriate in determining tax liability; however, there was no parallel tax proceeding to abstain from in this case.

Finally, Judge Scarcella found that lifting of the automatic stay was warranted in order to permit the 150-day period to run in order for the tax dispute to finally be resolved. Judge Scarcella noted that the Debtor could decide to either proceed in Tax Court or in Bankruptcy Court, and that the Bankruptcy Court's decision would be final and issue preclusion, or *res judicata*, would prevent a subsequent review by the Tax Court. Therefore, there was no other credible reason to continue tolling the 150 day period, and doing so would only "invite a potential for abuse and a waste of judicial resources."

While not deciding the burden of proof issue, Judge Scarcella discussed the matter, as it was the basis for the Debtor's insistence on being heard in the Bankruptcy Court. Judge Scarcella noted that the Debtor was incorrect in his belief that the burden of proof is on the IRS (while in Tax Court, the burden of proof would be on the taxpayer). Judge Scarcella found that the taxpayer's bankruptcy filing does not change the burden of proof imposed by substantive law with respect to allowance of a tax claim.

2019 WL 4584146
Only the Westlaw citation is currently available.
United States Bankruptcy Court, E.D. New York.

IN RE Maura E. LYNCH, Debtor.
R. Kenneth Barnard, as Chapter 7 Trustee
of the Estate of Maura E. Lynch, Plaintiff,
v.
Patricia M. Frank, Defendant.

Case No.: 15-74795 (AST)
|
Adv. Pro. No.: 18-08169 (AST)
|
Signed September 20, 2019

Attorneys and Law Firms

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Fredrick P. Stern, Fredrick P. Stern, PC, Nesconset, NY, for Defendant.

ORDER CONVERTING DEFENDANT'S MOTION TO DISMISS TO A MOTION FOR SUMMARY JUDGMENT

Alan S. Trust, United States Bankruptcy Judge

***1** Pending before the Court is the motion to dismiss (the "Motion to Dismiss") filed by Patricia M. Frank ("Frank"), to dismiss the complaint (the "Complaint") filed by R. Kenneth Barnard, Esq., solely in his capacity as Chapter 7 Trustee ("Trustee" or "Plaintiff"). Defendant seeks dismissal of the Complaint under Rule 12(b)(6) of the Federal Rules of Civil Procedure (the "Rules"), as incorporated by Rule 7012 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules") on the grounds that the Complaint fails to state a claim upon which relief can be granted. For the reasons stated below, the Court has converted the Motion to Dismiss to one for summary judgment.

Jurisdiction

This court has jurisdiction over this core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A), (K) and 1334(b), and the Standing Orders of Reference in effect in the Eastern District of New York dated August 28, 1986, and as amended on December 5, 2012, but made effective *nunc pro tunc* as of June 23, 2011.

Factual Background and Procedural History [1]

Procedural history

In 2010, Stephen Vaccaro ("Vaccaro") commenced a divorce action against Maura Lynch ("Lynch" or "Debtor"), Index No. 38437-10 in New York Supreme Court, County of Suffolk (the "State Court"). Following a nine-day trial, the State Court entered an order on December 12, 2012, as amended on March 15, 2013, directing, *inter alia*, equitable distribution of the parties' assets. The State Court ordered *inter alia*, that Vaccaro and Lynch cooperate to sell the property located at 43 Harbor Drive, Sag Harbor NY ("Harbor Drive") and evenly divide the proceeds between them following the satisfaction of any outstanding mortgages, liens, and judgments. In addition, the State Court declined to appoint a receiver at that time to manage the sale of Harbor Drive, but said that it would do so if Vaccaro and Lynch could not work together, or if one of them thwarted the sale of the property.

On May 3, 2013, following a motion by Vaccaro, the State Court appointed Vaccaro as receiver for Harbor Drive based on Lynch's failure to vacate Harbor Drive and cooperate in the sale of that property. The state court further directed Lynch to leave Harbor Drive by June 30, 2013 and to make the property presentable for real estate showings.

The State Court entered a final judgment in the Divorce Action on July 16, 2013, as amended on December 23, 2013, which reiterated that Harbor Drive was to be equitably distributed.

The State Court found Lynch in contempt on November 26, 2013 for, *inter alia*, obstructing the sale of Harbor Drive.

On or about April 8, 2014, Vaccaro entered into a contract to sell Harbor Drive to Frank for a purchase price of $1,325,000; the contract did not include a right of pre-closing possession for Frank (the "Vaccaro-Frank Contract").

On April 1, 2015, the state court replaced Vaccaro with Stephen O'Brien, Esq. ("O'Brien") as receiver and directed O'Brien to prevent waste or mismanagement of Harbor Drive and to dispose of it in accordance with its prior order. However, on Lynch's motion, the New York Appellate Division, Second Department issued an order on March 27, 2015 directing Vaccaro to show cause as to why the sale of Harbor Drive should not be stayed pending Lynch's appeal of various State Court orders, and the State Court accordingly stayed its April 1, 2015 order on April 14, 2015. Subsequently, on May 15, 2015, the Second Department denied Lynch's request for a stay of sale, and by order dated August 25, 2015, the State Court vacated its April 14, 2015 order, thereby allowing the sale of Harbor Drive to move forward.

***2** On September 24, 2015, the State Court authorized O'Brien to retain counsel and a broker to sell Harbor Drive in accordance with the Vaccaro-Frank Contract for $1,325,000. Again, no preclosing right of possession was accorded to Frank.

Before Frank closed on the purchase of Harbor Drive, Lynch filed her voluntary petition for relief under Chapter 11 of the Bankruptcy Code on November 9, 2015.

On November 17, 2015, Frank filed a motion for an order pursuant to 11 U.S.C. § 362(d) terminating the automatic stay in order to allow Frank to proceed with her purchase (the "Stay Motion"). Frank also asked the Bankruptcy Court to stay an ancillary eviction proceeding initiated by Lynch against Frank in the Justice Court of the Town of Southampton.

Subsequently, on November 23, 2015, Vaccaro filed a motion, as amended on November 30, 2015, seeking an order pursuant to 11 U.S.C. § 543(d) excusing O'Brien's compliance with Sections 543(a) and (b) of the Bankruptcy Code (the "Excusal Motion"), thus allowing O'Brien to retain possession of Harbor Drive, rather than delivering the property to Lynch. O'Brien joined the Excusal Motion on December 2, 2015.

On December 10, 2015, this Court held an evidentiary hearing on the Stay and Excusal Motions. Vaccaro, Lynch, Frank, and O'Brien were all represented by counsel at that hearing, and O'Brien testified. After reviewing evidence submitted by the parties and hearing argument from counsel, this Court orally granted the Excusal Motion in part and denied the Stay Motion in its entirety, after first affording the parties time to privately work out a mechanism by which the value of Harbor Drive could be quickly maximized for the benefit of creditors.

The Court shortly thereafter issued an Order setting protocols for an auction (the "Auction Order") of Harbor Drive, finding that it was "in the best interests of [Lynch's] bankruptcy estate, its creditors and other parties-in-interest, for" Harbor Drive to be sold by O'Brien. The Auction Order also provided that "Frank, who signed a contract to purchase the Harbor Drive Property for $1,325,000.00 has agreed to increase her offer to $1,425,000.00 and shall be deemed a stalking horse bidder and a Qualified Bidder." However, at no point did Frank ask for buyer protections such as a break up fee.

Frank and Debtor then sought stay and/or reconsideration of the Harbor Sale Order, which were denied. In particular, Frank argued that the Bankruptcy Court (1) failed to correctly apply New York law by *sua sponte* determining that the Vaccaro-Frank Contract had "expired"; (2) deprived Frank of due process by refusing to give effect to the Vaccaro-Frank Contract; and (3) improperly denied Frank of the protections of 11 U.S.C. § 365(i), which would allow her, as the purchaser in possession of Harbor Drive, to enforce the Vaccaro-Frank Contract. In the alternative, Frank asked this Court to stay the auction and sale of Harbor Drive pending appeal.

At a hearing on March 9, 2016, this Court orally denied Frank's motion for reconsideration. This Court determined that reconsideration of the Stay Order was unwarranted because (1) Frank's motion was untimely since it was filed more than 14 days after entry of the Stay Order; and (2) this Court did not make any mistake of law or fact in denying the Stay Motion. This Court held that the "Bankruptcy Code clearly supervenes State Court receivership orders, and this Court has statutory authority under Section 543 to excuse or condition the receiver's noncompliance with Sections 362, 542, and 543 with respect to bankruptcy of the estate which is precisely what this Court did in the receiver order entered on December 22nd." This Court also denied reconsideration of the Auction Order, and declined Frank's request for a stay of

sale pending appeal; in particular, this Court again noted that 11 U.S.C. § 365(i) is inapplicable as it is limited to contracts of sale made by the debtor, and Lynch was not a party to the Vaccaro-Frank Contract.

***3** An auction was held for Harbor Drive on February 22, 2016, and Frank was the winning bidder with the purchase price of $1,865,000.00 (the "Purchase Price"). This Court then held evidentiary hearings on February 24, 2016 and March 9, 2016 to determine whether to approve the sale of Harbor Drive to Frank. After hearing testimony and reviewing evidence, this Court found that there had been no violation of the Court's bid procedures, and found that approving the sale of Harbor Drive to Frank for the Purchase Price was in the best interest of the bankruptcy estate and, without any doubt, maximized the value of this asset to this estate.

On March 18, 2016, the Court issued an Order, which authorized O'Brien to sell Harbor Drive to Frank for the Purchase Price (the "Sale Order"). Thereafter, Frank moved on March 21, 2016 for a stay of the Sale Order pending appeal, which this Court denied by order dated March 24, 2016. In accordance with the Sale Order, O'Brien and Frank closed on the purchase of Harbor Drive on March 24, 2016, and the property deed was transferred to Frank.

Lynch appealed the Excusal Order and Frank continued her appeal of the Sale Order. The District Court consolidated the Lynch Appeal and the Frank Appeals by order dated May 10, 2016. The District Court affirmed this Court's Excusal Order and Sale Order by Order entered March 28, 2017 (the "District Court Order"). *Lynch v. Vaccaro*, 566 B.R. 290, 292 (E.D.N.Y. 2017), *aff'd sub nom. Frank v. Lynch*, 728 F. App'x 71 (2d Cir. 2018). In so doing, the District Court stated:

> Likewise, this Court "fail[s] to see how [it] could order a [$540,000] refund to the purchaser without affecting the validity of the sale." *The Charter Co.*, 829 F.2d at 1056; *see also Parker*, 499 F.3d at 622 (holding that Section 363(m) precludes granting relief that would "materially modify" the value of the sale asset). Further, allowing Frank to devalue Harbor Drive by recouping from the bankruptcy estate the premium she paid above the Contract price would implicate the policy concerns that Congress addressed by enacting Section 363(m). *See WestPoint*, 600 F.3d at 248-49 (noting that opening a final sale to an appellate challenge would encourage "a purchaser [to] demand a discount for the purchase of assets in which the terms and conditions of the sale cannot be protected from challenge even after closing the sale"). As noted, statutory mootness safeguards "the uniquely important interest in assuring the finality of a sale that is completed pursuant to 11 U.S.C. § 363(b) or (c) in bankruptcy proceedings," *id.* at 248, and thus consummation of a sale in bankruptcy greatly limits the ability of reviewing courts to fashion effective relief," *Parker*, 499 F.3d at 621.

Lynch v. Vaccaro, 566 B.R. at 304.

On June 25, 2018, the U.S. Court of Appeals for the Second Circuit entered a summary order affirming the District Court Order. *Frank v. Lynch*, 728 F. App'x 71 (2d Cir. 2018).

This adversary proceeding

On December 27 2018, the Trustee filed this adversary proceeding. He alleges, *inter alia*, as follows:

> 12. On January 25, 2016, Defendant filed a proof of claim in the sum of $125,000.00 arising from a contract deposit which she claimed to be secured against [Harbor Drive] (the "Original Claim").
>
> 13. On March 7, 2016, Defendant filed an amended proof of claim in the sum of $540,000.00 of which she claims $132,500.00 is secured by a "vendee's lien" against the [Harbor Drive] and $407,500.00 is unsecured (the "Amended Claim" [and together the "Frank Proofs of Claim"]).
>
> ....
>
> 20. Vaccaro, as receiver, entered into a contract of sale with Defendant dated April 8, 2014 (the "Contract of Sale") providing for her purchase of [Harbor Drive].
>
> ***4** 21. The Debtor was the sole fee owner of the [Harbor Drive] on the date the Contract of Sale was executed.
>
> 22. The Contract of Sale scheduled a closing for June 4, 2014.
>
> 23. Upon information and belief, the closing did not proceed in June 2014 due to a stay granted to the Debtor by the Supreme Court of the State of New York.

24. Defendant moved into the Real Property when the closing did not proceed in June 2014.

25. Defendant entered into and took possession of [Harbor Drive] without the consent of either Vaccaro, as receiver, or the Debtor.

26. On April 1, 2015, the Supreme Court of the State of New York replaced Vaccaro as receiver with Stephen O'Brien, Esq. ("O'Brien").

27. Defendant was in possession of [Harbor Drive] on the date of O'Brien's appointment as substitute receiver.

28. Upon information and belief, Defendant continued to be in possession of [Harbor Drive] through March 24, 2016, when she closed on the purchase of [Harbor Drive] as the high bidder at a public auction sale for the Real Property held on February 22, 2016.

29. The Contract of Sale did not provide Defendant with a preclosing right of possession.

30. Defendant provided no consideration for her use and occupancy of [Harbor Drive] from June 2014 through March 24, 2016.

Complaint, Para. 12-30. [dkt item 1]

The Trustee asserts four causes of action; the first two are essentially the same – for recovery of use and occupancy by Frank of Harbor Drive from June 2014 through March 24, 2016 in the amount of no less than $150,000.00; and the second two are for disallowance of the Frank Proofs of Claim.

On, January 25 2019, Frank filed her Motion to Dismiss, an affidavit in support of Fredrick P. Stern, ESQ., and a memorandum of law in support. [dkt items 4, 5]

On February 21, 2019, the Trustee filed his opposition and affidavit in support (the "Opposition"). [dkt items 8, 9]

On March 6, 2019, Frank filed a reply memorandum of law in support of her Motion to Dismiss along with a declaration in further support of Fredrick P. Stern, ESQ., (the "Reply"). [dkt items 11, 12]

Both Frank and the Trustee rely on documents which are not attached to or incorporated into the Complaint.

Discussion

Legal Standard for the Motion to Dismiss

This Court has addressed the application of Rule 12(b) and the flexible plausible pleading standard established by the Supreme Court on numerous occasions. *See Devices Liquidation Trust v. Pinebridge Vantage Partners (In re Pers. Commun. Devices, LLC)*, 528 B.R. 229, 233-34 (Bankr. E.D.N.Y. 2015), discussing *Ashcroft v. Iqbal*, 556 U.S. 662, 677-79, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009) and *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 546, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007); *Moxey v. Pryor (In re Moxey)*, 522 B.R. 428, 437-38 (Bankr. E.D.N.Y. 2014); *In re Ippolito*, 2013 WL 828316, at *3 (Bankr. E.D.N.Y. Mar. 6, 2013); *see also In re Int'l Tobacco Partners, Ltd.*, 462 B.R. 378, 385 (Bankr. E.D.N.Y. 2011); *In re Jones*, 2011 WL 1549060, at *2-3 (Bankr. E.D.N.Y. Apr. 21, 2011); *In re Coletta*, 391 B.R. 691, 693-94 (Bankr. E.D.N.Y. 2008).

Under the U.S. Supreme Court's *Iqbal/Twombly* analysis, a complaint must contain sufficient factual matter, which, when accepted as true, is adequate to "state a claim to relief that is plausible on its face" to survive a motion to dismiss. *Iqbal*, 556 U.S. at 678, 129 S.Ct. 1937; *Twombly*, 550 U.S. at 570, 127 S.Ct. 1955. A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the relief sought. *Iqbal*, 556 U.S. at 678, 129 S.Ct. 1937; *Twombly*, 550 U.S. at 556, 127 S.Ct. 1955. The plausibility standard "asks for more than a sheer possibility that a defendant has acted" so as to create liability. *Iqbal*, 556 U.S. at 678, 129 S.Ct. 1937. Where a complaint pleads facts that are "merely consistent with" a defendant's liability, it "stops short of the line between possibility and plausibility of 'entitlement to relief.' " *Id.* (quoting *Twombly*, 550 U.S. at 557, 127 S.Ct. 1955) (internal citations omitted).

***5** Neither *Iqbal* nor *Twombly* departed from the standard that, in considering a Rule 12(b)(6) motion, a court is to accept as true all factual allegations in the complaint and draw all inferences in favor of the plaintiff. *Iqbal*, 556 U.S. at 678-79, 129 S.Ct. 1937; *Twombly*, 550 U.S. at 555-56, 127 S.Ct. 1955;

see also *Cleveland v. Caplaw Enters.*, 448 F.3d 518, 521 (2d Cir. 2006). However, as the Supreme Court stated in *Iqbal*, "[t]hreadbare recitals of the elements of a cause of action, supported by mere conclusory statements, do not suffice." *Iqbal*, 556 U.S. at 678, 129 S.Ct. 1937. Moreover, a court need not "accept as true a legal conclusion couched as a factual allegation," and "[d]etermining whether a complaint states a plausible claim for relief will ... be a context-specific task that requires the reviewing court to draw on its judicial experience and common sense." *Id.* at 678-79, 129 S.Ct. 1937 (citing FED. R. CIV. P. 8(a)(2)).

In deciding the Motion to Dismiss, this Court must limit its review to facts and allegations contained in the Complaint, documents incorporated into the Complaint by reference or attached as exhibits and matters of which this Court may take judicial notice. *Blue Tree Hotels, Inv. (Canada), Ltd. v. Starwood Hotels & Resorts Worldwide, Inc.*, 369 F.3d 212, 217 (2d Cir. 2004); *see* *Staehr v. Hartford Fin. Servs. Group*, 547 F.3d 406, 425 (2d Cir. 2008) (Courts may take judicial notice of court filings to establish that matters have been publicly asserted, but not for the truth of the matters asserted in them); *Kavowras v. N.Y. Times Co.*, 328 F.3d 50, 57 (2d Cir. 2003) ("Judicial notice may be taken of public filings"). The Court may also "consider documents that are integral to the complaint ...." *Int'l Tobacco Partners, Ltd.*, 462 B.R. at 385; *see also* *Watts v. Jackson Hewitt Tax Serv. Inc.*, 579 F. Supp. 2d 334, 344 (E.D.N.Y. 2008) ("A document is integral to the complaint where the complaint relies heavily upon its terms and effects." (internal citations and quotation marks omitted)). Further, this Court has the authority to consider "the full text of documents that are quoted in the complaint or documents that the plaintiff either possessed or knew about and relied upon in bringing the suit." *Holmes v. Air Line Pilots Association*, 745 F. Supp. 2d 176, 198 (E.D.N.Y. 2010) (internal citations omitted). If the documents contradict the allegations of the Complaint, the documents themselves control and the Court does not need to accept as true any contradictory allegations concerning those documents. *Id.*

Conversion of the Motion to Dismiss to a Motion for Summary Judgment

Defendant asserts (a) the Complaint fails to allege a landlord-tenant relationship between the parties in connection with Franks' possession of Harbor Drive, which, according to Frank, is a requirement for a claim for relief for use and occupancy under New York law; and (b) the causes of action seeking to disallow the Frank Claims should be dismissed because "Debtor's breach of the contract by her actions which prevented the Frank Contract from closing pre-petition amounts to a rejection of the executory contract which allows Frank to seek an allowance of her claim under Section 502." *See Memorandum of Law in Support of Defendant, Patricia M. Frank's Motion to Dismiss Pursuant To FRCP 12(b)(6)*. [dkt item 6]

Plaintiff argues, however, that a landlord-tenant relationship existed because Frank took possession of Harbor Drive for temporary occupancy in exchange for repairs she was making to Harbor Drive; additionally the Complaint seeks unjust enrichment for Frank's possession of Harbor Drive. Plaintiff asserts that Frank's request for rejection damages has already been addressed by the Court in connection with the sale of Harbor Drive, Frank actively participated in the auction process by increasing her offer for Harbor Drive to $1,865,000 and thereby waived her claims.

***6** For the Court to consider the fact-based assertions made by both parties which are not attached to or incorporated into the Complaint, the Court must convert the Motion to Dismiss to a motion for summary judgment, and afford all parties a reasonable opportunity to present material pertinent to the motion. *See* FED. R. CIV. P. 12(d); FED. R. BANKR. P. 7012(b) *Cole v. Bourke*, 2016 U.S. Dist. LEXIS 16517, at *9-10 (E.D.N.Y. Jan. 27, 2016) ("[t]he essential inquiry in determining whether it is appropriate to convert a motion to dismiss into a motion for summary judgment is whether the non-movant should reasonably have recognized the possibility that the motion might be converted into one for summary judgment or was taken by surprise and deprived of a reasonable opportunity to meet facts outside the pleadings.") (internal citations and quotations omitted); *In re Gadsden*, 128 B.R. 45, 48 (Bankr. E.D.N.Y. 1991) (the bankruptcy court may treat a motion to dismiss as a motion for summary judgment if it gives both parties notice and a reasonable opportunity to submit affidavits and extraneous evidence so as to avoid taking a party by surprise).

Further, it appears to the Court that because many, but not all, of the disputes in this adversary proceeding are matters of law and not issues of fact, they may be susceptible of determination under Rule 7056.

Thus, in accordance with Rule 7001, 7012 and 7056, the Court will convert the Motion to Dismiss to one for summary judgment and afford the parties with a reasonable opportunity to submit affidavits and additional materials.

Based on the foregoing; it is hereby

ORDERED, that the Motion to Dismiss is hereby converted to a motion for summary judgment; and it is further

ORDERED, that the parties shall comply with the following deadlines: the parties shall file a joint statement of material facts pursuant to Bankruptcy Rule 7056 and Local Bankruptcy Rule 7056-1 on or before **October 15, 2019**; Frank and the Trustee may file a statement of additional facts on or before **October 29, 2019,** and each may file a response to the additional statements on or before **November 12, 2019**, and it is further

ORDERED, that the Trustee may cross move for full or partial summary judgment on or before **October 15, 2019,** in which case Frank may file a supplemental brief in opposition on or before **November 12, 2019**, and it is further

ORDERED, that this matter shall be on submission with the Court as of **November 13, 2019**.

All Citations

Slip Copy, 2019 WL 4584146

Footnotes

1 The factual background and procedural history are taken from the pleadings and exhibits submitted by the parties.

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2019 WL 4438963
Only the Westlaw citation is currently available.
United States Bankruptcy Court, E.D. New York.

IN RE: Mary Marjorie ATKINSON, Debtor.

Case No.: 19-71044-ast
|
Signed September 16, 2019

Attorneys and Law Firms

Richard F. Artura, Phillips, Artura & Cox, Lindenhurst, NY, for Debtor.

DECISION AND ORDER GRANTING RELIEF FROM THE AUTOMATIC STAY, CO-DEBTOR STAY, AND IN REM RELIEF

Alan S. Trust, United States Bankruptcy Judge

***1** Pending before the Court is the motion (the "Stay Relief Motion") of Wells Fargo Bank, N.A. as servicing agent for U.S. Bank National Association, as Trustee for MASTR Asset Backed Securities Trust 2006-WMC2, Mortgage Pass-Through Certificates, Series 2006-WMC2 ("U.S. Bank" or "Movant") seeking, among other things, in rem relief pursuant to 11 U.S.C. § 362(d)(4)(B) as to property located at 15 Hampton Place, Freeport, NY 11520 (the "Property"). The Court has concluded that U.S. Bank has met its burden of proof pursuant to 11 U.S.C. § 362(d)(4)(B) for in rem relief. Therefore, U.S. Bank's Stay Relief Motion is granted.

JURISDICTION AND VENUE

This Court has jurisdiction over this core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A), (G), and 1334(b), and the Standing Orders of Reference in effect in the Eastern District of New York dated August 28, 1986, and as amended on December 5, 2012, but made effective *nunc pro tunc* as of June 23, 2011.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The following constitutes this Court's findings of fact and conclusions of law made in accordance with Rule 7052 and 9014 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules").

Procedural history [1]

On January 15, 2018, Mary Atkinson ("Debtor"), represented by counsel, filed a voluntary petition under chapter 7 of title 11 of the United States Code (the "Bankruptcy Code"), assigned case number 18-70305-ast (the "First Case"). On March 2, 2018, U.S. Bank filed a motion for relief from the automatic stay as to the Property. [case no. 18-70305-ast; dkt item 10] After notice and a hearing, on June 5, 2018, the Court entered an Order granting U.S. Bank relief from the automatic stay as to the Property. [case no. 18-70305-ast; dkt item 13] On June 20, 2018, the Court entered a Final Decree [case no. 18-70305-ast; dkt item 14] and issued a notice closing the case without Debtor receiving a discharge, due to Debtor's failure to timely file a certification of financial management course or official form 423, as required by Interim Bankruptcy Rules 1007(b)(7) and 1007(c). [case no. 18-70305-ast; dkt item 15]

On September 10, 2018, Debtor, represented by counsel, filed a voluntary petition under chapter 7 of the Bankruptcy Code, assigned case number 18-76107-ast (the "Second Case"). On October 26, 2018, U.S. Bank filed another motion for relief from the automatic stay as to the same Property. [case no. 18-76107-ast; dkt item 10] After notice and a hearing, on November 21, 2018, the Court entered an Order granting U.S. Bank relief from the automatic stay as to the Property. [case no. 18-76107-ast; dkt item 11] On December 12, 2018, the Court entered an Order granting Debtor a chapter 7 discharge. [case no. 18-76107-ast; dkt item 15]

On February 13, 2019, Debtor, acting *pro se*, filed this her third case and her first under chapter 13 of the Bankruptcy Code.

***2** Marianne DeRosa was appointed the Chapter 13 Trustee (the "Trustee").

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U.S. Bank again moved for stay relief on March 12, 2019 [dkt item 14], this time also seeking relief from the co-debtor stay pursuant to 11 U.S.C. § 1301(c) and in rem relief pursuant to § 362(d)(4) (the "Third Motion"). In support of the Third Motion, U.S. Bank attached a Judgment of Foreclosure and Sale (the "Judgment of Foreclosure") entered on May 23, 2017 in the Supreme Court for the County of Nassau in favor of U.S. Bank against Debtor among others. Additionally, U.S. Bank asserted that, since April 2012, no one had made a payment on the note in the original principal amount of $400,000.00 secured by a mortgage on the Property, that the secured debt had swelled to the amount of $806,069.84, and the Property has a value of $400,000. U.S. Bank asserts that Debtor's First Case, Second Case, and this Third Case were each filed within approximately one week of scheduled foreclosure sales of the Property.

The Court heard the Third Motion on April 4, 2019 (the "Hearing"). U.S. Bank, Debtor, and the Trustee appeared at the Hearing; Debtor represented she was seeking to retain an attorney to assist her with her bankruptcy case. Pursuant to the record of the Hearing, the transcript of which is incorporated herein by reference, the Court found cause to conditionally grant the Motion pursuant to 11 U.S.C. §§ 362(d)(1), (4) and 1301(c) and directed U.S. Bank to settle a proposed order on the Debtor on 14 day's notice; the Court provided Debtor with the opportunity to file an objection to the proposed order and established that Debtor had the burden to show that she can adequately protect U.S. Bank's interest in the Property and that her proposed chapter 13 plan has a viable chance of being confirmed.

On April 10, 2019, the Trustee filed a motion to dismiss Debtor's case (the "Motion to Dismiss"). [dkt item 16]

On April 12, 2019, U.S. Bank filed a notice of settlement of proposed order (the "Notice of Settlement") and an affidavit of service on Debtor. [dkt item 17]

On April 25, 2019, Richard F. Artura ("Debtor's Counsel") appeared on behalf of Debtor and filed a letter in opposition to the Notice of Settlement along with a counter order (the "Opposition"). [dkt item 18] Debtor does not challenge the factual allegations concerning her defaults, the loan balance, the Property value, or the scheduled foreclosure sales, nor does she claim that U.S. Bank lacks standing to seek stay relief. Debtor's Opposition also does not address how she can adequately protect U.S. Bank's interest in the Property nor why her proposed chapter 13 plan is viable. The sole objection made by Debtor is to granting in rem relief.

On May 2, 2019, the Court held a hearing on the Motion to Dismiss, at which Debtor, Debtor's Counsel, and the Trustee appeared. The Court granted the Motion to Dismiss, and reserved only on the issue of in rem relief.

In rem stay relief

Congress added Section 362(d)(4) to the Bankruptcy Code in 2005, to address perceived abuses in the bankruptcy process by repeat filers. This section provides that the Court can Order that any and all future filings by any person or entity with an interest in the subject property will not operate as an automatic stay against the creditor and its successors and/or assigns for a period of two years after the date of the entry of such an order, if the Court finds that the filing of the bankruptcy filing was part of a scheme to delay, hinder, and defraud creditors that involved either-

> ***3** (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.

11 U.S.C. § 362(d)(4). *See In re Montalvo*, 416 B.R. 381, 386 (Bankr. E.D.N.Y. 2009). Here, U.S. Bank bears the burden of demonstrating a scheme to hinder, delay and defraud. *Id.*; *see also In re Lemma*, 394 BR. 315 (Bankr. E.D.N.Y. 2008); *In re Blair*, No. 09-76150-AST, 2009 WL 5203738, at *4 (Bankr. E.D.N.Y. Dec. 21, 2009).

In *Montalvo*, this Court joined those courts which hold that the mere timing and filing of several bankruptcy cases is an adequate basis from which a court can draw a permissible inference that the filing of a subsequent case was part of a scheme to hinder, delay, and defraud creditors. *Montalvo*, 416 B.R. 386; *Blair*, 2009 WL 5203738, at *4. (citations omitted). "The extent of the efforts by a debtor to prosecute [their] bankruptcy case and '[t]he timing and sequencing of the filings' are important factors in determining whether a debtor has engaged in 'a scheme to delay, hinder, and defraud.' " *In re Richmond*, 513 B.R. 34, 38 (Bankr. E.D.N.Y. 2014). "[T]he language [in section 362(d)(4)] was deliberately chosen by

Congress to impose a substantial burden of proof on secured creditors ....” *In re O'Farrill*, 569 B.R. 586, 591 (Bankr. S.D.N.Y. 2017) (citing 3 Collier on Bankruptcy ¶ 362.05[19][a]). *But see In re Gray*, 558 F. App'x 163, 166 (3d Cir. 2014) (multiple bankruptcy filings do not alone justify relief under 11 U.S.C. § 362(d)(4)(B)).

This Court has determined that U.S. Bank has met its burden of proof. Debtor filed two prior cases to stave off foreclosure sales, and in each case this Court granted U.S. Bank stay relief. While Debtor did earn her chapter 7 discharge in her Second Case, which mitigates in her favor, it does not preclude this Court from drawing the inference it has drawn; had Debtor's goal been just to obtain a discharge she could have avoided a second filing by simply completing her post-petition financial management education course in her First Case or by filing after the foreclosure sale was complete and any deficiency determined. Debtor has not provided evidence of any payments she made to U.S. Bank during or after any of the three bankruptcy filings, and she did not have a viable chapter 13 plan in this case. Debtor's mortgage was nearly seven years in default, had been under a foreclosure judgement for nearly two years prior to filing this case, and the Property value was substantially under the mortgage debt. The clear evidence before this Court is that this case is part of the type of multiple filing scheme for which Congress enacted § 362(d)(4).

Conclusion

Based thereon, having considered the evidence presented and the arguments of the parties, and with good cause appearing therefor, it is hereby

ORDERED, that the automatic stay in effect pursuant to 11 U.S.C. § 362(a), is hereby terminated pursuant to 11 U.S.C. § 362(d)(1) for cause, as to U.S. Bank, its agents, assigns or successors in interest, so that U.S. Bank, its agents, assigns or successors in interest, may take any and all action under applicable state law to exercise its remedies against the Property; and it is further

***4 ORDERED**, that the co-debtor stay under 11 U.S.C. § 1301(a) is also terminated as to U.S. Bank, its agents, assigns or successors in interest, so that U.S. Bank, its agents, assigns or successors in interest, may take any and all action under applicable state law to exercise its remedies against the Property; and it is further

ORDERED, that pursuant to 11 U.S.C. § 362(d)(4), if recorded in compliance with applicable state laws governing notices of interests or liens in real property, this Order shall be binding in any other case under this title purporting to affect the Property filed not later than **two (2) years** after the date of the entry of this Order, except that a debtor in a subsequent case under this title may move for relief from this Order based upon changed circumstances or for good cause shown, after notice and hearing; and it is further

ORDERED, that the Chapter 13 Trustee shall be served with a copy of the referee's report of sale within thirty (30) days of the report, and shall be noticed with any surplus monies realized from the sale of the Property; and it is further

ORDERED, that all other relief sought in the Motion is denied.

All Citations

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Footnotes

1 The factual background and procedural history are taken from the pleadings, exhibits, stipulations and other papers submitted by the parties in the above-captioned case.

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2020 WL 717411
Only the Westlaw citation is currently available.
United States Bankruptcy Court, E.D. New York.

IN RE: Kyle E. NORTON, dba Norton Law Group LLC dba The Law Offices of Kyle Norton PC, Debtor.
Juan A. Viles, Dianna Burkeen, Gary Burkeen, Danielle D'andrea, Frank D'andrea, Pamela Kelly, Timothy Kelly, Plaintiffs
v.
Kyle E. Norton, Defendant.

Case No.: 8-17-70855-ast
|
Adv. Proc.: 8-17-08125-ast
|
Signed January 14, 2020
|
Entered 01/15/2020

Attorneys and Law Firms

Raymond W. Verdi Jr., Patchogue, NY, for Defendant.

Eli J. Vonnegut, Davis Pok & Wardwell, LLP, New York, NY, for Plaintiffs.

ORDER GRANTING PLAINTIFFS MOTION FOR SUMMARY JUDGMENT

Alan S. Trust, United States Bankruptcy Judge

Procedural history

***1** On February 15, 2017 (the "Petition Date"), Kyle E. Norton (the "Debtor" or "Defendant") commenced his Chapter 7 case by filing a voluntary petition for relief under Chapter 7 of title 11 of the United States Code, 11 U.S.C. § 101, et seq. (the "Bankruptcy Code") in the United States Bankruptcy Court for the Eastern District of New York (the "Bankruptcy Court").

On April 21, 2017, the above caption plaintiffs (the "Plaintiffs") filed a Complaint against Debtor. [dkt no. 1] That same day, Plaintiffs' also filed a declaration of Eli H. Vonnegut in support of Plaintiffs' Complaint. [dkt item 2]

On May 24, 2017, Defendant filed an answer to the Complaint. [dkt item 9]

On August 10, 2017, Plaintiffs filed a motion for judgment on the pleadings (the "MJP"). [dkt item 11]

On September 6, 2017, Defendant filed an affidavit in opposition. [dkt item 14]

On March 12, 2019, the Court held a hearing and determined that the MJP should be converted to a motion for summary judgment.

By Order entered April 5, 2019 [dkt item 22], the Court converted the MJP to a motion for summary judgment and set specific deadlines related thereto.

On April 22, 2019, Plaintiffs timely filed their Rule 7056 Statement. [dkt item 23]

Defendant did not file any further pleadings.

Claims and litigation background

The State Court Action

Plaintiffs had filed suit in 2014 in New York Supreme Court in Nassau County (the "State Court") against Kyle Norton, Norton Law Group, and the Law Offices of Kyle Norton Aviles, under No. 10882/2012 (the "State Court Action"). Plaintiffs alleged common law fraud and other causes of action in connection with a loan modification scam principally designed and carried out by Norton. More specifically, Plaintiffs alleged they are low income/middle income New York homeowners who suffered financial hardship and fell behind on mortgage payments, and that when they sought help, they became victims of false advertising and a fraudulent loan modification scheme run by Norton. The scheme included Norton advertising his services and extremely high success rates; he charged a fixed up-front fee between $2,500-$5,000 and often told plaintiffs that he anticipated his fees would end up totaling less. Upon signing up with Norton, Plaintiffs were prohibited under their retainer agreements from speaking with their lenders. Once Norton received Plaintiffs' fees, he ceased communications with them. In most cases, Norton never communicated with

the lenders either, but still badgered plaintiffs for additional fees approaching double the amounts initially charged.

In 2011, the NY Attorney Grievance Committee for the 10th Judicial District officially admonished Norton Law Group.

On January 31, 2013, after Defendant failed to comply with document requests, Plaintiffs filed a motion to compel.

On June 18, 2013, Defendant produced certain documents, but withheld other documents responsive to the documents request.

On January 28, 2014, following Defendant's failure to produce documents responsive to the documents request, Plaintiffs moved to compel their production.

***2** On February 26, 2014, the State Court entered an order granting Plaintiffs' motion and compelling Defendants to produce the requested documents (the "Order to Compel").

Following Defendants failure to comply with the Order to Compel, on August 15, 2014 the State Court entered a decision striking their answer and granting judgment in favor of Plaintiffs. On May 4, 2015, the State Court entered judgment awarding damages in favor of each of the Plaintiffs, aggregating $204,100.63 (the "Judgment"). Collection efforts on the Judgment ceased when Norton filed this bankruptcy.

This Adversary Proceeding

In their Complaint, Plaintiffs request this Court determine that the damages awarded to them in the Judgment are nondischargeable under Section 523(a)(2) for actual fraud and false representations, and under Section 523(a)(4) for fraud while acting in fiduciary capacity as an attorney.

Through the MJP as converted to a motion for summary judgment, Plaintiffs assert that they should prevail as a matter of law based upon collateral estoppel and/or res judicata. Their request is support by the April 21, 2017 Declaration of Eli J. Vonnegut [dkt item 2], to which are attached various exhibits from the State Court Action:

- Exhibit A - Verified Complaint (detailing fraud against each plaintiff)
- Exhibit B - Decision and Order (granting judgment for plaintiffs)
- Exhibit C – Judgment
- Exhibit D – Answer (just denied all allegations in the complaint)
- Exhibit E – 2012 Document Requests
- Exhibit F – Document Production Order
- Exhibit G - Motion to Strike (strike defendants answer)
- Exhibit H – Non-party subpoena
- Exhibit I – Judgment-debtor subpoena
- Exhibit J – Motion to Compel (compliance with subpoenas)
- Exhibit K – Order to Compel
- Exhibit L - Contempt Order
- Exhibit M – Scheduling Stip
- Exhibit N – Norton 2016 Email Thread
- Exhibit O – Norton 2017 Email Thread
- Exhibit P – Affirmation of Adam G Mehes

Norton has not filed any controverting evidence.

Jurisdiction and Venue

This Court has jurisdiction over this core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A), (B), (I) and 1334(b), and the Standing Orders of Reference in effect in the Eastern District of New York dated August 28, 1986, and as amended on December 5, 2012, but made effective *nunc pro tunc* as of June 23, 2011.

Findings of Fact and Conclusions of Law

The Court is not required to state findings of fact and conclusions of law when ruling on summary judgment motions, pursuant to FRCP 52(a)(3), as incorporated by Rule 7052 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules").

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A. The Standard for Summary Judgment

Rule 56(c) of the Federal Rules of Civil Procedure, as incorporated by Bankruptcy Rule 7056(c), provides that summary judgment should be granted to the moving party if the Court determines that "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 n.4 (1986) (quoting FED. R. CIV. P. 56(c)) (internal quotation marks omitted). A movant has the initial burden of establishing the absence of any genuine issue of material fact. *Celotex*, 477 U.S. at 322-23. A fact is "material" if it "might affect the outcome of the suit under the governing law." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). An issue of fact is genuine "if the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Id.* If the movant meets its initial burden, the nonmoving party "must do more than simply show that there is some metaphysical doubt as to the material facts." *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 586 (1986). "If the evidence is merely colorable, or is not significantly probative, summary judgment may be granted." *Anderson,* 477 U.S. at 249-50 (internal citations omitted).

***3** The Second Circuit has repeatedly noted that, "[a]s a general rule, all ambiguities and inferences to be drawn from the underlying facts should be resolved in favor of the party opposing the motion, and all doubts as to the existence of a genuine issue for trial should be resolved against the moving party." *Brady v. Town of Colchester*, 863 F.2d 205, 210 (2d Cir. 1988) (citing *Celotex Corp.*, 477 U.S. at 330 n.2 (1986) (Brennan, J., dissenting)); *see also Tomka v. Seiler Corp.*, 66 F.3d 1295, 1304 (2d Cir. 1995); *Burrell v. City Univ. of New York,* 894 F. Supp. 750, 757 (S.D.N.Y. 1995). "If, when viewing the evidence produced in the light most favorable to the non-movant, there is no genuine issue of material fact, then the entry of summary judgment is appropriate." *Pereira v. Cogan*, 267 B.R. 500, 506 (S.D.N.Y. 2001); *see Burrell*, 894 F. Supp. at 758 (citing *Binder v. Long Island Lighting Co.*, 933 F.2d 187, 191 (2d Cir. 1991)).

B. Collateral Estoppel (Issue Preclusion)

It is well settled that a party may invoke the common law doctrines of collateral estoppel (issue preclusion) and res judicata (claim preclusion) to preclude another party from relitigating claims and issues that have already been decided in prior litigation. *See Allen v. McCurry*, 449 U.S. 90, 94 (1980); *Marvel Characters, Inc. v. Simon*, 310 F.3d 280, 286 (2d Cir. 2002) (a final judgment on the merits of an action precludes the parties or their privies from relitigating claims that were or could have been raised in the first action). Bankruptcy courts may apply issue preclusion in non-dischargeability litigation. *Grogan v. Garner*, 498 U.S. 279, 284 (1991) ("If the preponderance standard also governs the question of nondischargeability, a bankruptcy court could properly give collateral estoppel effect to those elements of the claim that are identical to the elements required for discharge and which were actually litigated and determined in the prior action."); *see also Ball v. A.O. Smith Corp.*, 451 F.3d 66, 69 (2d Cir. 2006); *Evans v. Ottimo*, 469 F.3d 278, 281 (2d Cir. 2006).

In addition to federal courts being asked to give preclusive effect to each other's judgments, federal courts are often called upon to give preclusive effect to judgments of the state courts, and vice versa. *Grogan*, 456 U.S. at 284-86; *Kelleran v. Andrijevic*, 825 F.2d 692, 694 (2d Cir. 1987) ("Congress has specifically required all federal courts to give preclusive effect to state-court judgments whenever the courts of the State from which the judgments emerged would do so...." quoting *Allen,* 449 U.S. at 96); *see also* U.S. CONST. art. IV, § 1 (Full Faith and Credit Clause); 28 U.S.C. § 1738 (1982).

Because Norton's liability was decided under state law, this Court will apply New York's rules of preclusion and will not engage in a separate analysis under the federal standards. *See De Curtis v. Ferrandina* (*In re Ferrandina*), 533 B.R. 11 (Bankr. E.D.N.Y. 2015).

In *Evans*, the Second Circuit addressed a substantially similar issue: whether chapter 7 debtors in a nondischargeability action should be permitted to relitigate their liability for fraud determined under a prepetition New York state default judgment. 469 F.3d at 280. The *Evans* debtors were properly served with a state court complaint which alleged fraud, failed to respond to that complaint, and failed to appear for the subsequent inquest at which the plaintiff offered evidence of the debtors' fraud; however, the *Evans* debtors failed to contest the state court's default fraud judgment before

filing for bankruptcy. *Id.* at 282. The *Evans* court held that collateral estoppel should be applied because the debtors were previously afforded a full and fair opportunity to litigate the issue of fraud and because the state court necessarily decided the issue. *Id.* at 282-83.

***4** More recently, the Second Circuit addressed collateral estoppel in the context of a federal court default judgment entered as a sanction against an appearing party. *Murphy v. Snyder* (*In re Snyder*), 939 F.3d 92 (2d Cir. 2019). The circuit court noted that "A party seeking to invoke collateral estoppel must establish that "(1) the identical issue was raised in a previous proceeding; (2) the issue was actually litigated and decided in the previous proceeding; (3) the party had a full and fair opportunity to litigate the issue; and (4) the resolution of the issue was necessary to support a valid and final judgment on the merits." *Ball*, 451 F.3d at 69 (internal quotation marks omitted). The court then turned to the requirement that the underlying issue be "actually litigated," noting that standard "generally bars a court from giving a default judgment preclusive effect. *See*, *e.g.*, *Abrams v. Interco Inc.*, 719 F.2d 23, 33 n.9 (2d Cir. 1983) (observing that the "accepted view" is "that the decision of issues not actually litigated, e.g., a default judgment, has no preclusive effect in other litigation")." The Second Circuit then stated:

> We join several other circuits in recognizing an exception to that rule: where the default judgment is entered as a sanction for bad conduct, and the party being estopped had the opportunity to participate in the underlying litigation, the default judgment has preclusive effect when determining the nondischargeability of a debt in a bankruptcy proceeding. [citation omitted].
>
> Affording a default judgment entered as a sanction preclusive effect furthers the goal of imposing the sanction in the first instance because it deprives the sanctioned party an opportunity to relitigate an issue that could and should have been decided in the first litigation.

Snyder, 939 F.3d at 101-102. This Court had reached a similar conclusion in *Ferrandina*, given the substantial participation of the debtor there in the pre-petition federal district court litigation.

Norton has provided no basis for this Court to deviate from this standard as enunciated by the Second Circuit in *Snyder*, nor argued that a different outcome would result from applying New York law. For the reasons to follow, this Court has determined that issue preclusion should be applied.

Applicability of issue preclusion to the State Court Judgment

1. Identity of Issues

The first issue the Court must decide is whether Plaintiffs' § 523(a)(2) claim for fraud in connection with the loan modification scam was necessarily decided in the State Court Action. *See Evans*, 469 F.3d at 282 ("[F]or a question to have been actually litigated so as to satisfy the identity requirement, it must have been properly raised by the pleadings or otherwise placed in issue and actually determined in the prior proceeding." (quoting *D'Arata*, 76 N.Y.2d at 667)). Section 523(a)(2)(A) provides that a debt is nondischargeable under circumstances where the debt is, "for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by – (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition." 11 U.S.C. § 523(a)(2)(A). *See Husky Int'l Elecs., Inc. v. Ritz*, 136 S. Ct. 1581, 194 L. Ed. 2d 655 (2016). False pretenses, false representation, and actual fraud represent three different concepts, and thus are treated as three separate causes of action. *In re Crossfield*, 2012 WL 3637919, at *3 (Bankr. E.D.N.Y. Aug. 22, 2012); *In re Hambley*, 329 B.R. 382, 396 (Bankr. E.D.N.Y. 2005).

Courts in this circuit have found the elements of common law fraud to be "virtually identical" to the elements of § 523(a)(2). *See, e.g.*, *In re Ottimo*, 2017 WL 2470861, at *4; *In re Adamo*, 560 B.R. 642, 648 (Bankr. E.D.N.Y. 2016); *In re Ippolito*, No. 12-70632-AST, 2013 WL 828316, at *5 (Bankr. E.D.N.Y. Mar. 6, 2013). Thus, to determine whether there is an identity of issues, this Court must closely analyze the allegations raised by Plaintiffs in the State Court Action and the elements of § 523(a)(2).

***5** Incident to their fraud claim, Plaintiffs' State Court complaint alleged, among other things, that Debtor (i) represented that he was negotiating with Plaintiffs' lenders and performing work for Plaintiffs, when he performed little to no work regarding Plaintiffs' issues; and (ii) made specific representations to Plaintiffs identifying certain programs that

they would qualify for and certain results that he could deliver within certain periods of time, which ended up being false. Plaintiffs' State Court complaint included an express cause of action for common law fraud in which Plaintiffs asserted that Debtor (i) "made intentional misrepresentations and/or failed to provide material information"; (ii) "made these representations and omissions knowing that they were false at the time they were made"; (iii) "offered these statements as fact, not opinion, with the intent to induce Plaintiffs to purchase their loan modification services, to convince Plaintiffs to remain as clients, or to prevent Plaintiffs from learning the true nature of Defendants" scheme"; (iv) Plaintiffs "had a reasonable right to rely and in fact relied" on the Debtors' claims; and (v) "Plaintiffs suffered damages as a direct and proximate result of their reasonable and justified reliance on the Debtors' intentional misrepresentations and failures to disclose." Thus, the fraud claim as alleged in Plaintiffs' State Court complaint bear a close identity of issues with Plaintiffs' § 523(a)(2) fraud claim here.

Because this Court did not find a claim plead in the State Court Action that was bore an identity to a § 523(a)(2) false pretenses claim, it will not analyze the false pretenses claim for issue preclusion purposes.

2. Actually litigated issue and decided in the prior action

The next issue is whether the underlying fraud claim was actually ligated, and decided in State Court. As noted above, where the default judgment is entered as a sanction for bad conduct, and the party being estopped had the opportunity to participate in the underlying litigation, courts can give preclusive effect to a post-answer default judgment.

Here, the Judgment was entered as a result of Debtor repeatedly failing to comply with Plaintiffs' discovery requests by withholding responsive documents for nearly a year, and failing to comply with the Order to Compel, thus, qualifying as bad conduct. Further, Debtor had the opportunity to participate in the underlying litigation by complying with the discovery requests. Given the Judgement was entered as a sanction for bad conduct, and Debtor having had the opportunity to participate in the underlying litigation, the Court finds the underlying issue was actually litigated and decided in the State Court Action.

3. Full and fair opportunity to litigate

The Court must next determine whether Debtor had a full and fair opportunity to litigate the fraud claim. The record of the proceedings in State Court detailed above leading up to the filing of this bankruptcy demonstrate that he did.

On August 24, 2012, Debtor was properly served with a state court complaint alleging, *inter alia*, fraud. Debtor answered the complaint on October 19, 2012. Despite answering the complaint, Debtor failed to comply with Plaintiffs' discovery and the Order to Compel, resulting in the State Court striking Debtors' answer and granting Judgment in favor of plaintiffs on May 4, 2015. Debtor failed to seek to set aside or appeal the Judgment for nearly 2 years prior to filing for bankruptcy on February 15, 2017.

As such, Debtor was afforded a full and fair opportunity to litigate his liability for fraud, and he should not be allowed to relitigate his liability here.

4. Resolution of the issue was necessary to support a valid and final judgment on the merits

The final requirement is whether the resolution of the issue was necessary to support a valid and final judgment on the merits. Here, the State Court's resolution of the properly plead fraud claim was necessary to the Judgment it entered; thus, collateral estoppel should be applied.

Nondischargeability under 523(a)(2)

As noted above, the state law fraud claim and the § 523(a)(2) actual fraud claim are essentially the same and therefore collateral estoppel should apply. As such the liability established under the Judgment is nondischargeable.

Nondischargeability under 523(a)(4)

As this Court has determined that the liability established under the Judgment is nondischargeable under § 523(a)(2), there is no need to address Plaintiffs § 523(a)(4) claim.

***6** Based on the foregoing, it is hereby

ORDERED, that the motion for summary judgment is granted; and it is further

ORDERED, that liability established under the Judgment in favor of each Plaintiff under the Judgment is nondischargeable; and it is further

ORDERED, that a Final Judgment hereon shall issue.

All Citations

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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NEW YORK
----------x
In re
JOE'S FRIENDLY SERVICE & SON, INC.,
d/b/a THATCHED COTTAGE AT THE BAY,

Chapter 7
Case No. 8-14-70001-reg

Debtor.
----------x
In re
THATCHED COTTAGE LP,

Chapter 7
Case No. 8-14-70002-reg
(Jointly Administered)

Debtor.
----------x
BETHPAGE FEDERAL CREDIT UNION and
BUSINESS SERVICES GROUP, LLC,

Plaintiffs,

-against-

Adv. Pro. No. 8-16-8035-reg

THE TOWN OF HUNTINGTON,
JOSEPH F. CLINE, INDIVIDUALLY,
RICHARD VACCHIO, INDIVIDIUALLY, and
TERENCE "TERRY" MCNALLY, INDIVIDUALLY,

Defendants.
----------x

Decision

Before the Court is the defendants' motion for a determination that this Court lacks subject matter jurisdiction over this adversary proceeding filed by non-debtors Bethpage Federal Credit Union ("BFCU") and Business Services Group, LLC ("BSG") (together, the "Plaintiffs") against non-debtors the Town of Huntington (the "Town"), Joseph F. Cline, individually ("Cline"), Richard Vacchio, individually ("Vacchio"), and Terence "Terry" McNally, individually ("McNally") (collectively, the "Defendants"). The Debtors, Joe's Friendly Service

& Son, Inc., d/b/a Thatched Cottage at the Bay ("Joe's Friendly") and Thatched Cottage LP ("Thatched LP") (collectively, the "Debtors"), are not parties to this adversary proceeding.

On September 24, 2014, pursuant to an Order of this Court, the chapter 7 trustee of the Debtors' jointly administered estates conducted an auction sale of substantially all the Debtors' assets under section 363 of the Bankruptcy Code (the "Code"). These assets consisted of real property and an accompanying well-known catering hall located in Centerport, NY. Pursuant to the terms of this sale, and as a result of the failure of the successful bidder to close on the purchase, the Plaintiffs as the backup bidder, were required to purchase the property from the estate. The Plaintiffs assert the Defendants' "placarding" (i.e., condemnation) of the catering hall building in the midst of the sale process was a primary cause of the winning bidder's decision to default on his contractual obligation and that this resulted in the Plaintiffs economic loss and other damages. The Plaintiffs assert that the Defendants did not follow proper procedures when placarding the building and allege due process and equal protection violations, negligence, and various other state tort claims. The Plaintiffs allege the Defendants conspired with the Debtors' principal to make the property economically unattractive to potential buyers which caused material harm to the Debtors' creditors and that these actions by the Defendants were done in violation of the Bankruptcy laws and in violation this Court's order mandating a sale of the property to the highest bidder.

The Plaintiffs chose the state court as its forum to assert these claims alleging damages in connection with the placarding of the building. It was the Defendants who removed the subject action to this Court and asserted that this Court has subject matter jurisdiction over the lawsuit and should exercise that jurisdiction. The Plaintiffs, having selected the state court to litigate these claims, moved to remand the action. However, the parties reached an agreement by which

they stipulated to have this matter heard before this Court and memorialized the agreement in a stipulation which was so-ordered by this Court on July 11, 2016. As per the stipulation, the Plaintiffs withdrew their motion to remand and submitted to the entry of final orders by this Court. Despite having removed this action to this Court and despite having entered into the July 11, 2016 so-ordered stipulation, which is a final non-appealable order of this Court, the Defendants filed an answer to the amended complaint on December 27, 2016 contesting this Court's jurisdiction to hear this matter.[1] This Court's lack of subject matter jurisdiction was most recently raised by Defendants' motion, dated December 17, 2019 [ECF No. 164] ("Motion"). The Court denied that Motion at the commencement of trial on January 13, 2020 and indicated that this written decision would follow.

The Defendants' Motion suffers from a litany of infirmities. First, it is the Defendants themselves who argued that this Court has subject matter jurisdiction over this lawsuit; the Plaintiffs wanted to be in state court. The representations in the Defendants' current motion are in direct conflict with prior representations that the Defendants made to ensure removal of this proceeding from state court. Second, by so-ordering the stipulation which caused the Plaintiffs to withdraw their motion to remand and submit to this Court's final orders, the Court necessarily found that it had subject matter jurisdiction over the dispute. That order is now final and non-appealable. Finally, the Defendants cite no change in fact or law to support or justify their change in position. In essence, the Defendants denied the Plaintiffs their desired forum and induced them to accept the change based on representations that the Defendants now seek to

[1] The Defendants retained new counsel on October 4, 2016 which may explain the apparent change in litigation strategy.

disavow. There is no tenable justification for the change in position other than Defendants' change in legal counsel subsequent to the date of the so-ordered stipulation.

The Court will not permit the Defendants to now argue that this Court lacks subject matter jurisdiction where this action was brought to this Court by the Defendants themselves; the Defendants represented that this Court has subject matter jurisdiction over this matter; the Plaintiffs relied on Defendants representations and their agreement to have this Court issue final orders in connection with this case; and this issue was previously determined by a so-ordered stipulation of the parties which has not been appealed.

Even so, examined on the merits, the Court finds that it has subject matter jurisdiction over this matter. Where a proceeding between non-debtors alleges damages resulting from a concerted effort to interfere with the administration of the estate pursuant to a court-ordered sale of estate assets, the proceeding is "core," and the bankruptcy court has subject matter jurisdiction over the dispute. *See* 28 U.S.C. § 157(b). The allegations against the Defendants raise issues which directly affect the integrity of this Court and the bankruptcy sale process. This Court surely has jurisdiction to hear such a dispute.[2]

For these and the reasons that follow, the Defendants' Motion is denied.

[2] The Court makes no findings of fact in this Decision other than those facts necessary to find subject matter jurisdiction. The trial of this matter is ongoing and the allegations of bad acts by the Defendants are still *sub judice*.

Factual Background[3]

Pre-petition, the Debtor, Thatched LP, owned property at 445 East Main Street, Centerport, New York (the "Property"). A catering hall operated by Debtor, Joe's Friendly, was located on the Property (the "Thatched Cottage"). The Property was encumbered by a mortgage held by Plaintiff, BFCU. Non-debtor, Ralph Colamussi ("Colamussi") was the principal of both Debtors and was integral to the day-to-day management of the Thatched Cottage.

The Property, located on the waterfront, was allegedly damaged by hurricanes in August of 2011 and October of 2012. Despite apparent efforts by Colamussi to obtain the funds to implement repairs to the Thatched Cottage, the record reflects that the damage was largely unremediated. During this time, although Colamussi was informed that improvements to the Property encroached onto property belonging to the Town, at no time did the Town inform Colamussi that the encroachments or hurricane damage necessitated a shutdown of the catering facility. The Debtors eventually defaulted on the BFCU loan, and BFCU commenced a foreclosure action on September 6, 2013.

On January 2, 2014, Thatched LP and Joe's Friendly filed separate voluntary petitions pursuant to chapter 11 of the Code. *See In re Joe's Friendly Serv. & Son, Inc.*, No. 14-BK-70001 (Bankr. E.D.N.Y.) (Grossman, Bankr. J.); *In re Thatched Cottage LP*, No. 14-BK-70002 (Bankr. E.D.N.Y.) (Grossman, Bankr. J.). The cases were jointly administered but not substantively consolidated. The Property constitutes the most valuable asset in Debtors' estates. The Thatched Cottage continued operations as a debtor-in-possession with no restrictions placed on it by the

[3] Unless stated otherwise, the facts herein are derived from *Bethpage Fed. Credit Union v. Town of Huntington (In re Joe's Friendly Serv. & Son, Inc.),* No. 16-AP-8035 (REG), 2019 WL 1313519 (Bankr. E.D.N.Y. Mar. 21, 2019*)*; *Bethpage Fed. Credit Union v. Town of Huntington (In re Joe's Friendly Serv. & Son, Inc.),* No. 19-CV-2010 (JS), 2019 WL 6310207 (E.D.N.Y. Nov. 25, 2019).

Town. In fact, the Town inspected the Property in its ordinary course and issued an occupancy and assembly permit on August 18, 2014.

After issues regarding Colamussi's mental health and fitness to operate the Thatched Cottage arose, the Court found that a chapter 11 trustee should be appointed. R. Kenneth Barnard was appointed as the chapter 11 trustee on July 14, 2014. The chapter 11 trustee moved to sell the Property pursuant to section 363(b) of the Code on July 24, 2014, which motion was granted. Pursuant to Court order entered August 11, 2014 authorizing the chapter 11 trustee to sell the Property (the "Sale Order"), a sale of the Property "as is" and "without all faults," was scheduled for September 24, 2014. At the auction sale, the chapter 11 trustee determined that Yama Raj ("Raj") was the highest bidder at $4,650,000 plus a buyer's premium of $186,000 for a total of $4,836,000, and that BFCU was the second highest bidder with a credit bid of $4,600,000 (the "Sale"). BFCU was bound by the terms of the Sale and required to close in the event of Raj's default pursuant to the bidding procedures approved by this Court. The Sale was originally scheduled to close on November 15, 2014.

Prior to the auction sale, on August 27, 2014, Colamussi emailed to the chapter 11 trustee engineering reports allegedly documenting unsafe conditions and costly repairs required at the Thatched Cottage. Colamussi also discussed the damage to the Thatched Cottage with the auctioneer prior to the sale. On September 23, 2014 Colamussi attempted suicide.

On October 6, 2014, the chapter 11 trustee, who had been winding down operations light of the impending sale, ceased operations at the Thatched Cottage.

On November 13, 2014, Colamussi hand-delivered to the Town's Fire Marshall's Office a package containing engineering reports indicating that the Thatched Cottage was unsafe (the "Colamussi Reports"). The Colamussi Reports were circulated throughout the Town

Supervisor's Office on November 14, 2014. On November 17, 2014, even though the catering hall had operated for many years at the same location with no interference from the Town, the Town advised Raj that the Thatched Cottage would not be permitted to reopen until an engineering report proved that the Thatched Cottage was safe and Raj entered into a licensing agreement regarding the encroachments onto Town property.

Although Raj endeavored to obtain engineering reports showing that the Property was safe, Town employees relying exclusively on the Colamussi Reports, placarded the Property on November 20, 2014. The placard stated in part: "This Building is hereby declared unsafe and unfit for human habitation pursuant to the Code of the Town of Huntington. The Occupancy of this dwelling or any party thereof is unlawful." The placard also advised that violators would be subject to a $15,000 fine and/or six months imprisonment and included a telephone number for the Town. The placard did not assert a specific section of the Town Code or any other reason for the placarding.

In contravention of Town Code provisions, the Town failed to notify the Debtors, BFCU, the chapter 11 trustee or the Court that the building was unfit for occupancy or that repairs were necessary. The Town placarded the Property despite being in the midst of discussions with Raj concerning the Thatched Cottage's condition and despite the fact that the Property was the subject of a bankruptcy proceeding and protected by the automatic stay of section 362(a) of the Bankruptcy Code.

Shortly after the Town placarded the Property, Raj refused to close on the sale and BFCU, through its servicer Plaintiff, BSG, was required to take title the Property as the back-up bidder under the Sale Order.

This case was converted to chapter 7 on June 24, 2015. R. Kenneth Barnard was appointed the chapter 7 trustee. Over the next year and a half, the Town and Plaintiffs were in regular communication. The Defendants' attorney informed the Plaintiffs' attorney that no person should be inside the Thatched Cottage until the structural defects have been addressed by a professional engineer or architect who advised that the Thatched Cottage is safe or until permit plans have been submitted to the Town. The Plaintiffs commissioned an engineering report that was submitted to the town on April 16, 2016 (the "Pacifico Report"). On April 19, 2016, three days after receipt of the Pacifico Report, the Town removed the placard. Shortly after the removal of the placard, the Plaintiffs contracted to sell the Thatched Cottage for $2,800,000. The sale closed in September of 2016.

Procedural History

A. The State Court Action and Removal to This Court

The Plaintiffs commenced an action in New York State Supreme Court, Suffolk County, on February 11, 2016 (the "Litigation") alleging Defendants' misconduct in connection with the posting of the placard. The claims arise out of allegations that the Defendants orchestrated a plan with Colamussi to interfere with the sale of the Property by attempting to make the Property economically and physically unattractive to a third-party buyer; and the Defendants failed to follow proper procedures in determining whether to post the placard which ultimately harmed Plaintiffs due to the significant decline in value of the Property resulting from the placarding. The chapter 7 trustee commenced an adversary proceeding against the Town and Town employees asserting violations of state law and 42 U.S.C. § 1983 based on facts similar to those alleged in the Plaintiff's Litigation. *See Barnard v. Town of Huntington*, No. 16-AP-8025 (Bankr. E.D.N.Y.) (Grossman, Bankr. J.).

The Defendants removed the Litigation to this Court on March 11, 2016 stating that "most of the factual allegations supporting each of the claims asserted in the [Litigation] relate to acts, occurrences or matters that either took place during the Bankruptcy Case or were addressed by [the Bankruptcy Court]"; "the Bankruptcy Court has jurisdiction over each cause of action asserted in the [Litigation]"; and the Litigation is a "core proceeding under 28 U.S.C. § 157, including subsections (A) and (N)." Notice of Removal 3. In the Notice of Removal, the Defendants "consent[ed] to the entry of final orders or judgments" by this Court "[t]o the extent any cause of action [ ] is subsequently determined to be non-core." Notice of Removal 3. After the Plaintiffs opposed removal and moved for remand, the parties entered into a so-ordered stipulation, where the Plaintiffs withdrew their motion to remand, consented to removal, and provided the Defendants with an extension of time to file an answer (the "So-Ordered Stipulation").

B. Litigation in the Bankruptcy Court

The Plaintiffs filed an amended complaint on August 12, 2016 asserting claims for tortious interference with contractual relations, tortious interference with prospective economic advantage, negligence, deprivation of procedural and substantive due process/deprivation of property rights pursuant to 42 U.S.C. § 1983, denial of equal protection pursuant to 42 U.S.C. § 1983, conspiracy pursuant to 42 U.S.C. § 1983, and attorneys' fees pursuant to 42 U.S.C. § 1988 (the "Amended Complaint"). The Defendants retained new counsel on October 4, 2016.

The Defendants filed a motion to dismiss the Amended Complaint which was primarily based on the assertion that the Plaintiffs lacked standing. The Court denied the Defendants' motion in its entirety on December 5, 2016. The Defendants filed an answer to the Amended

Complaint on December 27, 2016, adding the affirmative defense that the Defendants do not consent to the entry of final orders or judgment by this Court.

A pre-trial conference was held on January 11, 2017. The Defendants filed a motion to withdraw the reference on January 23, 2017. The Defendants did not obtain a stay of the Litigation pending the outcome of the motion, the matter proceeded in the bankruptcy court and the Court issued a pre-trial order setting a discovery deadline of April 28, 2017.

C. Summary Judgment

On July 31, 2017, the Defendants filed a motion for summary judgment, which the Plaintiffs opposed. The Court denied the Defendants' motion for summary judgment in its entirety on March 21, 2019.[4] The Defendants appealed the order denying summary judgment on the basis that the individually named Defendants are entitled to immunity. The District Court affirmed the denial of the Defendants' summary judgment motion on the basis of qualified immunity and dismissed the appeal with respect to the substantive due process and equal protection claims for lack of jurisdiction.

D. Motion for a Determination that this Court Lacks Subject Matter Jurisdiction

On November 25, 2019, the District Court issued a decision denying the Defendants' request to withdraw the reference to this Court. The District Court refrained from ruling on the Defendants' allegations that this Court did not have subject matter jurisdiction, finding that "[b]ecause the Court has denied the motion to withdraw the reference, the bankruptcy court should decide in the first instance any motion to dismiss for lack of subject matter jurisdiction."

[4] The Court reopened discovery on January 29, 2018 based on newly discovered evidence, and the parties filed supplemental briefs on April 13, 2018 which rendered the summary judgment motion fully submitted.

Bethpage Fed. Credit Union v. Town of Huntington (In re Joe's Friendly Service & Son Inc.), 17-MC-0190 (JS), 2019 WL 6307468, at *8 (E.D.N.Y. Nov. 25, 2019).

On December 17, 2019, the Defendants filed the instant motion for an order determining that this Court lacks subject matter jurisdiction to hear and adjudicate this proceeding. The Defendants assert that the Plaintiffs' claims do not "arise under" the Code, "arise in" the Debtors' bankruptcy cases, or "relate to" the Debtors' bankruptcy cases (the "Dfs' Mot." or "Defendants' Motion"). The Plaintiffs oppose the motion arguing that their claims "arise under" the Code, "arise in" the Debtors' bankruptcy cases, and "relate to" the Debtors' bankruptcy cases. The Plaintiffs also argue that the Defendants should be estopped from adopting a position regarding the Court's subject matter jurisdiction that is inconsistent with the Defendants' previous positions (the "Pls' Opp'n"). The Defendants filed a reply on January 10, 2020 (the "Dfs' Reply").

The Court ruled on the motion at the commencement of trial on January 13, 2020, finding that it has subject matter jurisdiction, and indicated that this written Decision would follow. The trial is currently scheduled to recommence on July 20, 2020.

Discussion

A. The Defendants Initiated Removal of this Litigation to the Bankruptcy Court

The statutory basis to remove a case from state court to federal court is governed by title 28 of the United States Code. "Except as otherwise expressly provided by Act of Congress, any civil action brought in a State court of which the district courts of the United States have original jurisdiction, may be removed by the defendant or the defendants, to the district court of the United States for the district and division embracing the place where such action is pending." 28 U.S.C. § 1441. "[D]istrict courts [ ] have original and exclusive jurisdiction of all cases under

title 11." 28 U.S.C. § 1334(a). "[T]he district courts [ ] have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11" notwithstanding "any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts" and except as stated in 28 U.S.C. § 1334(e)(2). 28 U.S.C. § 1334(b). Under 28 U.S.C. § 1334(e), "[t]he district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction (1) of all the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate;" and "(2) over all claims and causes of action that involve construction of section 327 of title 11, United States Code, or rules related to disclosure requirements under section 327." 28 U.S.C. § 1334(e).

With respect to removal to bankruptcy court, "[a] party may remove any claim or cause of action in a civil action other than a proceeding before the United States Tax Court or a civil action by a governmental unit to enforce such governmental unit's police or regulatory power, to the district court for the district where such civil action is pending, if such district court has jurisdiction of such claim or cause of action under section 1334 of this title." 28 U.S.C. § 1452.

The process of removing a case to a bankruptcy court is governed by Rule 9027 of the Federal Rules of Bankruptcy Procedure ("Fed. R. Bankr. P." or "Bankruptcy Rule"). To remove a case to a bankruptcy court, "a notice of removal [must] be filed with the clerk for the district and division within which is located the state or federal court where the civil action is pending" and must "contain a short and plain statement of the facts which entitle the party filing the notice to remove, contain a statement that upon removal of the claim or cause of action, the party filing the notice does or does not consent to entry of final orders or judgments by the bankruptcy court, and be accompanied by a copy of all process and pleadings." Fed. R. Bankr. P. 9027(a)(1). After

filing a notice of removal, the filing party must serve a copy of the notice of removal on all parties to the removed claim or cause of action as well as a copy with the clerk of court from which the claim or cause of action is removed. Fed. R. Bankr. P. 9027(b), (c).

Removal of the claim or cause of action is "effected" on the filing of the notice of removal. Fed. R. Bankr. P. 9027(c); 28 U.S.C. § 1446. If the civil action was initiated before the subject bankruptcy case, a notice of removal must be filed within the longer of 90 days after the order for relief in a case under the Code, 30 days after entry of an order terminating a stay if the subject proceeding was stayed under section 362 of the Code, or "30 days after a trustee qualifies in a chapter 11 reorganization case but not later than 180 days after the order for relief." Fed. R. Bankr. P. 9027(a)(2). If the civil action was initiated after the subject bankruptcy case, "a notice of removal may be filed with the clerk only within the shorter of (A) 30 days after receipt, through service or otherwise, of a copy of the initial pleading setting forth the claim or cause of action sought to be removed, or (B) 30 days after receipt of the summons if the initial pleading has been filed with the court but not served with the summons." Fed. R. Bankr. P. 9027(a)(3). "A motion to remand the case on the basis of any defect other than lack of subject matter jurisdiction must be made within 30 days after the filing of the notice of removal under section 1446(a). If at any time before final judgment it appears that the district court lacks subject matter jurisdiction, the case shall be remanded." 28 U.S.C. § 1447(c).

After removal to the district court, or bankruptcy court if the case has been referred to a bankruptcy judge, the bankruptcy judge, "may issue all necessary orders and process to bring before it all proper parties whether served by process issued by the court from which the claim or cause of action was removed or otherwise." Fed. R. Bankr. P. 9027(e)(1). A party who filed a pleading in connection with the removed claim or cause of action but did not file the notice of

removal "shall file a [signed] statement that the party does or does not consent to final orders or judgment by the bankruptcy court" within 14 days after the filing of the notice of removal. Fed. R. Bankr. P. 9027(e)(3).

Removal is a very powerful tool which may deprive a plaintiff of its choice of forum and should not be employed frivolously. The Defendants submitted to this Court's jurisdiction by filing a notice of removal under 28 U.S.C. § 1452 and representing that this Court had subject matter jurisdiction over the Litigation. Unlike the Plaintiffs, who were deprived of their chosen forum upon the filing of the notice of removal, the Defendants actively sought this forum. The Plaintiffs opposed the notice of removal by filing a motion to remand. Instead of stipulating to remand as the Defendants should have if they really did believe this Court lacked subject matter jurisdiction over the Litigation, the Defendants again submitted to this Court's jurisdiction in a stipulation so-ordered by this Court. As a result, Plaintiffs withdrew their motion for remand and agreed litigate here. The Defendants' subsequent efforts to undo the removal and the So-Ordered Stipulation is puzzling, at best.

B. Reconsideration

Although not styled as a motion to reconsider the So-Ordered Stipulation, this Court finds that the instant Motion by the Defendants is just that. In the So-Ordered Stipulation, the Court necessarily, albeit implicitly, found it had subject matter jurisdiction.[5] The Defendants are in effect seeking to reverse this finding and as such, the Defendants' Motion may be considered as

[5] The Court similarly did so when it denied the Defendants' motions to dismiss and for summary judgment. *See* Order Denying Mot. to Dismiss Adversary Proceeding 1, December 12, 2016, ECF No. 34; *Bethpage Fed. Credit Union v. Town of Huntington (In re Joe's Friendly Serv. & Son, Inc.)*, No. 16-AP-8035 (REG), 2019 WL 1313519 (Bankr. E.D.N.Y. Mar. 21, 2019*). See Tancredi v. Metro. Life Ins. Co.*, 378 F.3d 220, 225 (2d Cir. 2004) ("In dismissing, and affirming the dismissal of, plaintiffs' complaint for failure to state a claim, both the district court and this Court implicitly recognized subject matter jurisdiction.").

a motion for reconsideration. *See Byrne v. Liquid Asphalt Sys., Inc.*, 250 F.Supp.2d. 84, 88 (E.D.N.Y. 2003). Defendants neither appealed nor sought leave to appeal the So-Ordered Stipulation. *See* 28 U.S.C. § 158. Reconsideration of the So-Ordered Stipulation is time-barred. Even if it were not, reconsideration would be denied on the merits as discussed below. Moreover, Defendants should not be permitted to this back-door challenge to subject matter jurisdiction that it freely consented to.

Motions to reconsider are analyzed under Bankruptcy Rule 9023, which incorporates Rule 59 of the Federal Rules of Civil Procedure ("Fed. R. Civ. P." or "Federal Rule of Civil Procedure") and Bankruptcy Rule 9024 which incorporates Federal Rule of Civil Procedure 60. Federal Rule of Civil Procedure 60(b) permits a party to seek relief from a "*final* judgment, order, or proceeding." It does not provide for relief from interlocutory orders. *Remington Prod., Inc. v. N. Am. Philips, Corp.*, 755 F. Supp. 52, 54 (D. Conn. 1991) ("[Federal Rule of Civil Procedure] 60(b) applies only to final determinations and not to interlocutory orders.") (citing *Fennell v. TLB Kent Co.*, 865 F.2d 498, 501 (2d Cir. 1989))." Interlocutory orders may be challenged pursuant to Bankruptcy Rule 9023. *See Byrne*, 250 F.Supp.2d.at 88; E.D.N.Y. LBR 9023-1(b) ("A motion for reconsideration of an order may be made pursuant to Bankruptcy Rule 9023").

The So-Ordered Stipulation here was an interlocutory order subject to review under Bankruptcy Rule 9023, as it "did not end the adversary proceeding on the merits . . . [or] dispose of discrete issues within the adversary proceeding." *North Fork Bank v Abelson*, 207 B.R. 382, 389 (E.D.N.Y. 1997); *Menoken v. McNamara*, 213 F.R.D. 193, 195 (D.N.J. 2003) ("[A]n order denying remand to the state court, finding removal was proper, is generally not appealable as a final order.").

Pursuant to Local Bankruptcy Rule 9023-1(b), "a motion for reconsideration of an order may be made pursuant to Bankruptcy Rule 9023." Rule 9023 states,

> Except as provided in this rule and Rule 3008, Rule 59 FR Civ P applies in cases under the Code. A motion for a new trial or to alter or amend a judgment shall be filed, and a court may on its own order a new trial, no later than 14 days after entry of judgment. In some circumstances, Rule 8008 governs post-judgment motion practice after an appeal has been docketed and is pending.

"A motion to reconsider must be filed within 14 days of the entry of the judgment." *In re Hassan*, 527 B.R. 97, 102 (Bankr. E.D.N.Y. 2015); *see also* Fed. R. Bankr. P. 9001(7) ("judgment" in this context means any appealable order); 28 U.S.C. § 158(a)(3) (interlocutory orders are appealable with leave of court).

Here, the So-Ordered Stipulation was docketed on July 11, 2016. The Defendants' Motion was filed on December 12, 2019, which is several years beyond the 14 days allotted by Bankruptcy Rule 9023 and the Court is precluded from enlarging the Defendants' time to file the motion to reconsider. Fed. R. Bankr. P. 9006(b)(2) ("The court may not enlarge the time for taking action under Rules 1007(d), 2003(a) and (d), 7052, 9023, and 9024"). Therefore a motion for reconsideration would be untimely.

Courts have found that when a motion brought under Rule 9023 is untimely, it should be evaluated under Rule 9024. *See In re 231 Fourth Avenue Lyceum LLC*, 513 B.R. 25, 30 (Bankr. E.D.N.Y. 2014) ("As the Motion [to reargue a lift-stay motion] is untimely under Bankruptcy Rule 9023, it will be evaluated as a motion under Bankruptcy Rule 9024, which incorporates [FRCP] 60(b)"). Even still, a motion pursuant to Federal Rule of Civil Procedure 60(b) would be untimely, as it "must be made within a reasonable time—and for reasons (1), (2), and (3) no more than a year after entry of the judgment or order or the date of the proceeding." Fed. R. Civ.

P. 60(c)(1). Bankruptcy Rule 9006(b) similarly prohibits enlargement of time. Therefore, to the extent this Motion seeks to reconsider this Court's prior finding on subject matter jurisdiction, the motion may be denied as untimely under both Rules 9023 and 9024. *Kyriazi v. Rumsfeld*, 67 Fed.Appx. 7, 10 (2d Cir. 2003) (affirming a district court's denial of a FRCP 60(b) motion as untimely).

Even if reconsideration of the So-Ordered Stipulation were not time-barred under Bankruptcy Rules 9023 and 9024, the Court would still deny reconsideration on the merits. The Second Circuit has held that the "standard for granting a motion for reconsideration is strict, and reconsideration will generally be denied unless the moving party can point to controlling decisions or data that the court overlooked – matters, in other words, that might reasonably be expected to alter the conclusions reached by the court." *S. New England Telephone Co., v. Global Naps, Inc.*, No. 3:04-cv-2075 (JCH), 2007 WL 9757857, at *1 (D. Conn. Dec. 28, 2007) (quoting *Shrader v. CSX Transp., Inc*, 70 F.3d 255, 257 (2d Cir. 1995)). "There are three grounds that justify granting a motion for reconsideration: (1) an intervening change in controlling law; (2) the availability of newly discovered evidence; and (3) the need to correct clear error or prevent manifest injustice." *Id*. "That the court overlooked controlling law or material facts before it may also entitle a party to succeed on a motion to reconsider." *Id.* A motion for reconsideration "will not be granted if the party is merely seeking to relitigate the issue already decided by the court." *Byrne*, 250 F.Supp.2d at 88. "The decision to grant or deny a motion for reconsideration is within the sound discretion of the court." *Id.*

The Defendants do not assert an intervening change in controlling law or that new evidence is available. The only articulated change since the filing of the notice of removal is that the Plaintiffs amended their complaint, which the Defendants argue destroys this Court's subject

matter jurisdiction. Mot. 2-3. However, "after proper removal to federal court, post-removal amendments generally do not destroy statutory subject-matter jurisdiction." *In Touch Concepts Inc. v. Cellco P'ship,* 788 F.3d 98, 100-01 (2d Cir. 2015). The record is devoid of any evidence that reconsideration is necessary to "prevent manifest injustice" or that this Court "overlooked controlling law or material facts" that entitle the Defendants to reconsideration of the So-Ordered Stipulation. *Global Naps*, 2007 WL 9757857, at *1. To the extent the Defendants' Motion is in effect a motion to reconsider this Court's prior finding of subject matter jurisdiction, the Motion is denied.

C. Judicial Estoppel

The Plaintiffs argue that the Defendants should be judicially estopped from adopting the position that the Court lacks subject matter jurisdiction because the Defendants took the position that this Court had subject matter jurisdiction, obtained removal on that basis, and actively participated in this Litigation for nearly four years.

a. Applicable Standard

The Supreme Court has described the doctrine of judicial estoppel as follows:

> [W]here a party assumes a certain position in a legal proceeding, and succeeds in maintaining that position, he may not thereafter, simply because his interests have changed, assume a contrary position, especially if it be to the prejudice of the party who has acquiesced in the position formerly taken by him. This rule, known as judicial estoppel, generally prevents a party from prevailing in one phase of a case on an argument and then relying on a contradictory argument to prevail in another phase.

New Hampshire v. Maine, 532 U.S. 742, 749 (2001) (internal citations and quotations omitted). The purpose of the doctrine is "to protect the integrity of the judicial process by prohibiting parties from deliberately changing positions according to the exigencies of the

moment." *Id.* at 749-50 (internal citations and quotations omitted). While "[t]he circumstances under which judicial estoppel may appropriately be invoked are probably not reducible to any general formulation of principle," courts often weigh several factors in determining whether judicial estoppel should be applied to a specific case: (1) whether a party's later position is "clearly inconsistent" with its earlier position; (2) "whether the party has succeeded in persuading a court to accept that party's earlier position, so that judicial acceptance of an inconsistent position in a later proceeding would create the perception that either the first or second court was misled;" and (3) "whether the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped." *Id.* at 750-51 (internal citations and quotations omitted). These factors are not meant to serve as inflexible prerequisites or as an exhaustive formula, and courts are permitted to use "additional considerations" to "inform the doctrine's application in specific factual contexts." *Id.* at 751. The Second Circuit has "further limit[ed] judicial estoppel to situations where the risk of inconsistent results with its impact on judicial integrity is certain." *Intellivision v. Microsoft Corp.,* 484 Fed.Appx. 616, 619 (2d Cir. 2012) (summary order) (citing *Republic of Ecuador v. Chevron Corp.,* 638 F.3d 384, 397 (2d Cir. 2011)).

Although the Second Circuit has not held that judicial estoppel can never be applied to matters affecting subject matter jurisdictions, it has recognized that "as an equitable doctrine, judicial estoppel does not rest easily with the concept of standing, a prerequisite to federal subject matter jurisdiction" and that special care should be taken in determining whether judicial estoppel applies. *Id.* at 621 (internal citations and quotations omitted). With respect to subject matter jurisdiction, the Supreme Court held in *Ins. Corp. of Ir., Ltd. v. Compagnie des Bauxites de Guinee,* 456 U.S. 694 (1982), that "no action of the parties can confer subject-matter

jurisdiction upon a federal a court . . . [so] the consent of the parties is irrelevant, principals of estoppel do not apply, and a party does not waive the requirement by failing to challenge jurisdiction early in the proceedings." *Ins. Corp. of Ir.*, 456 U.S. at 702.[6] While judicial estoppel does not apply to positions taken on questions of law and cannot be used to confer subject matter jurisdiction as a matter of law, it may be applied to the factual representations that support a legal conclusion that subject matter jurisdiction exists. *See Techno-TM, LLC v. Fireaway, Inc.*, 928 F.Supp.2d 694, 698-99 (S.D.N.Y. 2013) (applying judicial estoppel to prevent members of the plaintiff company from assuming a contrary position with respect to their domicile and therefore finding that there was no diversity jurisdiction).

b. Application

The Defendants' current position that this Court lacks subject matter jurisdiction is "clearly inconsistent" with their prior position in securing removal of this action from state court. While judicial estoppel does not apply to legal arguments, it does apply to the inconsistent factual representations made in support of the inconsistent legal arguments asserted here. *See Techno-TM*, 928 F.Supp.2d 694 at 688-89. Specifically, the Defendants previously asserted that "[m]ost of the factual allegations supporting each of the claims asserted in the [Litigation] relate to acts, occurrences or matters that either took place during the Bankruptcy Case or were addressed by this Court in the Bankruptcy Case." Notice of Removal 3. The brevity of the Defendants' representation does not limit its broad scope; that is, the Defendants took the

[6] With respect to "principals of estoppel," the Supreme Court directly cited *Am. Fire & Cas. Co. v. Finn*, 341 U.S. 6, 17-18 (1951). *Id. American Fire* stood for the proposition that estoppel cannot create jurisdiction. *American Fire*, 341 U.S. at 16-18 (distinguishing cases where "[t]he defendant who had removed the action was held to be estopped from protesting that there was no right to removal," and reasoning that "[s]ince the federal court could have had jurisdiction originally, the estoppel did not endow it with a jurisdiction it could not possess.").

position in the notice of removal that this lawsuit relates to the sale of property of the estate which took place pursuant to an Order of this Court, and makes allegations that Defendants improperly interfered with the sale process.

The Defendants now take the position that this Litigation does not concern orders of this Court or property of the Debtors' estates. The Defendants have not alleged new facts, a change in law, or any tenable distinction that would reconcile its change in position. As such, the Court must conclude that the Defendants were either disingenuous in either their prior position, or the current one. After years of litigation and associated costs, acceptance of the Defendants' current position concerning subject matter jurisdiction without any change in the materials facts of this case would prejudice the Plaintiffs who have litigated in this forum for years and would be forced to incur additional expense if required to the re-litigate in a new forum.

The Court finds that the Defendants here are judicially estopped from contradicting their prior factual representation that "most of the factual allegations supporting each of the claims asserted in the [Litigation] relate to acts, occurrences or matters that either took place during the Bankruptcy Case or were addressed by this Court in the Bankruptcy Case." Notice of Removal 3. The result is that the Defendants' Motion is neutered of its support to the extent it conflicts with the Defendants' prior representation. The Defendants' are left with the argument that this Court lacks subject matter jurisdiction even though the factual allegations supporting the Plaintiffs' claims "relate to acts, occurrence or matters that either took place during the Bankruptcy Case or were addressed by this Court."

D. Promissory Estoppel

The Defendants represented in the notice of removal that "[t]o the extent any cause of action is subsequently determined to be non-core under 28 U.S.C. § 157, the Defendants consent

to the entry of final orders or judgments by the United States Bankruptcy Court." The Plaintiffs argue that this constituted a promise that the Plaintiffs relied on when they agreed to withdraw their objections to removal and that they would be prejudiced if the Defendants were permitted to renege on their promise in light of the substantial preparation and motion practice that has already occurred. Pls' Opp'n 16-17.

a. Applicable Standard

"A cause of action for promissory estoppel under New York law requires the plaintiff to prove three elements: 1) a clear and unambiguous promise; 2) reasonable and foreseeable reliance on that promise; and 3) injury to the relying party as a result of the reliance." *Kaye v. Grossman*, 202 F.3d 611, 615 (2d Cir. 2000).

b. Application

Black's Law Dictionary defines a "promise" as, "[t]he manifestation of an intention to act or refrain from acting in a specified manner, conveyed in such a way that another is justified in understanding that a commitment has been made; a person's assurance that the person will or will not do something;" and "[t]he words in a promissory note expressing the maker's intention to pay a debt." PROMISE, Black's Law Dictionary (11th ed. 2019); *See also CP Found. of Nassau, Inc. v. Meyers*, 17-CV-1866 (JMA)(AYS), 2019 WL 1384083, at *3 (E.D.N.Y. Mar. 27, 2019). Here, the Defendants manifested an intention in the notice of removal to permit this Court to bind both them and the Plaintiffs via final orders and judgments for non-core proceedings. The parties soon thereafter agreed to the So-Ordered Stipulation where the Plaintiffs agreed to withdraw their motion to remand and consented to removal. The Plaintiffs reasonably relied on the Defendants' promise in the form of their consent to the entry of final orders and judgments for non-core proceedings by this Court. The Plaintiffs entered into the So-Ordered Stipulation and withdrew

their motion to remand under the expectation that Defendants consented to the entry of final orders and judgments by this Court regardless of whether the proceedings were core or non-core. If this Court were to condone the Defendants late-hour change in litigation strategy Plaintiffs would be injured by the duplication of litigation efforts, and the associated costs, that would ensue if this matter were transferred back to state court. Accordingly, the Defendants are promissorily estopped from withdrawing their consent to this Court's entry of final orders and judgments in this matter.

E. Law of the Case

There are two branches to the law of the case doctrine. First, the "mandate rule" requires "a trial court to follow an appellate court's previous ruling on an issue in the same case." *U.S. v. Quintieri*, 306 F.3d 1217, 1225 (2d. Cir. 2002). "The second and more flexible branch is implicated when a court reconsiders its own ruling on an issue in the absence of an intervening ruling on the issue by a higher court." *Id.* There, once a "court has ruled on an issue, that decision should generally be adhered to by that court in subsequent stages of the same case unless cogent and compelling reasons militate otherwise." *Norton v. Town of Brookhaven*, 2:13-cv-3520 (ADS)(GRB), 2020 WL 364159, at *4 (E.D.N.Y. Jan. 21, 2020) (internal quotations and citations omitted). "Compelling reasons include an intervening change in law, availability of new evidence, or the need to correct a clear error or prevent manifest injustice. The law of the case doctrine is discretionary and does not limit a court's power to reconsider its own decisions." *Id.* (internal citations and quotations omitted). However, the law of the case doctrine does not apply to motions challenging a court's subject matter jurisdiction. *Id.* at *5.

The Plaintiffs argue that the Defendants' consent to jurisdiction became the law of the case after the Defendants represented that most of the factual allegations in this Litigation

related to acts, occurrences, or matters that occurred in the bankruptcy cases or were addressed by this Court, and the Court "accepted Defendants' representations as a basis to exercise its jurisdiction and expend valuable resources in adjudicating this matter." However, the law of the case doctrine should not be applied in this instance, and the Court may consider anew whether it has subject matter jurisdiction over the Litigation. *Norton*, 2020 WL 364159, at *5.

F. Subject Matter Jurisdiction

a. Applicable Standard

District courts have "original and exclusive jurisdiction of all cases under title 11." 28 U.S.C. § 1334(a). A district court may refer a bankruptcy case or proceeding to the bankruptcy judges for the district. 28 U.S.C. § 157(a). The Eastern District of New York has, by standing order, referred all cases arising under title 11 to the Bankruptcy Court. Eastern District of New York Standing Order of Reference dated August 28, 1986, as amended by Order dated December 5, 2012. "A bankruptcy court's power to adjudicate matters in a bankruptcy case turns in part on whether the proceedings are 'core' or 'non-core.'" *Kirschenbaum v. U.S. Dep't of Labor (In the Matter of Robert Plan Corp.)*, 777 F.3d 594, 596 (2d Cir. 2015). Core proceedings "aris[e] under" or "aris[e] in" a bankruptcy case. *Id.*; 28 U.S.C. § 157(b).

A proceeding "aris[es] under" the Code when it "clearly invoke[s] substantive rights created by federal bankruptcy law." *Robert Plan Corp.*, 777 F.3d at 596. A proceeding "aris[es] in" a bankruptcy case when it invokes "claims that are not based on any right expressly created by [the Code], but nevertheless, would have no existence outside of the bankruptcy." *Id.* at 596-97. Congress codified a non-exhaustive list of 16 different types of matters that constitute "core proceedings." 28 U.S.C. § 157(b)(2). A proceeding may also be "core" by virtue of its nature if either "(1) the type of proceeding is unique to or uniquely affected by the bankruptcy

proceedings, ... or (2) the proceeding[ ] directly affect[s] a core bankruptcy function." *Luan Inv. S.E. v. Franklin 145 Corp., (In re Petrie Retail, Inc.),* 304 F.3d 223, 229 (2d Cir. 2002) (internal citations omitted). "Bankruptcy judges may hear and enter final judgments in 'all core proceedings arising under title 11, or arising in a case under title 11.'" *Stern v. Marshall,* 564 U.S. 462, 474 (2011).

A bankruptcy court also has jurisdiction to "hear a proceeding that is not a core proceeding but that is otherwise related to a case under" the Code. 28 U.S.C. § 157(c)(1). Whether a proceeding is "related to a case under" the Code generally depends on "whether the outcome of the proceeding could conceivably have any effect upon the debtors' estate being administered." *Robert Plan Corp.,* 777 F.3d at 597. Some courts also find "related to" jurisdiction where the parties are sufficiently "intertwined" with a debtor. *Nemsa Establishment, S.A. v. Viral Testing Sys. Corp.,* No. 95-Cv-0277 (LAP), 1995 WL 489711, at *3-5 (S.D.N.Y. Aug. 15, 1995); *Ameritrust Co., N.A. v. Opti-Gage, Inc. (In re Opti-Gage, Inc.),* 128 B.R. 189, 195 (S.D. Ohio 1991) (holding "that proceedings are 'related to' bankruptcy cases not only where the outcome of the proceeding may conceivably have an effect upon the estate being administered, but also where parties are sufficiently *intertwined* with the debtor") (emphasis in original). "When a bankruptcy judge determines that a referred proceeding is not a core proceeding but is otherwise related to a case under title 11, the judge may only submit proposed findings of fact and conclusions of law to the district court." *Stern*, 564 U.S. at 475 (citing 28 U.S.C. § 157(c)(1)) (internal quotations omitted). The district court then enters a final judgment after a *de novo* review of any matter to which a party objects. *Id*. A bankruptcy judge may nevertheless enter appropriate orders and judgments for proceedings related to a case under title 11 if all parties to the proceeding consent. 28 U.S.C. § 157(c)(2).

b. Application

i. Core v. Non-Core

The Defendants maintain that there is no "arising under" or "arising in" jurisdiction. The Defendants allege that there is no "arising under" jurisdiction because the Plaintiffs' claims do not invoke a substantive right created by the Code, including the failure to allege a violation of the automatic stay. The Defendants also argue that the Plaintiffs' claims do not concern the administration of the estate because the Property was not property of the estate when the Plaintiffs commenced this action. The Defendants similarly claim that there is no "arising in" jurisdiction because the "[ ] Complaint does not assert any rights or claims arising from any orders entered by this Court, nor do Plaintiffs seek the interpretation of any orders of this Court." Dfs' Mot. 7. The Defendants assert that the "Plaintiffs' claims are based purely on federal non-bankruptcy and state law and could proceed in a court without bankruptcy jurisdiction," as the "substance of Plaintiffs' claims is whether they were damaged by Defendants' actions in the posting of the placard on the Thatched Cottage and maintaining that placard until April 2016." *Id.*

The Plaintiffs assert that the Defendants admitted that this Litigation was a "core" proceeding and a matter concerning the administration of the estate that included an order approving the sale of property of the estate. Pls' Opp'n 4 (citing 11 U.S.C. §§ 157(b)(2)(A), (N)). The Plaintiffs argue that the Thatched Cottage and accompanying land were the single largest assets in the Debtors' estates, which means that this matter necessarily concerned the administration of the bankruptcy estate. The Plaintiffs state that their damages were incurred in connection with BFCU's obligation as the second highest bidder under the Court's sale order and

bidding procedures to take title to the premises and the Town's allegedly unlawful placement and refusal to remove the placard for seventeen months.

The Plaintiffs rely on the Second Circuit's decision in *In re Petrie*, which "affirmed that a dispute between two non-debtors was a 'core' proceeding because, at the time of commencement, it involved (i) rights or obligations created by the Bankruptcy Court's sale order; and (ii) matters concerning the administration of the estate as to core bankruptcy functions." Pls' Opp'n 5 (citing *Petrie*, 304 F.3d at 229-30). The Plaintiffs analogize this matter to *Petrie*, stating that this adversary proceeding concerned the administration of the estate and the Plaintiffs' rights and obligations under the sale order. Further, the Plaintiffs contend that this adversary proceeding "flows" from the Court's administration of the Debtor's estate and is therefore a "core" matter. Pls' Opp'n 5 (citing *Sterling Vision, Inc. v. Sterling Optical Corp. (In re Sterling Optical Corp.)*, 302 B.R. 792, 807 (Bankr. S.D.N.Y. 2003)). The Plaintiffs contend that "this dispute has no practical existence outside of bankruptcy because it is inexorably intertwined with, and necessarily dependent upon, the subject debtors' bankruptcy petition." Pls' Opp'n 8.

In response to the argument that the Plaintiffs' claims "arise in" the Debtors' bankruptcy cases because their damages were incurred in connection with BFCU's obligations as the second highest bidder, the Defendants argue (1) the Plaintiffs are not seeking an interpretation of an order of the Court; (2) "the Amended Complaint does not make any allegation or assert any claim for damages as a result of Plaintiffs' obligation under the bid procedures and sale orders;" (3) the "Defendants had no obligations under any of the sale orders and there are no allegations that any of the Defendants forced Plaintiffs to bid at the auction;" and (4) "the sale orders do not direct Defendants to undertake any action and expressly provides that Plaintiffs are purchasing

the Thatched Cottage properties 'as is', 'where is' and subject to all faults, regulations, violations or conditions requiring corrective action." Dfs' Mot. 8. The Defendants argue that *Petrie* is inapplicable because, unlike *Petrie*, the Plaintiffs do not seek to enforce the sale and confirmation orders, and the Amended Complaint presents no issue in dispute that require the interpretation of an order of the Court. Dfs' Reply 5.

With respect to "arising under" jurisdiction, Plaintiffs have not identified any section other than section 362 of the Bankruptcy Code, that applies to its claims. However, any reliance by the Plaintiffs on the assertion that a violation of the automatic stay under section 362 created "arising under" jurisdiction is misplaced because none of the claims or pleadings in the Amended Complaint allege a stay violation.[7] Therefore, the Court finds that it does not have "arising under" jurisdiction under this analysis. However, the Plaintiffs were the largest secured creditor in this case, and the Plaintiffs' claims concern damages allegedly incurred through the administration of its collateral pursuant to section 363 of the Bankruptcy Code and orders of this Court, which is a matter affecting the administration of the estate.

Matters affecting the administration of the estate fall squarely within this Court's core jurisdiction. 28 U.S.C. § 157(b)(2)(A). The Property was the largest asset in the Debtors' estate. "The purpose of a § 363(b) sale is to transform assets . . . into cash in an effort to maximize value" and "the benefit to the debtor's entire estate." *In re TWA*, Case No. 01-00056 (PJW), 2001 Bankr. LEXIS 980, at *31-33 (Bankr. D. Del. Apr. 2, 2001). The Plaintiffs have alleged that the Defendants' actions were designed to thwart the sale of the Property to a person other than

[7] While the Court acknowledged the potential violation of the automatic stay in its Decision denying summary judgment, the Plaintiffs did not allege a violation of the automatic stay, nor is any relief sought by the Plaintiffs dependent on a finding of a violation of the automatic stay. *Joe's Friendly*, 2019 WL 1313519, at *9-10.

Colamussi, thereby impeding the administration of the estate as directed by the Court. The Plaintiffs allege that the estates' return on the sale of the Property was directly impacted by the Defendants actions, as the section 363 sale ultimately realized $236,000 less than Raj's winning bid. The Plaintiffs' status as the largest secured creditor of the Debtors' estates is significant. The Plaintiffs entered this bankruptcy with a $5.7 million secured claim. While the Plaintiffs did take title to the Property pursuant to their credit bid, they ultimately sold the Property for approximately $2 million less than Raj's original bid at the section 363 auction. Although a less than favorable return on the sale of real estate is not necessarily actionable, a party's interference with a section 363(b) sale in violation of the law is. The Plaintiffs allege that Defendants exercised control over the Property in violation of the Town's procedures when they placarded the Property in between the Sale and closing. The Plaintiffs allege that the depreciated value of the Property was the direct result of the Defendants' interference with the Sale and subsequent failure to remove the placard. In short, the Amended Complaint alleges injury to the largest creditor of the Debtors' estate caused by the Defendants' interference with this Court's Sale Order.

The Plaintiffs' contention that this Court does not possess jurisdiction to oversee allegations of a blatant attack on the sale process and the administration of the estate assets is off the mark. To further suggest that under these facts this Court's jurisdiction lapsed as soon as the Property was no longer property of the estate is absurd. The Defendants advocate a rule which would strip the bankruptcy court of jurisdiction to decide allegations that a defendant sabotaged the section 363(b) sale process. The Court will not simply brush off allegations of interference with the bankruptcy sale process which is fundamental to this Court's core jurisdiction. *See*

Petrie, 304 F.3d at 229; 28 U.S.C. § 157(b)(2)(N) ("Orders approving the sale of property are core bankruptcy proceedings.")[8]

The fact that the Plaintiffs' claims, all pursuant to New York common law and federal non-bankruptcy law, may be brought outside of a bankruptcy action is of no import. "Common-law claims closely connected with the administration of the bankruptcy can qualify as 'arising in' a bankruptcy even though they may, in a literal sense, be brought outside a bankruptcy action." *Lothian Cassidy, LLC v. Lothian Exploration & Dev. II, L.P.*, 487 B.R. 158, 162 (S.D.N.Y. 2013). This Court finds the same is true for the federal non-bankruptcy claims asserted herein. Accordingly, the Court finds that this Litigation is a core proceeding in that it "ar[ose] in" the Debtors' jointly administered bankruptcy cases.

Even if the Litigation was not a "core" proceeding as enumerated in sections 157(b)(2)(A), (N), it is "core" by virtue of its nature. This proceeding is "unique to or uniquely affected by" the bankruptcy proceedings because the factual predicate for the Litigation, alleged malfeasance affecting a section 363(b) sale ordered by the Court, would not exist without the underlying bankruptcy case. *Petrie*, 304 F.3d at 229. Further, the interference with a section 363 sale approved by a Court order "directly affect[s]" both the administration of the estate and an order approving the sale of property, both of which are "core bankruptcy function[s]." *Id.* Where, as here, a lawsuit between two non-debtors, one of which is the largest secured creditor of the

[8] Additionally, the Sale Order imposed obligations upon the Plaintiffs with respect to the Sale which obligations bolster their argument that this Court has subject matter jurisdiction to hear this dispute. The bid procedures associated with the Sale were approved by the Sale Order and required Plaintiff, BFCU to purchase the Property upon Raj's default. Plaintiffs' rights and obligations with respect to the sale were therefore "established as part of the core bankruptcy court function of approving the sale of the [Property]." *Petrie*, 304 F.3d at 229-30.

estate, alleges a scheme to intentionally interfere with the administration of the estate, the lawsuit is a core proceeding.

ii. Related to Jurisdiction

While this Court has "arising in" jurisdiction over this Litigation, it does not have "related to" jurisdiction. In the chapter 7 context, a bankruptcy court has "related to" jurisdiction over a dispute if the "outcome of the proceeding could conceivably have any effect upon the debtor's estate being administered." *Robert Plan Corp.,* 777 F.3d at 597. Some courts have also found "related to" jurisdiction where the parties to a proceeding among non-debtors are sufficiently "intertwined" with the debtor. *Nemsa,* 1995 WL 489711, at *3-5.

The Defendants argue that the Court lacks "related to" jurisdiction because the Plaintiffs seek damages on their own behalf, not on behalf of the estate, and therefore the claims will not have any conceivable effect on the Debtors' estate. Dfs' Mot. 10-11. The Defendants also argue that "jurisdiction does not follow the property, but rather, lapses when the property leaves the debtor's estate." *Id*. 10-11 (*quoting In re Hall's Motor Transit Co.,* 889 F.2d 520, 522 (3d Cir. 1989)). The Defendants further suggest that the Plaintiffs' claims are not based on the Sale Order but are focused on the Property. The Plaintiffs responded that at the commencement of the action, the outcome of this adversary proceeding would "conceivably have an[] effect on the estate[s]" because the subject Property was the Debtors' primary asset. Pls' Opp'n 10-11 (citing *ML Media Partners, LP v. Century/ML Cable Venture (In re Adelphia Commc'ns Corp.),* 285 B.R. 127, 136-37 (Bankr. S.D.N.Y. 2002)).

The Court agrees with the Defendants that the outcome of this Litigation will not have any effect on the estate. The Plaintiffs do not seek damages on behalf of the estate. Damages here are based on the Defendants' alleged devaluing of the Property resulting from the improper

placement of the placard thus causing a substantially diminished repayment on Plaintiffs' secured debt. A recovery from this suit would benefit the Plaintiffs alone and is therefore insufficient to establish "related to" jurisdiction. *Cf. Parmalat Capital Fin. Ltd. v. Bank of Am. Corp.*, 639 F.3d 572, 579 (2d Cir. 2011) ("If either [plaintiff] is successful in their claims against [the defendant], the funds they recover will benefit the respective bankruptcy estates . . . It is not difficult to conclude that the "conceivable effect" test is satisfied. The present actions are therefore "related to" the § 304 proceeding.").

Similarly, the parties are not sufficiently "intertwined" with the Debtors to establish "related to" jurisdiction. It is true that at the time the Defendants removed this Litigation from state court the chapter 7 trustee had commenced an adversary proceeding against the Town and other defendants on behalf of the Debtors' estates. As the Defendants noted, the chapter 7 trustee "assert[ed] nearly identical claims against [the] Defendants to those asserted in" the Litigation, and "most of the factual allegations supporting each of the claims asserted in the [Litigation] relate to acts, occurrences or matters that either took place during the Bankruptcy Case or were addressed by this Court in the Bankruptcy Case." Notice of Removal 3. The chapter 7 trustee's complaint alleged claims of (i) a willful violation of the automatic stay; (ii) tortious interference with contractual relations; (iii) negligence; (iv) deprivation of substantive and procedural due process; and (v) attorneys' fees based on the placarding of the Property and surrounding circumstances. *See* Adversary Complaint, *Barnard v. Town of Huntington, et al.*, No. 16-AP-8025 (Bankr. E.D.N.Y.) (Grossman, Bankr. J.)[9] Although the trustee's claims and the instant Litigation are based on the identical factual circumstances, a factual nexus between a civil proceeding and a bankruptcy case is insufficient to establish "related to" jurisdiction. *Nemsa,*

[9] The trustee's action against the Town has been settled and is now closed.

1995 WL 489711, at *4 (citing *Opti-Gage, Inc.*, 128 B.R. at 196). The test is instead whether the parties are sufficiently intertwined with the Debtors. *Id.* at *5. Here, both parties are non-debtors and neither is "sufficiently intertwined" with the Debtors' to establish "related to" jurisdiction. !

Since the outcome of this Litigation will have no conceivable effect on the Debtors' estate and the parties are not sufficiently intertwined with the Debtors, there is no "related to" jurisdiction over this Litigation.

Conclusion

For the reasons stated above, the Court finds that the Defendants should be estopped from contesting this Court's subject matter jurisdiction over this Litigation in that they affirmatively sought this Court's jurisdiction by removing this matter from state court; they later stipulated to the entry of final orders by this Court in non-core matters, a stipulation which was so-ordered by this Court and which was not timely appealed or reconsidered and which was relied upon by the Plaintiffs in their decision to allow this matter to remain before the bankruptcy court.

The Court further finds that it has subject matter jurisdiction over the Litigation. This matter is "core" as that term is defined in 28 U.S.C. § 157(b) in that it is a "matter concerning the administration of the estate" that "arises in" these bankruptcy cases. An Order consistent with this Decision will be entered forthwith.

Dated: Central Islip, New York
June 11, 2020

Robert E. Grossman
United States Bankruptcy Judge

2020 WL 1867898
Only the Westlaw citation is currently available.
United States Bankruptcy Court, E.D. New York.

IN RE: Deirdre VENTURA, Debtor.

Case No. 8-18-77193-reg
|
Signed April 10, 2020

Synopsis
Background: Individual Chapter 11 debtor, the operator of a bed and breakfast, amended her petition to designate herself as a "small business debtor" and to proceed as such under subchapter V of Chapter 11, newly amended provisions which were added to the Bankruptcy Code pursuant to the Small Business Reorganization Act of 2019 (SBRA). Mortgagee and United States Trustee (UST) filed objections.

Holdings: The Bankruptcy Court, Robert E. Grossman, J., held that:

[1] as matters of first impression, procedural and timing issues did not bar debtor from amending her petition to take advantage of the benefits of the SBRA;

[2] debtor could amend her petition to designate herself as a "small business debtor" notwithstanding prior court orders allowing mortgagee to file its own proposed plan of reorganization, scheduling a confirmation hearing, and approving mortgagee's disclosure statement;

[3] debtor qualified as a "small business debtor," even though the majority of her debt consisted of a mortgage encumbering the property where she both resided and operated a bed and breakfast;

[4] debtor was not judicially estopped from claiming that her mortgage debt arose from commercial or business activities; and

[5] debtor was not barred from utilizing subchapter V solely on the basis that the mortgage she sought to modify was a purchase money mortgage secured by her residence.

Objections overruled.

Procedural Posture(s): Motion to Amend.

West Headnotes (34)

[1] Bankruptcy

Amendments to the Bankruptcy Code pursuant to the Small Business Reorganization Act of 2019 (SBRA), which added subchapter V to Chapter 11 of the Code, were instituted to broaden the opportunity for small businesses to successfully utilize the benefits of Chapter 11. 11 U.S.C.A. § 1181 et seq.

[2] Bankruptcy

Subsection of the Bankruptcy Code generally permitting Chapter 11 debtors to propose a plan that modifies the rights of holders of secured claims specifically excludes modification of claims secured by liens on a debtor's residence. 11 U.S.C.A. § 1123(b)(5).

[3] Bankruptcy

Changes to the Bankruptcy Code set forth in the Small Business Reorganization Act of 2019 (SBRA) were intended to allow small businesses and individuals to take advantage of a Chapter 11 process that would be less costly and time consuming than the current process. 11 U.S.C.A. § 1181 et seq.

[4] Bankruptcy

By enacting the Small Business Reorganization Act of 2019 (SBRA), which added subchapter V to Chapter 11 of the Bankruptcy Code, Congress intended to streamline the reorganization process for small business debtors because small

businesses have often struggled to reorganize under Chapter 11. 11 U.S.C.A. § 1181 et seq.

[5] **Bankruptcy**

Under the Bankruptcy Code, as amended by the Small Business Reorganization Act of 2019 (SBRA), a trustee will be appointed in every case under subchapter V of Chapter 11. 11 U.S.C.A. § 1183.

[6] **Bankruptcy**

Under the Bankruptcy Code, as amended by the Small Business Reorganization Act of 2019 (SBRA), the trustee appointed in every case under subchapter V of Chapter 11 acts as a fiduciary for creditors, in lieu of an appointed creditors committee, and is also charged with facilitating the subchapter V debtor's small business reorganization and monitoring the debtor's consummation of its plan of reorganization. 11 U.S.C.A. §§ 1183(a), 1183(b).

[7] **Bankruptcy**

Prior to enactment of the Small Business Reorganization Act of 2019 (SBRA), which added subchapter V to Chapter 11 of the Bankruptcy Code, small business debtors were required to file a plan of reorganization within 120 days after the order for relief, and "any party in interest" could file a plan at certain times and under certain circumstances; the newly enacted law gives subchapter V debtors the exclusive right to file a plan of reorganization, which generally must be filed within 90 days after entry of the order for relief. 11 U.S.C.A. §§ 1121(b), 1121(c), 1189(a), 1189(b).

[8] **Bankruptcy**

Procedural and timing issues did not bar individual Chapter 11 debtor from amending her petition to take advantage of the benefits of the Small Business Reorganization Act of 2019 (SBRA), which added subchapter V to Chapter 11 of the Bankruptcy Code, even though she had not designated herself as a "small business debtor" on petition, which was filed more than 15 months prior to Act's effective date; SBRA was silent as to its applicability to pending cases, both 90-day plan-filing and 60-day status-conference deadlines had expired but could be extended if the need for extension was attributable for circumstances for which debtor should not be justly held accountable, debtor was not required to comply with the procedural requirements of a law that did not then exist, and there was no statutory prohibition against the court exercising its discretion to reset timelines to allow debtor to avail herself of the newly enacted law. 11 U.S.C.A. §§ 1183, 1188(a), 1189(b); Fed. R. Bankr. P. 1009(a), 1020(a).

[9] **Bankruptcy**

Under the Bankruptcy Code, as amended by the Small Business Reorganization Act of 2019 (SBRA), the bankruptcy court's finding of incorrect designation of a "small business debtor" is triggered by an objection to the designation. 11 U.S.C.A. § 1183 et seq.; Fed. R. Bankr. P. 1020(a).

[10] **Bankruptcy**

Although, under the bankruptcy rules, a voluntary petition, list, schedule, or statement may be amended by a debtor as a matter of course at any time before the case is closed, such amendment by the debtor is not necessarily controlling; the designation by the debtor in the original petition still retains evidentiary effect as it is signed under penalty of perjury. Fed. R. Bankr. P. 1009(a).

[11] **Bankruptcy**

Under the Bankruptcy Code, both the 90-day deadline for a subchapter V debtor to file a Chapter 11 plan and the 60-day deadline to hold a status conference may be extended if the need for an extension is attributable to circumstances for which the debtor should not be justly held accountable. 11 U.S.C.A. §§ 1188(a), 1189(b).

[12] Bankruptcy

Debtor who operated bed and breakfast could amend her petition to designate herself as "small business debtor" under subchapter V of Chapter 11, which was added to Bankruptcy Code by the Small Business Reorganization Act of 2019 (SBRA) while her case was pending, despite prior court orders allowing mortgagee to file its own proposed plan and scheduling a confirmation hearing; though mortgagee argued that Act's retroactive application would prejudice its "vested" rights, there was no statutory bar to such application, amendment of Code's "small business debtor" definition did not impair existing creditor rights and so did not amount to a "taking," applying Act's anti-modification exception to modify the mortgage would not deprive mortgagee of any state-law rights as, due to debtor's discharge in prior case, it could look solely to value of property to satisfy her obligation, and, until plan was confirmed, no property rights could be said to have vested in mortgagee. U.S. Const. Amend. 5; 11 U.S.C.A. §§ 101(51D)(A), 1190(3).

[13] Mortgages and Deeds of Trust

Under New York law, a mortgagee is granted a bundle of rights when it becomes such with respect to a mortgagor's property: the note and mortgage afford in personam rights against the mortgagor, including a right to proceed against her to collect the amount due and owing under the note, as well as in rem rights to proceed against the property and seek a sale of the property, with the sale proceeds applied against the amount due and owing, and, to the extent the sale leaves a deficiency, the right to proceed against the mortgagor for the deficiency.

[14] Bankruptcy

Exception to the Bankruptcy Code's anti-modification provision added to subchapter V of Chapter 11 by the Small Business Reorganization Act of 2019 (SBRA) permits a subchapter V debtor to modify the rights of certain mortgagees by allowing the debtor to bifurcate a claim into a secured and unsecured claim based on the value of the underlying collateral. 11 U.S.C.A. § 1190(3).

[15] Bankruptcy

Although the Bankruptcy Code works to abrogate contractual rights, it does not affect the vested property rights of mortgagees.

[16] Bankruptcy

Bankruptcy Code's definition of "small business debtor," as amended by the Small Business Reorganization Act of 2019 (SBRA), excludes debtors whose primary business is owning "single asset real estate." 11 U.S.C.A. § 101(51D)(A).

[17] Bankruptcy

Debtor qualified as a "small business debtor" under newly amended definition added to the Bankruptcy Code by the Small Business Reorganization Act of 2019 (SBRA), even though the majority of her debt consisted of a mortgage encumbering the property where she both resided and operated a bed and breakfast; debtor's total secured and unsecured debts fell within statutory threshold, and more than 50% of debtor's debts rose from her "commercial or business activities," as, though the subject property, a six-bedroom historic mansion, was clearly debtor's primary residence, the primary

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purpose of purchasing the property appeared to have been to own and operate a bed and breakfast, given goal of debtor, who had long history in hotel business, to combine her business with the needs of her life as a single parent, and there was evidence that town would not have granted debtor a permit to run bed and breakfast unless she lived there. 11 U.S.C.A. § 101(51D)(A).

[18] Bankruptcy

Fact that a debtor incurs mortgage debt to buy a residence does not automatically mean that the debt is "consumer debt," within the meaning of the Bankruptcy Code. 11 U.S.C.A. § 101(8).

[19] Bankruptcy

Under the Bankruptcy Code, test for determining whether debt should be classified as business debt, rather than as "consumer debt," is whether it was incurred with an eye toward profit; courts must look at substance of transaction and borrower's purpose in obtaining loan, rather than merely looking at form of transaction. 11 U.S.C.A. § 101(8).

[20] Estoppel

A debtor may be judicially estopped from changing its legal position when a court has adopted and relied on it and the party claiming judicial estoppel suffers an unfair detriment as a result, unless mistake or inadvertence is an applicable defense.

[21] Estoppel

General test for determining when judicial estopped may be invoked considers whether: (1) a party's later position is clearly inconsistent with its earlier position, (2) the party's former position has been accepted in some way by the court in the earlier proceeding, such that judicial acceptance of an inconsistent position in a later proceeding would create the perception that either the first or the second court was misled, and (3) the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped.

[22] Bankruptcy

Judicial estoppel may be applied in the bankruptcy context when a debtor changes its designation on the petition.

[23] Bankruptcy

Debtor who operated bed and breakfast was not judicially estopped from claiming that mortgage debt arose from commercial or business activities, so as to establish that she qualified as "small business debtor" under subchapter V of Chapter 11, despite contention that she stated in original schedules and in prior bankruptcy filings that she had primarily consumer debt; given hybrid nature of property, it was not clear that debtor's change of description of mortgage debt as business debt was inconsistent with prior description, as she repeatedly referred to property as bed and breakfast in current case, property was integral to business, and debtor was attempting to be clear and forthright in her representations, court took no specific action in either current or prior case based on description of mortgage as consumer debt, and debtor did not take unfair advantage of mortgagee by changing description of debt, but acted to take advantage of new definition, to attempt to save business. 11 U.S.C.A. § 101(51D)(A).

[24] Statutes

Bankruptcy court is charged with interpreting all federal and state statutes according to their plain meaning.

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[25] **Statutes**

In determining the degree of ambiguity or clarity of statutory language, courts cannot examine the language in isolation.

[26] **Statutes**

In construing statutory language, the court must determine the specific context in which the language appears, and the statutory scheme's broader framework in order to preserve the coherence and consistency of the statutory scheme.

[27] **Statutes**

In matters of statutory interpretation, the plain meaning of statutory language may be illuminated by considering not only the particular statutory language at issue, but also the structure of the section in which the key language is found, and the design of the statute as a whole and its object.

[28] **Bankruptcy**

Individual Chapter 11 debtor, the operator of a bed and breakfast at which she resided, was not barred from utilizing subchapter V of Chapter 11 solely on the basis that the mortgage she sought to modify was a purchase money mortgage secured by her residence; debtor's property fell squarely within section of the Bankruptcy Code governing modification of secured creditors' claims by subchapter V debtors, which specifically permits modification of certain claims secured by mortgages on a debtor's principal residence, and primary purpose of the mortgage was not to provide debtor with a place to live, but to benefit debtor's business activities, as she did not purchase a residence and use one room as office space but, rather, used the mortgage proceeds to purchase the historic building that housed her business, renting rooms and spending considerable time and resources on obtaining the proper permits to run the property as a bed and breakfast. 11 U.S.C.A. § 1190(3).

[29] **Bankruptcy**

Unlike the section of the Bankruptcy Code generally permitting Chapter 11 debtors to propose plans that modify the rights of holders of secured claims, which precludes modifications of claims secured by mortgages on the debtor's principal residence, the section of the Code governing debtors who designate themselves as subchapter V debtors specifically permits the modification of claims secured by mortgages on the debtor's principal residence. 11 U.S.C.A. §§ 1123(b)(5), 1190(3).

[30] **Bankruptcy**

Unlike the section of the Bankruptcy Code generally permitting Chapter 11 debtors to propose plans that modify the rights of holders of secured claims, except with respect to claims secured by mortgages on the debtor's principal residence, which takes an all-or-nothing approach to loans securing the debtor's residence, the section of the Code permitting debtors who designate themselves as subchapter V debtors to modify claims secured by mortgages on the debtor's principal residence asks the court to determine whether the primary purpose of the mortgage was to acquire the debtor's residence. 11 U.S.C.A. §§ 1123(b)(5), 1190(3).

[31] **Bankruptcy**

Subparagraphs of the section of the Bankruptcy Code permitting Chapter 11 debtors who designate themselves as subchapter V debtors to modify certain claims secured by mortgages on the debtor's principal residence direct the court to conduct a qualitative analysis to determine whether the principal purpose of the debt was not

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to provide the debtor with a place to live, and whether the mortgage proceeds were primarily for the benefit of the debtor's business activities. 11 U.S.C.A. § 1190(3).

[32] Bankruptcy

Purpose and intent of the Small Business Reorganization Act of 2019 (SBRA), which added subchapter V to Chapter 11 of the Bankruptcy Code, is to assist small business owners in whatever form they take, and to give them speedy access to relief via the bankruptcy process so as to keep them in business and to benefit the employees, suppliers, customers and others who rely on that business. 11 U.S.C.A. § 1181 et seq.

[33] Bankruptcy

Under the section of the Bankruptcy Code permitting Chapter 11 debtors who designate themselves as subchapter V debtors to modify certain claims secured by mortgages on their principal residences so long as the principal purpose of the debt was not to provide the debtor with a place to live, but was primarily for the benefit of the debtor's business activities, some business owners, such as business owners who took out a second mortgage and used the proceeds to buy farm equipment or a taxi medallion, easily fall into that classification. 11 U.S.C.A. § 1190(3).

[34] Bankruptcy

Factors to be considered in determining whether a mortgage is subject to modification under the section of the Bankruptcy Code permitting Chapter 11 debtors who designate themselves as subchapter V debtors to modify certain claims secured by mortgages on their principal residences include: (1) whether the mortgage proceeds were used primarily to further the debtor's business interests, (2) whether the property is an integral part of the debtor's business, (3) the degree to which the specific property is necessary to run the business, (4) whether customers need to enter the property to utilize the business, and (5) whether the business utilizes employees and other businesses in the area to run its operations. 11 U.S.C.A. § 1190(3).

Attorneys and Law Firms

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MEMORANDUM DECISION OVERRULING OBJECTIONS TO THE DEBTOR'S ELECTION AS A SUBCHAPTER V DEBTOR

Robert E. Grossman, United States Bankruptcy Judge

Introduction

***1 [1]** The matter before the Court presents a series of legal issues that are for the most part issues of first impression. The Court is being asked to rule on questions of law resulting from amendments to the Bankruptcy Code pursuant to the Small Business Reorganization Act of 2019 which became effective on February 19, 2020. These amendments, commonly referred to as the SBRA, were instituted to broaden the opportunity for small businesses to successfully utilize the benefits of chapter 11 of the Bankruptcy Code. Congress recognized that many of the benefits afforded to large corporate debtors under chapter 11 were for all practical purposes out of the reach of smaller businesses. Chapter 11 is often an expensive and highly complicated proposition. Many small businesses have neither the money nor the time to navigate the process, even with the considerations given to small businesses prior to the enactment of the SBRA. Had Congress been given a crystal ball with the power to see what the world is facing today, including the severe disruption to our Nation's economy and its impact on small businesses, Congress likely could not have drafted a more effective set of mechanisms to help these businesses reorganize and hopefully survive. These amendments will be analyzed and

challenged over the coming months and years, as are all new significant changes to the law. While this case may be one of the first to require a court to rule on the applicability and interpret complex issues, courts in this country have been called upon since the founding of our Republic to respond to similar challenges.

In the case of Deirdre Ventura (the "Debtor"), these issues arise in the context of objections to the Debtor's recent amendments to her petition to designate herself as a small business debtor and to proceed as a subchapter V debtor. The objections require the Court to answer the following questions:

1) Can the Debtor amend her petition to take advantage of the benefits of the SBRA where the Debtor's case has been pending for over fifteen months and a creditor's proposed plan of reorganization has been scheduled for a hearing on confirmation?

2) Assuming the SBRA applies to the Debtor's case, does the Debtor qualify as a "small business debtor" within the newly amended definition of 11 U.S.C. § 101(51D)(A) where the majority of her debt consists of a mortgage encumbering the property where she both resides and operates a bed and breakfast?

3) Assuming the Debtor fits within the definition of a small business debtor, is the Debtor barred from utilizing provisions applicable to subchapter V debtors to modify the mortgage encumbering the property where she both resides and operates a bed and breakfast?

For the reasons set forth below, the Court answers the first two questions in the affirmative and finds that under its interpretation of 11 U.S.C. § 1190(3), the Debtor is not barred from utilizing this SBRA provision solely on the basis that the mortgage she seeks to modify is a purchase money mortgage secured by her residence. Based on the Court's answers to these questions, the objections to the Debtor's amended petition are overruled.

***2** While these conclusions do not mean that the Debtor will succeed as a subchapter V debtor, the Debtor will be given a chance to proceed under this subchapter. The Debtor must still fulfill her obligations under subchapter V, including proposing a feasible plan and coordinating with the newly appointed subchapter V trustee.

Procedural History and Facts

In 1981, the Debtor began working in the real estate brokerage business specializing in the sales and development of hotels and lodges. Ultimately, she became the sole owner of Innvest Hotel Brokers, LLC which she used to conduct a lodging property brokerage business. (Debtor's Objection to Mot. of Gregory Funding for Order Denying & Voiding Debtor's Election as a Sub-Chapter V Debtor, 1:2, Mar. 24, 2020, ECF No. 97.).

The Debtor, along with another individual, purchased the Harbor Rose Property (the "Property") in December 2007. The acquisition of the Property was financed in part by a $1 million dollar loan ("Note") secured by a mortgage ("Mortgage") on the Property from Wells Fargo Bank, N.A. ("Wells Fargo"). (Emergency Mot. to Prohibit Use of Cash Collateral. & for Relief from Auto. Stay, Exh. A, Nov. 12, 2018, ECF No. 17.). The Note and the Mortgage were eventually assigned in 2015 to Gregory Funding, as servicer for U.S. Bank National Association, as Indentured Trustee on Behalf of and with Respect to Ajax Mortgage Loan Trust 2015-B Mortgage-Backed Notes Series 2015-B ("Gregory"). *Id.* Exh. B. According to the proof of claim filed in this case, Gregory is owed $1,678,664.80. (Claim No. 3-1, Dec. 21, 2018.).

The Property is not a typical Long Island residence. The original structure was built in the mid-1800's and is located in Cold Spring Harbor, a small waterfront village on Long Island's North Shore. (Ventura Aff. ¶ 7.). The Property is registered on The National Registry of Historic Places. *Id.* It is also recognized as a significant historic structure by the Town of Huntington Historic Preservation Society. *Id.* Rooms at the property from the time the Debtor acquired it were made available for rent by the Debtor as advertised on Craigslist, Facebook and Wimdu (a European version of Airbnb). (Ventura Aff. ¶ 5.). The Debtor has included as exhibits to her submission copies of emails from potential guests from 2009 through 2011. (Debtor's Objection to Mot. of Gregory Funding for Order Denying & Voiding Debtor's Election as a Sub-Chapter V Debtor, Exh. A, Mar. 24, 2020,

ECF No. 97.). The documentary evidence supports a finding that paying guests were staying at the Property within the first year that the Debtor purchased the Property. At the time the Debtor purchased the Property, the Huntington Town Code only permitted individuals to rent two guest rooms out of their property. (Ventura Aff. ¶ 11.).

As with many local businesses, the Great Recession of 2008 had a drastic impact on the Debtor's hotel brokerage business. (Debtor's Objection to Mot. of Gregory Funding for Order Denying & Voiding Debtor's Election as a Sub-Chapter V Debtor, 3:3, Mar. 24, 2020, ECF No. 97.). Eventually, the Debtor defaulted on the Mortgage. *Id*. On January 18, 2013, Debtor filed a voluntary petition for relief from her creditors under chapter 7. (Case No. 8-13-70280-reg, ECF No. 1.) ("First Case"). The First Case was filed as a no-asset chapter 7 case, and the majority of the Debtor's debts were listed as consumer debts. *Id*. ECF 11. On May 1, 2013, the Debtor received a discharge and the case was closed shortly therafter. *Id*. ECF No. 16. On May 3, 2013, the Debtor formed Harbor Rose LLC ("Harbor Rose") as a New York State limited liability company. (Ventura Aff. ¶ 3 n.1.).

***3** On February 6, 2014 the Debtor filed a voluntary petition for relief under chapter 13 ("Second Case"). (Case No. 8-14-70473-reg, ECF No. 1.). The Second Case was dismissed for the failure to file necessary documents. *Id*. ECF No. 33. Despite the fact that the Debtor described her debts as primarily consumer debts, the Debtor included in Schedule I a breakdown of income and expenses from the operations of Harbor Rose. *Id*. ECF No. 10. From the information set forth in the Second Case, it is clear that the Debtor's sole source of income was derived from Harbor Rose, which was operating at the Property. Based on the information provided by the Debtor in the Second Case, there does not appear to be an attempt by the Debtor to mislead her creditors or to create a false impression regarding her use of the Property, notwithstanding her description of her debts as primarily consumer debts.

On February 18, 2015, the Debtor executed a loan modification with respect to the Note and Mortgage (the "Loan Modification"). (Emergency Mot. to Prohibit Use of Cash Collateral. & for Relief from Auto. Stay, 8:4, Nov. 12, 2018, ECF No. 17.). As part of the modification the co-owner of the Property transferred his interest to the Debtor. *Id.* Although the Loan Modification gave the Debtor more favorable terms, the Debtor defaulted on her obligations under the Loan Modification. *Id.* 9:4. In February of 2016, Gregory commenced a foreclosure action against the Debtor in the Supreme Court for the State of New York, Suffolk County. *Id.* 10:5.

Despite the Debtor's financial setbacks, the Debtor took steps to increase her ability to rent rooms to guests at the Property. The Debtor obtained a permit to operate as a bed and breakfast on May 4, 2016. (Ventura Aff. ¶ 11.). The Debtor urged one of the Town Councilpersons to sponsor an amendment to allow bed and breakfasts to provide up to four guest rooms and permit a maximum stay of 29 days. (Ventura Aff. ¶ 12.). The Debtor was successful in her endeavors and on November 16, 2017, the Debtor obtained a Certificate of Permitted Use for four guest rooms. (Ventura Aff. ¶ 13.). By June, 2018, the Debtor upgraded the Property to provide four guestrooms. *Id.* The Debtor also obtained the proper permits to add an additional bathroom for guests, replaced the HVAC for a portion of the Property, upgraded the electric service, and built an enclosed porch with heat for year-round use. *Id.*

It appears there is no other such bed and breakfast in the Town of Huntington, and according to the Debtor's affidavit, there is no other similar bed and breakfast on Long Island as of March 24, 2020. (Ventura Aff. ¶ 10.). The Town of Huntington requires as a condition to receiving the bed and breakfast permit that the owner operator reside at the bed and breakfast premises. *Id.* In addition to its lodgings, Harbor Rose offers health and wellness package, including yoga classes, acupuncture treatments, massage treatments. (Emergency Mot. to Prohibit Use of Cash Collateral. & for Relief from Auto. Stay, 19:6, Nov. 12, 2018, ECF No. 17.).

On August 8, 2018, a judgment of foreclosure and sale was granted in favor of Gregory, with a sale date scheduled for October 25, 2018 (the "Foreclosure Sale"). *Id.* at 14-15:5-6. Pursuant to Gregory's Broker's Price Opinion dated October 02, 2018, the Property was valued at $1,200.000.00. *Id.* Exh. H. On October 24, 2018 (the Petition Date"), the Debtor filed a voluntary petition under chapter 11 (the "Current Case"). As of the Petition Date, Gregory was owed a total amount of $1,678,664.80. *Id.* at 17:6. The current value of the Property is unknown.

In the Current Case, the Debtor again described her debts as primarily consumer debts. (Case No. 8-18-77193-reg, ECF

No. 1.). The Debtor also stated that she was an individual chapter 11 debtor and did not designate herself as a small business debtor. *Id.* The Debtor's description of the Property in the Current Case accurately set forth that it was being used as a place of business. For example, when the Debtor was asked "What is the property?" she checked the box "Other" and wrote "B&B Inn" on Schedule A/B instead of checking the box for "Single-family" home. *Id.* In Schedule C, the Debtor claimed an exemption for the Property pursuant to 11 U.S.C. § 522(b)(2) wherein she described it as "Bed & Breakfast." *Id.* Again, on Schedule D, the Debtor described the Property as a "Bed and Breakfast." *Id.* The Debtor also lists her income and expenses from the operations of Harbor Rose in her Statement of Current Monthly Income. *Id*. ECF No. 26.

***4** On November 12, 2018, Gregory moved this Court for an Order: (1) directing the Debtor to establish a Debtor in possession account, directing immediate turnover of cash collateral to the Debtor in possession account, and prohibiting the Debtor's use of cash collateral until the motion and request for adequate protection payments to Gregory could be heard, pursuant to 11 U.S.C. § 363(C)(2)(B); (2) granting Gregory relief from the automatic stay pursuant to 11 U.S.C. § 362(d)(1); or alternatively (3) adequate protection payments pursuant to 11 U.S.C. § 363(e). (Emergency Mot. to Prohibit Use of Cash Collateral. & for Relief from Auto. Stay, at 3, Nov. 12, 2018, ECF No. 17.). In December 2018, the Debtor agreed to pay monthly adequate protection payments to Gregory in the amount of $3,5000, to maintain proper insurance on the Property, and to timely remit taxes due subsequent to January 1, 2019. (Agreed Order Resolving Mot. for Adequate Protection Payments, at 1-2, Dec. 13, 2018, ECF No. 32.).

With the consent of the parties, the Court entered an order directing the Debtor and Gregory to participate in the Loss Mitigation Program with respect to the Property. (Order Directing the Debtor and Creditor Gregory Funding, as servicer for US Bank as Indentured Trustee to Ajax Mortgage Loan to participate in the Loss Mitigation Program, Dec. 20, 2018, ECF No. 35.). In June of 2019, the parties agreed to terminate loss mitigation, to increase the adequate protection payment to Gregory to $4,800 monthly, and to require that by September 30, 2019, the Debtor file a proposed disclosure statement and chapter 11 plan of reorganization acceptable to Gregory in its sole and absolute discretion. (Further Agreed Order Concerning Adequate Protection Payments, *Inter Alia*, June. 11, 2019, ECF No. 53.). In the event the Debtor's proposed disclosure statement and plan were deemed unsatisfactory to Gregory, Gregory would be permitted to file a competing plan which would provide for the sale of the Property to satisfy the Mortgage. *Id.* The Debtor failed to file a proposed disclosure statement and plan by the September 30, 2019 deadline, which effectively terminated the Debtor's exclusivity as an individual chapter 11 debtor.

At the November 19, 2019 status conference, the Court directed the Debtor and Gregory to each file a proposed plan of reorganization and disclosure statement by December 13, 2019. As expected, Gregory's proposed plan provided for an auction sale of the Property subject to higher and better offers. (Chapter 11 Plan of Liquidation, Dec. 13, 2019, ECF No. 60.). Gregory's proposed plan also provided for a carve out from the sale proceeds to pay all the other classes in full. *Id.* The Debtor's proposed plan sought to modify the Mortgage by reducing the secured portion of Gregory's claim to $1,050,00, which the Debtor represented was the value of the Property at that time, and repaying the secured portion of the claim over 30 years at 4.25 percent interest per annum. (Debtor's First Amended Plan of Reorganization, Dec. 20, 2019, ECF No. 67.). According to the Debtor's proposed plan, Gregory would receive no payment on account of the unsecured portion of its claim because the Debtor had previously received a discharge in the First Case. *Id.*

[2] The viability of the Debtor's plan hinged on her ability to utilize 11 U.S.C. § 1123(b)(5) to bifurcate the Mortgage into a secured and unsecured claim, and to pay only the secured portion in full. However, because the Debtor resided at the Property, and 11 U.S.C. § 1123(b)(5) specifically excluded modification of claims secured by liens on a debtor's residence, the Court determined that the Debtor's proposed plan was unconfirmable on its face. So long as any portion of the Property constituted the Debtor's residence, 11 U.S.C. § 1123(b)(5) could not be used to modify the Mortgage. This conclusion was consistent with *In re Macaluso*, 254 B.R. 799 (Bankr. W.D.N.Y. 2000), *In re Addams*, 564 B.R. 458 (Bankr. E.D.N.Y. 2017) and *In re Wages*, 508 B.R. 161 (9th Cir. BAP 2014). For these reasons, on January 13, 2020, the Court did not approve the Debtor's disclosure statement. (Order Approving Disclosure Statement Relating to Chapter 11 Plan of Gregory Funding as Plan Sponsor, *Inter Alia*, Jan. 13, 2020, ECF No. 79.). At the same hearing, the Court approved

Gregory's Disclosure Statement and authorized Gregory to solicit votes. *Id.* The Court also set February 26, 2020 as the date for a hearing on the confirmation of Gregory's proposed plan (the "Confirmation Hearing"). *Id.*

***5** **[3]** In preparation for the Confirmation Hearing, Gregory solicited the necessary votes and filed the certification of ballots on February 20, 2020. (Certificate as to Balloting Accepting and Rejecting the Chapter 11 Plan, Feb. 20, 2020, ECF No. 81.). One day prior to the date the certification of ballots was filed, and seven days prior to the Confirmation Hearing, the SBRA became effective. Pub. L. No. 116-54 § 5, 133 Stat. 1079, 1087. Congress made clear that the changes to the Code set forth in the SBRA were intended to allow small businesses and individuals to take advantage of a chapter 11 process that would be less costly and time consuming than the current process. H.R. REP. No. 116-171, at 2 (2019).

At the Confirmation Hearing, the Court advised the parties of the SBRA and offered the Debtor the opportunity to proceed with the hearing as scheduled or the Court would adjourn the hearing for a short time to allow the Debtor to determine whether she wished to amend her petition. The Debtor opted to have the Confirmation Hearing adjourned. On March 3, 2020, the Debtor filed a letter with the Court advising that she intended to amend her petition. (Letter to Court regarding Debtor's Intention to Amend Her Petition, Mar. 3, 2020, ECF No. 85.).

On March 6, 2020, the Debtor amended her petition to designate herself as a small business debtor under the newly amended definition, and to elect to proceed as a subchapter V debtor. (Aff. Pursuant to E.D.N.Y. LBR 1009-1(a), Mar. 6, 2020, ECF No. 87.). On March 6, 2020, the United States Trustee (the "U.S. Trustee") appointed Salvatore LaMonica, Esq., as the subchapter V trustee (the "Trustee") pursuant to 11 U.S.C. § 1183(a). (Notice of Appointment of Subchapter V Trustee, Mar. 6, 2020, ECF No. 88.). On March 10, 2020, the Court entered a scheduling order setting a status conference for April 1, 2020 and setting the Debtor's deadline to file a plan for June 8, 2020. (Order Scheduling Status Conference Under 11 U.S.C. § 1188, Mar. 9, 2020, ECF No. 91.).

On March 9, 2020, Gregory filed a motion objecting to the Debtor's designation as a subchapter V debtor (the "Motion"), raising a wide range of objections to the Debtor's designation, including objections based on prejudice to Gregory's vested rights in this case, as the Court was at the point of holding a hearing to confirm Gregory's proposed plan. (Mot. to Object to Debtor's Designation as a Sub-Chapter V, 16:6, Mar. 10, 2020, ECF No. 92.). [1] In addition, Gregory asserts that the Debtor is not eligible for subchapter V relief because she does not fit within the definition of "small business debtor" as set forth in newly amended 11 U.S.C. § 101(51D)(A). *Id.* 18-19:7-8. Even if she fits within the definition, Gregory asserts that the Debtor should be judicially estopped from amending her designation based on her prior representations to Gregory as well as her prior statements in the prior bankruptcy filings and the Current Case. (Reply in Connection with Objection to Debtor's Designation as a Sub-Chapter V Debtor, 8:4, Mar. 26, 2020, ECF No. 99.). Gregory also argues that the Debtor cannot modify the Mortgage pursuant to pursuant 11 U.S.C. § 1190(3) because the Debtor used the Mortgage proceeds to purchase a residence, not to invest in Harbor Rose. (Mot. to Object to Debtor's Designation as a Sub-Chapter V, 32:13, Mar. 10, 2020, ECF No. 92.).

On March 19, 2020 the U.S. Trustee filed an Objection ("U.S. Trustee Objection") to the Debtor's election to be treated as a subchapter V case, raising timing and technical issues. (United States Trustee's Objection to Debtor's Election to Be Treated as a Subchapter V Case, Mar. 19, 2020, ECF No. 96.). On March 24, 2020, the Debtor filed her opposition to the Motion (Debtor's Objection to Mot. of Gregory Funding for Order Denying & Voiding Debtor's Election as a Sub-Chapter V Debtor, Mar. 24, 2020, ECF No. 97.), and Response to the U.S. Trustee Objection. (Resp. to United States Trustee's Objection to Debtor's Election to Be Treated as a Subchapter V Case, Mar. 24, 2020, ECF No. 98.). In her submissions, the Debtor pointed to her professional experience in the hotel business, the unique characteristics of the Property, her consistent use of the Property as a bed and breakfast, and the improvements the Debtor made to the Property as sufficient grounds for finding that the Debtor is a small business debtor within the definition of § 101(51D)(A), and that she qualified to proceed as a subchapter V debtor.

***6** On March 30, 2020, the Debtor filed a letter indicating that since the Debtor filed her amended petition to make a retroactive election under subchapter V, the Debtor has been unable to have any meaningful negotiations with Gregory.

(Letter Pursuant to 11 U.S.C. § 1188(c) Outlining Efforts by the Debtor to Attain Consensual Plan of Reorganization, Mar. 30, 2020, ECF No. 101.). The Debtor further notes that the Trustee has attempted to persuade Gregory to negotiate with the Debtor, to no avail. *Id*. On April 1, 2020, the Court held a telephonic hearing on the Motion and the U.S. Trustee's Objection, which was attended by the Debtor's counsel, Gregory's counsel, the U.S. Trustee and the subchapter V Trustee. Thereafter, the matter was marked submitted.

Discussion

[4] On August 23, 2019, the President signed the SBRA into law, which became effective on February 19, 2020. Pub. L. No. 116-54 § 5, 133 Stat. 1079, 1087. The SBRA is codified in 11 U.S.C. §§ 1181-1195, and certain Bankruptcy Code sections that existed prior to the SBRA have been modified as well. *Id.* By enacting this law, Congress intended to streamline the reorganization process for small business debtors because small businesses have often struggled to reorganize under chapter 11. H.R. REP. No. 116-171, at 1-2 (2019).

Of pertinence, the Report from the House Committee on the Judiciary contains, *inter alia*, the following statement:

> Small businesses--typically family-owned businesses, startups, and other entrepreneurial ventures— "form the backbone of the American economy." By their very nature, however, the longevity of these businesses is limited. According to the Small Business Administration Office of Advocacy, approximately 20 percent of small businesses survive the first year, but by the five-year mark only 50 percent are still in business and by the ten-year mark only one-third survive. Notwithstanding the 2005 Amendments, small business chapter 11 cases continue to encounter difficulty in successfully reorganizing...the legislation allows these debtors "to file bankruptcy in a timely, cost-effective manner, and hopefully allows them to remain in business" which "not only benefits the owners, but employees, suppliers, customers, and others who rely on that business."

Id. at 2. (Citing the Unofficial Transcript of Oversight of Bankruptcy Law and Legislative Proposals: Hearing Before the Subcomm. on Antitrust, Commercial, & Admin. Law of the H. Comm. on the Judiciary, 116th Cong. 27 (2019) (on file with H. Comm. on the Judiciary staff)).

Newly amended 11 U.S.C. § 101(51D)(A) of the Bankruptcy Code defines a "small business debtor", in part, as "...a person engaged in commercial or business activities ... that has aggregate noncontingent liquidated secured and unsecured debts as of the date of the filing of the petition ... in an amount not more than $2,725,625... not less than 50 percent of which arose from the commercial or business activities of the debtor. " 11 U.S.C. § 101(51D)(A).[2] The definition of "small business" excludes debtors whose primary business is owning "single asset real estate." *Id.*

Prior to enactment of the SBRA, the only statutory provision the Debtor could have considered to modify the Mortgage was 11 U.S.C. § 1123(b)(5). This section permits chapter 11 debtors to propose a plan that modifies the rights of holders of secured claims "...other than a claim secured only by a security interest in real property that is the debtor's principal residence." 11 U.S.C. § 1123(b)(5).[3]

***7** The SBRA has given small business debtors who designate themselves as subchapter V debtors another tool to be used when proposing a plan. Section 1190(3) provides as follows:

> A plan filed under this subchapter—
>
> (3) notwithstanding section 1123(b)(5) of this title, may modify the rights of the holder of a claim secured only by a security interest in real property that is the principal residence of the debtor if the new value received in connection with the granting of the security interest was—
>
> > (A) not used primarily to acquire the real property; and
> >
> > (B) used primarily in connection with the small business of the debtor.

11 U.S.C. § 1190(3).

[5] **[6]** Furthermore, a trustee will be appointed in every subchapter V case. The subchapter V trustee will act as a fiduciary for creditors, in lieu of an appointed creditors' committee. The subchapter V trustee is also charged with facilitating the subchapter V debtor's small business reorganization and monitoring the subchapter V debtor's

consummation of its plan of reorganization. 11 U.S.C § 1183 (a), (b).

[7] Prior to enactment of the SBRA, small business debtors were required to file a plan of reorganization within 120 days after the order for relief, and "any party in interest" could file a plan at certain times and under certain circumstances. 11 U.S.C. §§ 1121(b), (c). The newly enacted law gives subchapter V debtors the exclusive right to file a plan of reorganization, which must be filed within 90 days after entry of the order for relief. 11 U.S.C. § 1189(a), (b). This plan deadline may be extended by the Court "...if the need for the extension is attributable to circumstances for which the debtor should not justly be held accountable." 11 U.S.C. § 1189(b).

1. Does the SBRA apply to the Debtor's case?

a. Procedural and timing issues

[8] The SBRA is silent as to whether it applies to pending cases, or only to cases commenced after the effective date. In the Current Case, the Debtor did not designate herself as a small business debtor on her petition, which was filed over fifteen months prior to the effective date of the SBRA. The Debtor has since amended the petition to reflect 1) that she is a small business debtor and 2) that she seeks to proceed as a subchapter V debtor. The sole reason for filing the amended petition is to take advantage of the changes to the Bankruptcy Code and Rules pursuant to the SBRA. While the U.S. Trustee does not specifically urge the Court to find that the SBRA should only apply to cases filed after February 19, 2020, the U.S. Trustee does argue that procedural issues prevent the Debtor from electing to proceed as a subchapter V small business debtor. In the Motion, Gregory raises a wide range of objections to the Debtor's designation, including due process objections based on prejudice to Gregory's vested rights in this case, estoppel arguments, and objections based on whether the Mortgage is subject to modification under § 1190(3).

[9] According to Fed. R. Bankr. P. 1020(a), once a small business debtor designates itself in the petition, "...the status of the case as a small business case shall be in accordance with the debtor's statement under this subdivision, unless and until the court enters an order finding that the debtor's statement is incorrect." Fed. R. Bank. P. 1020(a). The Court's finding of incorrect designation is triggered by an objection to the designation. *See In re Angel Fire Water Co., LLC*, No. 13–10868 ta11, 2015 WL 251570, at *6 (Bankr. D. N.M. Jan. 20, 2015) (finding that because the debtor never elected to be a small business debtor and no party objected to its status, it would be inappropriate for the court to alter the debtor's statement *sua sponte*).

***8** **[10]** Pursuant to Fed. R. Bankr. P. 1009(a), "[a] voluntary petition, list, schedule or statement may be amended by a debtor as a matter of course at any time before the case is closed." However, such amendment by the debtor is not necessarily controlling. The designation by the debtor in the original petition still retains evidentiary effect as it is signed under penalty of perjury. *In re Roots Rents, Inc.,* 420 B.R. 28, 39-40 (Bankr. D. Idaho. 2009).

As the U.S. Trustee points out, the SBRA imposes several requirements in subchapter V cases. First, a "SBRA trustee" is appointed by the U.S. Trustee, who is charged with development of a consensual plan. 11 U.S.C. § 1183(b)(7). Within 60 days of entry of the order for relief, the Court must hold a status conference with the SBRA trustee. 11 U.S.C. § 1188(a). Subsection (b) provides that the court may extend the 60-day deadline if "...the need for an extension is attributable to circumstances for which the debtor should not justly be held accountable." 11 U.S.C. § 1188(a). Pursuant to 11 U.S.C. § 1189(b), the subchapter V debtor shall file a plan within 90 days of entry of the order for relief, "...except that the court may extend the period if the need for the extension is attributable to circumstances for which the debtor should not be justly held accountable." 11 U.S.C. § 1189(b). In addition, the subchapter V debtor must submit a status report 14 days prior to the status conference detailing efforts to reach a consensual plan. 11 U.S.C. § 1188(c).

[11] According to the U.S. Trustee, there is no bar to applying the SBRA retroactively to cases commenced prior to February 19, 2020. However, because the order for relief in the Debtor's case was entered on October 24, 2018, the Debtor's 90-day deadline to file a plan has expired, and it does not appear that the SBRA trustee can effectively function as the facilitator of a consensual plan. Furthermore, many status hearings have already taken place in this case without the participation of a subchapter V trustee. First, the Court notes that both the 90 day deadline to file a plan and the 60 day deadline to

hold a status conference may be extended if the need for an extension is attributable to circumstances for which the debtor should not be justly held accountable. Given that the Debtor's case was filed over fifteen months ago, the Court finds that to argue the Debtor should have complied with the procedural requirements of a law that did not exist is the height of absurdity. The Debtor is not required to comply with deadlines that clearly expired before the Debtor could have elected to proceed as a subchapter V debtor.

In one of the very few written decisions regarding the SBRA, the Bankruptcy Court found that any practicality and scheduling issues arising from an SBRA designation in a case commenced prior to the effective date of the SBRA, while they might result in redundant hearings or the "procedurally awkward" process of resetting deadlines, did not pose an absolute bar to retroactive application of the SBRA. *See In re Progressive Solutions, Inc.*, No. 8:18-bk-14277-SC, 2020 WL 975464, at *4 (Bankr. C.D. Cal. February 21, 2020) (The United States Trustee raised objections on several grounds related to practicality and scheduling issues which the court overruled. The court ultimately permitted the resetting or rescheduling of these procedural matters "...in order to provide due process to all parties involved, unless vested rights of parties would be abridged or otherwise prejudiced.").

***9** Armed with this case law and since there is no prohibition provided by Congress, the Court finds that it is within the Court's discretion to reset the timelines to allow the Debtor to avail herself of the newly enacted law that was not at her disposal when she filed the Current Case. Therefore, the Court overrules any objections raised by the U.S. Trustee or Gregory based on procedural or timing issues imposed by the SBRA.

b. Gregory's substantive rights

[12] Gregory also argues that retroactive application of the SBRA to the Debtor's case is impermissible because it would be predjudicial to Gregory with respect to its "vested rights." Gregory interprets vested rights to mean prior orders issued by this Court permitting Gregory to file its own plan and approving Gregory's disclosure statement, along with the Court's finding that the Debtor's proposed disclosure statement was patently unconfirmable. However, an analysis of Gregory's argument and applicable case law leads the Court to a different conclusion.

Both Gregory and the U.S. Trustee acknowledge that there is no statutory prohibition to applying the SBRA to cases that were pending prior to the effective date of this legislation. The few cases that discuss this issue agree that while there is a presumption against retroactivity, this presumption applies to " 'new provisions affecting contractual or property rights, matters in which predictability and stability are of prime importance.' " *In re Moore Props. of Person Cty., LLC*, No. 20-80081, 2020 WL 995544, at *3 (Bankr. M.D.N.C. February 28, 2020) (citing *Landgraf v. USI Film Products*, 511 U.S. 244, 271, 114 S.Ct. 1483, 128 L.Ed.2d 229 (1994) (other citations omitted)). As Judge Kahn noted, and this Court agrees, subchapter V incorporates many of the provisions already applicable to small business debtors. *In re Moore Props. of Person Cty., LLC*, 2020 WL 995544, at *4, n.10. At least one other court considering this issue has drawn the same conclusion. *In re Body Transit, Inc. d/b/a Rascals Fitness*, 613 B.R. 400, ——, 2020 WL 1486784, at *6 (Bankr. E.D. Pa. 2020) (holding that "...in general, the new subchapter V provisions do not impair the vested property interests of creditors and, therefore, the concerns supporting application of the canon of statutory construction disfavoring the retroactive application of new law are absent."). In addition, the amendment of the definition of "small business debtor" in 11 U.S.C. § 101(51D)(A) of the Bankruptcy Code did not appear to affect the contractual or vested property rights of parties that existed prior to the effective date of the SBRA. *In re Moore Props. of Person Cty., LLC*, 2020 WL 995544, at *4, n.10.

In discussing the applicability of the SBRA to a pending bankruptcy case, Judge Kahn in *In re Moore Props. of Person Cty., LLC* relied on guidance from the Supreme Court, which considered the issue of retroactivity in the context of a newly enacted bankruptcy statute. *Id.* at *3. (citing *United States v. Sec. Indus. Bank*, 459 U.S. 70, 103 S.Ct. 407, 74 L.Ed.2d 235 (1982)). The Court in *Sec. Indus. Bank* was called on to determine whether § 522(f) of the 1978 Bankruptcy Act, which provided debtors with a vehicle to remove certain liens that attached to property of the debtor's estate prepetition, violated the Fifth Amendment. *United States v. Sec. Indus. Bank*, 459 U.S. 70, 103 S.Ct. 407, 74 L.Ed.2d 235 (1982). Instead of dealing with this Constitutional clash head-on, the Supreme Court held that this provision was not intended to

apply to property interests created before the enactment of the 1978 Bankruptcy Act. *Id.* The Court acknowledged that the Congressional authority to enact legislation "...has been regularly construed to authorize the retrospective impairment of contractual obligations." *Id.* at 74, 103 S.Ct. 407. (citing *Hanover National Bank v. Moyses*, 186 U.S. 181, 188, 22 S.Ct. 857, 46 L.Ed. 1113 (1902)). However, the Supreme Court distinguished between using that authority to modify existing contractual obligations and using it to "defeat traditional property interests." *Id.* at 75, 103 S.Ct. 407. The Court in *Landgraf v. USI Film Products* further taught that "[t]he presumption against statutory retroactivity is founded upon elementary considerations of fairness dictating that individuals should have an opportunity to know what the law is and to conform their conduct accordingly," and the principle that "settled expectations should not be lightly disrupted." *Landgraf v. USI Film Products*, 511 U.S. 244, 245, 265, 114 S.Ct. 1483, 128 L.Ed.2d 229 (1994). After analyzing the Supreme Court's rulings, Judge Kahn concluded that in the case before him, there were no taking or retroactivity concerns which were the focus of the Supreme Court in *Landgraf* and *Security Indus. Bank*. *In re Moore Props. of Person Cty., LLC*, 2020 WL 995544, at *4.

***10** Judge Kahn did single out 11 U.S.C. § 1190(3) as a potential area of concern if it were to be retroactively applied to affect a property right existing prior to the enactment of the SBRA, but he did not make a ruling as to whether this provision violated the Fifth Amendment prohibition against taking property without compensation. *Id.* at *4, n.14.

While Gregory speaks in terms of damage to its vested rights resulting from the progress made in the Debtor's bankruptcy case, Gregory is focused on the wrong question. The correct question to ask is whether designation of the Debtor as a subchapter V debtor will impair Gregory's rights as they existed prior to the effective date of the SBRA. Clearly, the amendment to the definition of "small business debtor" does not amount to a taking of property. The SBRA merely amends the definition of small business debtor to ensure that certain debtors can avail themselves of a less costly and time-consuming path to reorganization that befits the family – owned businesses and other "Main Street" businesses that are currently in such dire need of relief. *See In re Moore Props. of Person Cty., LLC*, 2020 WL 995544, at *5 n.10 (Bankr. M.D.N.C. February 28, 2020) ("...the SBRA [amends] the definition of 'small business debtor' under chapter 1, but that revision does not affect contractual or vested property rights any more than the general availability of subchapter V.").

[13] The more difficult question is whether 11 U.S.C. § 1190(3) should apply to property rights which vested prior to the effective date of the SBRA, such as Gregory's rights as mortgagee. In order to answer this question, the nature of Gregory's rights must be defined. At the time Gregory became the mortgagee with respect to the Property, Gregory was granted a bundle of rights under New York State law. *Butner v. U.S.*, 440 U.S. 48, 55, 99 S.Ct. 914, 59 L.Ed.2d 136 (1979). The Note and Mortgage afforded *in personam* rights against the Debtor including a right to proceed against the Debtor to collect the amount due and owing under the Note. In addition, Gregory was granted *in rem* rights to proceed against the Property and seek a sale of the Property. The proceeds of the sale would then be applied against the amount due and owing. The right to sell the Property would generate only an amount of money that reflects the value of the Property as established at a free and fair auction sale. To the extent the sale left a deficiency, Gregory would have been entitled to proceed against the Debtor for the deficiency. However, because the Debtor previously received a discharge of her personal obligations, Gregory is left with only its rights against the Property under New York State law. In this unique case, Gregory can no longer seek entry of a judgment against the Debtor personally because of the discharge entered in the First Case. It should also be noted that Gregory may still avail itself of all rights granted to a secured creditor under the Code that have not been amended by the SBRA.

[14] **[15]** The exception to the anti-modification provision permits a debtor to modify the rights of certain mortgagees by allowing the debtor to bifurcate a claim into a secured and unsecured claim based on the value of the underlying collateral. 11 U.S.C. § 1190(3). Since Gregory can look solely to the value of the Property to satisfy the Debtors obligation as a result of the discharge the Debtor received in the First Case, application of 11 U.S.C. § 1190(3) will not deprive Gregory of any rights Gregory retained under state law. Even if the Note had not been discharged in the First Case, the Court is not convinced that 11 U.S.C. § 1190(3) would raise sufficient Constitutional doubts to warrant only prospective application. The Bankruptcy Code works to abrogate contractual rights, but does not affect the vested property rights of mortgagees. As the Supreme Court stated in *Security Indus. Bank*, "our cases recognize, as did the common law, that the contractual

right of a secured creditor to obtain repayment of his debt may be quite different in legal contemplation from the property right of the same creditor in the collateral. Compare *Hanover National Bank v. Moyses*, *supra*, with *Lousisville Joint Stock Land Bank v. Radford*, [295 U.S. 555, 55 S.Ct. 854, 79 L.Ed.2d 1593 (1935)] *supra*, and *Kaiser Aetna v. United States*, 444 U.S. 164, 100 S. Ct. 383, 62 L. Ed.2d 332 (1979)." 459 U.S. 70, 75, 103 S.Ct. 407. Consequently, applying § 1190(3) to the modify the Mortgage would not violate Gregory's Fifth Amendment rights.

***11** This still leaves the Court to consider whether applying the SBRA to the Debtor's case is predjudicial based on the history of this case, including the fact that the Court had previously rejected the Debtor's proposed plan and was poised to rule on whether to confirm Gregory's proposed plan. To this Court, this question does not raise Constitutional issues, nor does it require the Court to treat the rulings in the Debtor's case as "vested" rights. Until a plan is confirmed no property rights can be said to have vested in either the Debtor or Gregory. What Gregory is alluding to is whether by permitting the Debtor to elect treatment as a subchapter V debtor would cause prejudice to Gregory. As Judge Clarkson stated in *Progressive Solutions*, he would consider whether "...other events occurring during the pendency of the present case ... would be disturbed by the designation of the case as a Subchapter V case." *In re Progressive Solutions, Inc.*, 2020 WL 975464, at *4. Similarly, in *In re Body Transit, Inc. d/b/a Rascals Fitness*, Judge Frank took into consideration whether permitting the debtor to elect treatment as a subchapter V debtor would unduly prejudice the objecting party. *In re Body Transit, Inc. d/b/a Rascals Fitness*, —— B.R. at ——, 2020 WL 1486784, at *7. Given that subchapter V was not available to the Debtor on the Petition Date and the Debtor has made very clear from the outset the nature of Property as a business, the Court will not penalize the Debtor because after careful analysis by Congress the law has been amended to address the needs of debtors that engage in the type of business she operates. These types of debtors who are willing to risk everything to start and maintain their own businesses should not be penalized, rather, they should be applauded. Gregory will retain many of the rights it had at the inception of the case, any delay caused by this ruling is not sufficiently prejudicial to Gregory, given the current economic conditions. For these reasons, the Court finds that the SBRA applies to the Debtor's case in its totality.

2. Does the Debtor fit within the definition of a "small business debtor"?

[16] As previously stated, the SBRA amended the definition of "small business debtor", in part, to provide that it is "a person engaged in commercial or business activities ... that has aggregate noncontingent liquidated secured and unsecured debts as of the date of the filing of the petition ... in an amount not more than $2,725,625... not less than 50 percent of which arose from the commercial or business activities of the debtor. " 11 U.S.C. § 101(51D)(A). The definition of "small business debtor" excludes debtors whose primary business is owning "single asset real estate." *Id.*

[17] The Debtor listed on Schedule D filed on the Petition Date the Mortgage in the amount of $1,5000.000.00. This debt combined with the other secured and unsecured debts totals $1,562.182.00 which is within the threshold statutory threshold of § 101(51D). What remains to be determined is whether more than 50% of the Debtor's debts rose from her commercial or business activities, which was not part of the calculation when determining whether a debtor was a small business debtor prior to the effective date of the SBRA.

Since there is no statutory definition of what constitutes "commercial or business activities," Gregory looks to the definition of "consumer debt" to assist in determining what types of debt fit within this new description. A consumer debt is a debt "...incurred by an individual primarily for a personal, family, or household purpose." 11 U.S.C. § 101(8). "Debt" means "liability on a claim," 11 U.S.C. § 101(11) (1982), and "claim," in turn, is broadly defined as any "right to payment, whether or not such right is ... secured, or unsecured." 11 U.S.C. § 101(4)(A).

Gregory correctly points out that this Court has previously held that a residential mortgage fell within the definition of "consumer debt." *In re Lemma*, 393 B.R. 299 (Bankr. E.D.N.Y. 2008). For the parties' understanding, there was no allegation in the *Lemma* case that the debtors used their residence for anything other than their personal residence. Other courts have drawn the same conclusion. *In re Kelly*, 841 F.2d 908, 912 (9th Cir. 1988) (recognizing that "[t]he statutory scheme so clearly contemplates that consumer debt include debt secured by real property that there is no room left for any

other conclusion."); and *In re Hall*, 258 B.R. 45, 50 (Bankr. M.D. Fla. 2001) (a purchase money mortgage on a residence is a consumer debt). The same could be true of HELOCs, depending upon the use of the mortgage proceeds. *See In re Naut*, No. 07-20280 (REF), 2008 WL 191297, at *6 (E.D. Pa. Jan. 22, 2008) (holding that the debt was consumer debt because virtually all the proceeds from the refinancing and second mortgage debts were used to purchase and improve the property, not for any business purpose.); *Cox v. Fokkena* (*In re Cox*), 315 B.R. 850, 8-9 (8th Cir. BAP 2004) (despite the debtor's contention that they bought their home for investment purposes, the record revealed that the debt fit squarely within the definition of a consumer debt because the proceeds were used to complete the construction of and furnish the family's home.).

***12** **[18]** **[19]** However, the fact that a debtor incurs mortgage debt to buy a residence does not automatically mean that the debt is consumer debt. "The test for determining whether a debt should be classified as a business debt, rather than as a consumer debt, is whether it was incurred with an eye toward profit...[c]ourts must look at the substance of the transaction and the borrower's purpose in obtaining the loan, rather than merely looking at the form of the transaction." *In re Martin*, No. 12-38024, 2013 WL 5423954, at *6 (S.D. Tex. Sept. 26, 2013). *See also In re Booth*, 858 F.2d 1051, 1055 (5th Cir. 1988) (a debt incurred with an eye toward profit is a business debt, rather than consumer debt.).

Gregory asserts that the form of the transaction was solely a residential loan for the purposes of purchasing a primary residence, not operating a business. Gregory points to the Mortgage whereby the Debtor declared, "I will occupy the Property and use the Property as my principal residence within 60 days after I sign this Security Instrument." (Emergency Mot. to Prohibit Use of Cash Collateral. & for Relief from Auto. Stay, Exh. A, 8:6, Nov. 12, 2018, ECF No. 17.). Gregory also directs the Court's attention to the fact that Harbor Rose was not formed until six years after the Mortgage was originally granted, and any subsequent change in the Debtor's use of the Property does not change the nature of the debt. Gregory asserts that none of the Debtor's debts, let alone 50% of the debts, are derived from the operation of Harbor Rose and none of the Mortgage proceeds were used to renovate the Property for the benefit of the business. Finally, Gregory emphasizes the Debtor's previous characterization of the Mortgage debt as consumer debt in her prior bankruptcy filings and the Current Case as grounds for finding that the Debtor is not a small business debtor within the definition of 11 U.S.C. § 101(51D)(A).

In response, the Debtor points to her long history in the hotel business, her stated need to create a business that would keep her close to her adopted daughter, and the very unique characteristics of the Property to support a finding that the Mortgage debt was indeed incurred for commercial purposes. The Debtor purchased a six-bedroom historic mansion with the intention of converting this large house into a guest house. From the outset, the Debtor asserts she rented the guest rooms by advertising on various websites. The Debtor also invested in the Property by installing a new septic system to accommodate her business. Six year after purchasing the Property, she decided to register the Property as the first legal bed and breakfast in the Town of Huntington.

While the Property is clearly the Debtor's primary residence, the primary purpose of purchasing the Property appears to have been to own and operate a bed and breakfast. The Debtor's goal was to combine her business with the needs of her life as a single parent. The fact that the Debtor resides at the Property does not control whether the Mortgage is in the nature of a debt which arose from the commercial or business activities of the Debtor. In fact, the Debtor's affidavit in support of her opposition to the Motion indicates that the Town of Huntington will not grant a permit to run a bed and breakfast if the owner/ operator does not live inside the facility itself.

Case law supports this finding. *See In re Martin*, No. 12-38024, 2013 WL 5423954, at *6 (Bankr. S.D. Tex. Sept. 26, 2013) ("[c]ourts must look at the substance of the transaction and the borrower's purpose in obtaining the loan, rather than merely looking at the form of the transaction..."). Based on the case law and the relevant facts, the Court finds that the Debtor fits within the definition of a small business debtor under the SBRA.

3. Does judicial estoppel apply to preclude the Debtor from claiming that the Mortgage debt arose from commercial or business activities?

***13** As an alternative argument, Gregory asserts that the Debtor is judicially estopped from asserting that the Mortgage debt arose from her commercial or business activities. Gregory points out that the Debtor's current position that her debts are not primarily consumer debts is clearly inconsistent with her earlier position that those same debts are primarily consumer debts in her prior bankruptcy filings and in the original schedules filed in the current case.

[20] A debtor may be judicially estopped from changing its legal position when a court has adopted and relied on it and the party claiming judicial estoppel suffers an unfair detriment as a result, unless mistake or inadvertence is an applicable defense. *See New Hampshire v. Maine*, 532 U.S. 742, 742-743, 121 S.Ct. 1808, 149 L.Ed.2d 968 (2001) (" '[W]here a party assumes a certain position in a legal proceeding, and succeeds in maintaining that position, he may not thereafter, simply because his interests have changed, assume a contrary position, especially if it be to the prejudice of the party who has acquiesced in the position formerly taken by him.' ") (citing *Davis v. Wakelee*, 156 U.S. 680, 689, 15 S.Ct. 555, 39 L.Ed. 578 (1895)). *See also Ahrens v. Perot Sys. Corp.*, 205 F.3d 831, 833 (5th Cir. 2000) ("Judicial estoppel applies to protect the integrity of the courts--preventing a litigant from contradicting its previous, inconsistent position when a court has adopted and relied on it.") (other citations omitted)). Inadvertence can be shown where the party in question either lacks sufficient knowledge of the undisclosed claims or would have no motive for their concealment. *Superior Crewboats, Inc. v. Primary P & I Underwriters* (*In re Superior Crewboats, Inc.*), 374 F.3d 330, 335 (5th Cir. 2004) (citing *In re Coastal Plains, Inc.*, 179 F.3d 197, 210 (5th Cir. 1999)).

[21] The Supreme Court in *New Hampshire v. Maine* recognized that "'[t]he circumstances under which judicial estoppel may appropriately be invoked are probably not reducible to any general formulation of principle.'" *New Hampshire v. Maine*, 532 U.S. at 750, 121 S.Ct. 1808. However, a general test for determining when judicial estopped may be invoked has been developed, as follows: (i) a party's later position is clearly inconsistent with its earlier position, (ii) the party's former position has been accepted in some way by the court in the earlier proceeding, such that "judicial acceptance of an inconsistent position in a later proceeding would create 'the perception that either the first or the second court was misled,' " and (iii) the "party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped." *New Hampshire v. Maine*, 532 U.S. at 750-51, 121 S.Ct. 1808.

[22] Judicial estoppel has been applied in the bankruptcy context where a debtor changes its designation on the petition. *See In re Save Our Springs (S.O.S.) Alliance, Inc.*, 393 B.R. 452 (Bankr. W.D. Tex. 2008) (judicial estoppel prevented the debtor from amending its petition to designate itself as a non-small business debtor because it was inconsistent with its original designation and the debtor had already enjoyed the benefits of expedited proceedings as a small business debtor.).

Relying on *In re Jones*, 556 B.R. 327 (Bankr. E.D. Mich. 2016) and *In re Orlando*, No. 17-41616 (CJP), 2018 WL 3637231 (Bankr. D. Mass. July 30, 2018), Gregory asserts that bankruptcy courts have adopted judicial estoppel to bar debtors from changing the description of their debts from consumer debts to non-consumer debts. In *In re Jones*, after the U.S. Trustee moved to dismiss the chapter 7 debtor's case under section 707(b) of the Bankruptcy Code, the debtor changed her response and indicated that her debts were "not primarily consumer debts, but were not primarily business debts either." *In re Jones*, 556 B.R. 327 at 330. The court in *In re Jones* noted that the timing of the debtor's change was indicative of "gamesmanship" on the part of the debtor in order to render section 707(b) inapplicable and escape possible dismissal of the case. *Id.* at 335. Similarly, in *In re Orlando*, the bankruptcy court found that the debtor's change in his position regarding the nature of his debts from consumer debts to business debts after the U.S. Trustee filed a motion to dismiss the debtor's case under 11 U.S.C. § 707(b) was a "late strategy change" instead of a mistake or inadvertence. *In re Orlando*, 2018 WL 3637231, at *4.

***14** **[23]** In applying the above factors to the Debtor's case, the Court finds that judicial estoppel does not bar the Debtor's change in description of the nature of her debts. First, it is not clear that her change of description of her Mortgage debt as a business debt is inconsistent with the Debtor's prior description of her debts. The Debtor referred to the Property as a bed and breakfast in the Current Case. By way of example, when the Debtor was asked "What is the property?" she checked the box "Other" and wrote "B&B Inn" on Schedule A/B instead of checking the box for "Single-family" home. (Case No. 8-18-77193-reg, ECF No.1.). In

Schedule C, the Debtor claimed an exemption for the Property pursuant to 11 U.S.C. § 522(b)(2) wherein she described it as "Bed & Breakfast." *Id.* Again, on Schedule D, the Debtor described the Property as a "Bed and Breakfast." *Id.* The Debtor also lists her income and expenses from the operations of Harbor Rose in her Statement of Current Monthly Income. *Id*. ECF No. 26. These representations by the Debtor reflect the hybrid nature of the Property, which is rare. The Property is integral to the business operations, and the Court finds that the Debtor was attempting to be clear and forthright in her representations regarding the Property and the Mortgage.

Second, the Court took no specific action in the Current Case or in the prior bankruptcy filings based on a description of the Mortgage debt as consumer debt. This Court was not misled about the nature of the Mortgage which encumbered the Property. Third, the Debtor cannot be said to have taken unfair advantage over Gregory by changing the description of her debts to fit within a statute that did not exist at the time of the Petition Date. It is more akin to an innocent choice by the Debtor than gamesmanship. The Debtor's change in status was not made in response to a 11 U.S.C. § 707(b) motion to dismiss by the U.S. Trustee, nor was it done with "the obvious motive" to make a certain law inapplicable. In fact, the law was not applicable at the time of the Petition Date because it did not exist. The SBRA was designed to protect small business debtors by affording them the right to reorganize in a timely, cost-effective manner. The Court also takes into consideration whether the Debtor's change in description of her debt, if permitted, would be unfairly detrimental to Gregory. Gregory points to the unfair burden and delay imposed, as Gregory was poised to confirm its proposed plan of liquidation that would have resulted in a sale of the Property and payment to Gregory from the sale proceeds. While the Court recognizes that there will be some prejudice to Gregory if the Debtor is permitted to recharacterize her debt, the Debtor must still satisfy the requirements of subchapter V in order to confirm a plan. There is no guarantee that the Debtor will be successful in this attempt, but given the current economic climate, it is doubtful that a sale of the Property could take place any time in the near future. Given the unique circumstances of this case, the prejudice to Gregory is minimized.

Finally, Gregory relies on case law where courts have judicially estopped debtors from changing their representations in petitions and schedules, made under penalties of perjury, when those changes were made because of changed circumstances in their bankruptcy cases. *See In re Osborne*, 490 B.R. 75 (Bankr. S.D.N.Y. 2013) (Court applied judicial estoppel where the debtors moved to vacate the discharge and dismiss their chapter 7 case following the discovery of a previously undisclosed asset.). Here, the Debtor is not reacting to the discovery of some wrongdoing she may have committed, nor did the Debtor make false claims in her petition. The Debtor is merely amending her petition and avail herself of the right created by a statute that did not exist as of the time of Petition Date. The cases cited by Gregory have a common denominator that is inapposite to the present case; they did not concern a newly enacted law that is designed to protect debtors like the Debtor in the Current Case, who are small business owners.

For all the reasons stated herein, this Court finds that the instant case comes within the purview of 11 U.S.C. § 101(51D)(A) because the primary use of the Property was, and remains, for the operation of a bed and breakfast, rather than as a principal residence. The fact that the Harbor Rose entwines the Debtor's personal and business life does not control whether the Mortgage is a business debt or a consumer debt. In essence, the Debtor is not changing her position; the significant changes to the Bankruptcy law enable the Debtor to take advantage of a new definition of "small business debtor" in order to attempt to save her business.

4. *Is the Debtor entitled to utilize 11 U.S.C. § 1190(3)?*

***15** Both the Debtor and Gregory agree that in order to propose a plan and successfully exit bankruptcy, the Debtor must be permitted to modify the Mortgage. Prior to the effective date of the SBRA, the only statutory provision the Debtor could rely on to modify the Mortgage was 11 U.S.C. § 1123(b)(5). This section permits chapter 11 debtors to propose a plan that modifies the rights of holders of secured claims "...other than a claim secured only by a security interest in real property that is the debtor's principal residence..." 11 U.S.C. § 1123(b)(5). The Debtor's proposed plan sought to utilize this provision to modify the Mortgage, but this Court found that because the Debtor uses the Property for both business and residential purposes, the Property is the Debtor's principal residence. *See In re Harriman*, 2014 WL 1312103 at *3 (Bankr. N.D. Cal.) (citing *In re Wages*, 508 B.R. 161, 168

(9th Cir. BAP 2014)). Therefore, the Debtor was prohibited from modifying the Mortgage under the law as it existed at the time.

The SBRA has given small business debtors who designate themselves as subchapter V debtors another tool to be used when proposing a plan. § 1190(3) provides as follows:

> A plan filed under this subchapter—
>
> (3) notwithstanding section 1123(b)(5) of this title, may modify the rights of the holder of a claim secured only by a security interest in real property that is the principal residence of the debtor if the new value received in connection with the granting of the security interest was—
>
> (A) not used primarily to acquire the real property; and
>
> (B) used primarily in connection with the small business of the debtor.

11 U.S.C. § 1190(3).

Although there are three decisions of record regarding application of the SBRA, only *In re Moore Props. of Person Cty., LLC* mentioned this particular provision. The *In re Moore Props. of Person Cty., LLC* court found that it did not apply in the case before it because the debtor was not an individual. *In re Moore Props. of Person Cty., LLC*, 2020 WL 995544, at *4 n.14. In *dicta*, the court did state that if this section did apply, the court would consider whether the application of 11 U.S.C. § 1190(3) constituted an impermissible taking. *Id.* Therefore, the Court cannot look to prior case law to interpret this section.

[24] **[25]** **[26]** **[27]** This Court shall commence its analysis by employing the applicable rules of statutory construction. The Court is charged with interpreting all federal and state statutes according to their plain meaning. *Tyler v. Douglas*, 280 F.3d 116, 123 (2d Cir. 2001), *cert. denied*, 536 U.S. 906, 122 S.Ct. 2361, 153 L.Ed.2d 182 (2002). In determining its degree of ambiguity or clarity, courts cannot examine statutory language in isolation. *Robinson v. Shell Oil Co.*, 519 U.S. 337, 341, 117 S.Ct. 843, 136 L.Ed.2d 808 (1997). The Court must determine the specific context in which the language appears, and the statutory scheme's broader framework in order to preserve the coherence and consistency of the statutory scheme. *U.S. v. Ron Pair Enters., Inc.*, 489 U.S. 235, 240-41, 109 S.Ct. 1026, 103 L.Ed.2d 290 (1989) (citing *Northern Pipeline Construc. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 52-53, 102 S.Ct. 2858, 73 L.Ed.2d 598 (1982)). "[I]n matters of statutory interpretation, the plain meaning of statutory language is often illuminated by considering not only the particular statutory language at issue, but also the structure of the section in which the key language is found, and the design of the statute as a whole and its object." *Pellegrino v. United States Transp. Sec. Admin.*, 896 F.3d 207, 216 n.10 (3d Cir. 2018) *reh'g en banc granted*, 904 F.3d 329 (3d Cir. 2018).

[28] **[29]** Armed with these principles, the Court will undertake its interpretation of this section. First, unlike 11 U.S.C. § 1123(b)(5), which precluded modifications of claims secured by mortgages on the debtor's principal residence, 11 U.S.C. § 1190(3) specifically permits the modification of claims secured by mortgages on the debtor's principal residence. Therefore, the plain language of the first paragraph of 11 U.S.C. § 1190(3) does not act as an impediment to the Debtor's attempt to modify the Mortgage. Indeed, the Property falls squarely within this paragraph.

***16** Second, subparagraphs (A) and (B) do not bar the Debtor outright from using this provision to modify the Mortgage. Subparagraphs (A) and (B) further limit the application of this provision to mortgage proceeds that were:

> (A) not used primarily to acquire the real property; and
>
> (B) used primarily in connection with the small business of the debtor.

[30] Starting with subparagraph (A), the statute reads that the mortgage proceeds cannot have been used "primarily to acquire the real property." As a matter of common usage, the word "primarily" means "for the most part." *Primarily*, Merriam-Webster's Law Dictionary, (last visited Apr. 9, 2020). In the context of the 1954 Internal Revenue Code, the Supreme Court held that "primarily" means "of first importance" or "principally" rather than meaning "substantial." *Malat v. Riddell*, 383 U.S. 569, 572, 86 S.Ct. 1030, 16 L.Ed.2d 102 (1966). The phrase "real property" refers back to the real property that is the debtor's residence. In this case, the question for the Court to answer is whether the Mortgage proceeds were used primarily to purchase the Debtor's residence. Unlike 11 U.S.C. § 1123(b)(5) which

took an all-or-nothing approach to loans securing the debtor's residence, 11 U.S.C. § 1190(3) asks the Court to determine whether the primary purpose of the mortgage was to acquire the debtor's residence.

[31] **[32]** Subparagraph (B) requires the Court to determine whether the mortgage proceeds were used primarily in connection with the debtor's business. Both of these subparagraphs direct the Court to conduct a qualitative analysis to determine whether the principal purpose of the debt was not to provide the debtor with a place to live, and whether the mortgage proceeds were primarily for the benefit of the debtor's business activities. This interpretation is consistent with the purpose and intent of the SBRA, which is to assist small business owners in whatever form they take, and to give them speedy access to relief via the bankruptcy process. As stated above, the Congressional intent of the SBRA was to keep small business owners in business, and to benefit the employees, suppliers, customers and others who rely on that business. A reading of this provision which takes into account the primary purpose of the mortgage debt instead of a bright-line test that would reject any business owner in the Debtor's unique position is consistent with the intent of the legislation.

[33] Clearly, some business owners, such as business owners who took out a second mortgage and used the proceeds to buy farm equipment or a taxi medallion, easily fall into this classification. However, an inflexible reading of this statute would bar legitimate business owners such as the Debtor from obtaining relief under the SBRA. The Court does not find that this interpretation would be consistent with the goals of the SBRA.

[34] The Court proposes that the following factors be considered to determine whether the mortgage in question is subject to modification under this section:

1. Were the mortgage proceeds used primarily to further the debtor's business interests;

2. Is the property an integral part of the debtor's business;

3. The degree to which the specific property is necessary to run the business;

4. Do customers need to enter the property to utilize the business; and

***17** 5. Does the business utilize employees and other businesses in the area to run its operations.

In the Debtor's case, she did not purchase a residence and use one room as an office space. The Debtor bought real property and commenced using the rooms to rent and spent considerable time and resources on obtaining the proper permits to run the Property as a bed and breakfast. The primary purpose of the Property is to offer rooms for nightly fees. Harbor Rose serves a variety of guests, including guests visiting the nearby Cold Spring Harbor labs. Harbor Rose also provides holistic services to the guests staying at the Property with package services offered for additional fees. Although the Mortgage proceeds were not used to refurbish the Property or to obtain the proper zoning changes and permits, the Mortgage proceeds were used to purchase the building that houses the business run by the Debtor.

Based on its interpretation of 11 U.S.C. § 1190(3), the Court finds that there is sufficient evidence to hold a full evidentiary hearing to determine whether the Debtor may use this statute to modify the Mortgage. Therefore, if the Debtor proposes a plan which provides for bifurcation of the Mortgage, the Court shall schedule a hearing to determine whether she may take advantage of this provision using the factors listed above, along with any additional evidence produced by the parties.

Conclusion

For all the reasons stated herein, the Court finds that the Debtor is a "small business debtor" within the purview of 11 U.S.C. § 101(51D)(A) and is eligible to proceed as a subchapter V debtor in this case. Therefore, the Court overrules the U.S. Trustee Objection and overrules the objections raised by Gregory in the Motion. An order consistent with this Memorandum Decision will be entered forthwith.

All Citations

--- B.R. ----, 2020 WL 1867898

Footnotes

1 Gregory has filed an Objection to Debtor's Designation as a Sub-Chapter V. ECF No. 89 and a motion seeking the same relief, ECF No. 92. The Court will refer to both filings as the Motion, ECF No. 92.

2 Late on the evening of March 25, 2020, the U.S. Senate unanimously passed the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) (S.3548) to combat the U.S. spread of coronavirus, which threatens to plunge U.S. into a global recession. For one year, the Act increases the eligibility threshold to file under subchapter V of chapter 11 of the Bankruptcy Code to businesses with less than $7.5 million of debt.

3 As set forth in the facts, the Court ruled that because the Debtor resided at the Property, she could not modify the Mortgage under this provision.

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United States Bankruptcy Court, E.D. New York.

In re: David Telles, Debtor.

Case No. 8-20-70325-reg
|
Dated: Central Islip, New York April 30, 2020

Chapter 13

Memorandum Decision

Robert E. Grossman United States Bankruptcy Judge

***1** Before the Court is a motion for relief from the automatic stay *nunc pro tunc* to January 15, 2020 filed by Wilmington Savings Fund Society, FSB as owner trustee of The Residential Credit Opportunities Trust V-D ("Wilmington"). This is the second decision issued by this Court in response to the Supreme Court's holding concerning *nunc pro tunc* relief in *Roman Catholic Archdiocese of San Juan v. Acevedo Feliciano,* 140 S. Ct. 696 (2020). This decision accompanies *In re Benitez*, No. 19-70230 (REG), 2020 WL 1272258 (Bankr. E.D.N.Y. Mar. 13, 2020).

Wilmington holds a judgment of foreclosure and sale with respect to the property at 68 Paumanake Road, Blue Point NY 11715 (the "Property") belonging in part to David Telles (the "Debtor"). Wilmington purchased the Property at a foreclosure sale that took place two days after the Debtor filed a bankruptcy petition. Wilmington was unaware of the Debtor's bankruptcy filing at the time of the foreclosure sale. This lack of knowledge appears to be largely due to the Debtor's failure to notify the state court referee of his bankruptcy. Wilmington now asks this Court for relief from the automatic stay *nunc pro tunc* to the day before the sale. Wilmington argues that the Court should not permit such an obvious abuse of the bankruptcy laws to benefit the Debtor. Wilmington is not arguing that it did not violate the automatic stay, but it asks this Court to utilize its power to grant the requested relief in the interest of fairness and in keeping with the purpose of the bankruptcy laws. This argument has been accepted in the past when courts, including courts in this district, have granted *nunc pro tunc* relief to correct what they in good faith believed were unfair results. While this Court has the utmost respect for the judges that have granted similar relief, this Court has never granted relief from the automatic stay *nunc pro tunc* to put its imprimatur on an otherwise void foreclosure sale. In the past, these motions have been routinely denied without issuing a written decision, but the Court finds that in light of *Acevedo*, the reasons for the Court's position are worth explaining.

In *Acevedo* the Supreme Court held that "[f]ederal courts may issue *nunc pro tunc* orders, or 'now for then' orders, ... to 'reflect [ ] the reality' of what has already occurred .... 'Such a decree presupposes a decree allowed, or ordered, but not entered, through inadvertence of the court.' ... Put colorfully, '[n]unc pro tunc orders are not some Orwellian vehicle for revisionist history — creating 'facts' that never occurred in fact.'" *Acevedo*, 140 S. Ct. at 700-01 The issue in *Acevedo* concerned orders issued by a state court that lacked jurisdiction at the time of their issuance. Because the state court did not have jurisdiction over the case, its orders were deemed void. The Supreme Court held that *nunc pro tunc* relief could not cure the jurisdictional defect and therefore the state court orders were void and of no force and effect.

The circumstances here are materially the same. The state court was divested of jurisdiction upon the filing of the Debtor's bankruptcy. Because the foreclosure sale whereby Wilmington acquired title to the property was held after the filing of the bankruptcy petition, the state court had already been divested of jurisdiction to conduct the foreclosure sale, rendering all subsequent acts by the state court in the foreclosure proceeding void. Therefore, as a matter of law Wilmington never received valid title to the Property, and the Debtor's interest in the Property remains property of the bankruptcy estate subject to this Court's further orders. Even though the facts of this case as well as other cases pending across the nation may lead this Court to sympathize with a purchaser who successfully bids on such property without knowledge of the intervening bankruptcy, the Court cannot ignore or paper over the fact that we must abide by the law as set forth in the Bankruptcy Code. If these laws need to be amended it is the responsibility of Congress. The automatic stay is a bedrock principle of the bankruptcy laws. It provides a debtor with breathing space and promotes the preservation of a debtor's assets for the benefit of all creditors. The laws are equally clear regarding the circumstances pursuant to which

a party may seek relief from the automatic stay. This Court does not believe it can avoid what is an unambiguous statute by artificially legitimizing a void foreclosure sale conducted *coram non judice* through use of a *nunc pro tunc* order. For these and the reasons that follow, Wilmington's motion is denied.

Factual Background and Procedural History

***2** The Debtor holds an interest in the Property. Mot. Ex. C. The Property is secured by a mortgage originally held by Onewest Bank, FSB. Non-debtor Jeffrey A. Bevis ("Bevis") is the mortgagor. Mot. Ex. A. Onewest Bank, FSB commenced a foreclosure action with respect to the Property on January 7, 2011. *Id.* The Debtor, who apparently resided at the Property but had no legal interest in the Property at the time, was included as a defendant in the foreclosure action. Manniello Aff. 2; Mot. Ex. A. A judgment of foreclosure and sale was entered on March 5, 2019. Mot. Ex. A. A sale was scheduled for May 16, 2019 (the "May Sale"). Mot. Ex. B.

Two days before the May Sale, Bevis deeded a ten percent interest in the Property to the Debtor. Mot. Ex. C. The Debtor filed a petition for relief under chapter 13 of the Bankruptcy Code (the "Code") on the day after receiving an interest in the Property and one day before the

May Sale (the "First Bankruptcy"). The First Bankruptcy was dismissed pursuant to section 521(i) of the Code on July 1, 2019 for failure to file the required schedules and statements. After dismissal of the First Bankruptcy, a second foreclosure sale was scheduled for January 16, 2020 (the "January Sale"). Mot. Ex. F. The Debtor filed a second chapter 13 petition on January 14, 2020 (the "Second Bankruptcy"). Counsel for Wilmington represented that at some point before the January Sale Onewest Bank, FSB assigned its interest in the Property to Wilmington. Wilmington asserts that neither it nor the state court referee received notice from the Debtor of the Second Bankruptcy. Manniello Aff. 2-3. The Debtor maintains that counsel for Wilmington received proper notice. Opp'n. 1-2. Although representing that it had performed a search on the PACER database for any bankruptcies filed by Bevis on the day before and day of the January Sale, Wilmington admits it inadvertently neglected to perform a similar search for the Debtor – a named defendant in the foreclosure action. *Id.* at 4-5. Wilmington asserts that it did not receive notice of the Second Bankruptcy until a prospective purchaser obtained a title report. *Id* at 2-3. The January Sale was held as scheduled despite the filing of the Second Bankruptcy, and Wilmington emerged as the successful bidder. Mot. Ex. G.

The chapter 13 trustee filed a motion to dismiss the case returnable for April 30, 2020. Out of concern that the case would be dismissed before it could address the issues with the January Sale, Wilmington sought an emergency hearing where the Court would hear its motion to lift the automatic stay *nunc pro tunc* to January 15, 2020 prior to dismissal of the Second Bankruptcy (the "Motion"). The requested relief was designed for this Court to bless the state court sale of the Property. The Court issued an order to show cause on April 24, 2020 scheduling the matter to be heard with the chapter 13 trustee's motion to dismiss on April 30, 2020. The Debtor responded to the Motion and the chapter 13 trustee's motion to dismiss the case on the day before the hearing, but the Debtor failed to appear at the hearing. At the hearing, Court denied the Motion and advised that a written decision would follow. The chapter 13 trustee's motion was adjourned to June 11, 2020 at 9:30 a.m.

Discussion

1. The Motion

Wilmington relies on the assertion that "[a] bankruptcy court may enact an 'annulment'—granting relief from the automatic stay nunc pro tunc, thereby retroactively lifting the stay to permit a certain otherwise forbidden course of action, such as a civil litigation or a foreclosure proceeding." Manniello Aff. 3 (quoting *NKL Enters., LLC v. Oyster Bay Mgmt. Co., LLC,* No. 12-CV-5091 (ADS), 2013 US Dist LEXIS 59479, at *9, 2013 WL 1775051 (E.D.N.Y. Apr. 25, 2013)). Wilmington also cites *In re Cunningham,* 506 B.R. 334 (Bankr. E.D.N.Y. 2014) and *In re Jean-Francois,* 516 B.R. 699 (E.D.N.Y. 2014) to support the proposition that other courts in this district have permitted the use of *nunc pro tunc* relief in similar situations. *See* Manniello Aff. 5.

***3** Wilmington argues that (1) the Debtor should not be granted the "breathing room" of the automatic stay because he was already afforded that opportunity in the First Bankruptcy and took no steps to comply with his responsibilities as

a debtor; (2) the Debtor never intended to proceed in good faith with this case, and the sole purpose for filing was to impede Wilmington's foreclosure efforts; and (3) Wilmington's continuation of the sale while the stay was in place was unintentional. Wilmington's position is that the conduct of the Debtor and Bevis combined with Wilmington's good faith participation in the subject proceedings give rise to "compelling circumstances" that would permit this Court to grant relief *nunc pro tunc* to January 15, 2020. Maniello Aff. 4-5. Wilmington also asserts that it is entitled to relief from the automatic stay pursuant to section 362(d)(2) because the amount of the subject mortgage exceeds the value of the Property. Manniello Aff. 4-5. The Debtor states in response that (1) he filed the petition in good faith and has submitted the required documentation; (2) Wilmington's counsel received notice of this bankruptcy; and (3) the foreclosure sale was conducted in violation of the automatic stay and is therefore void *ab initio*. Opp'n. 1-4.

2. Nunc Pro Tunc Relief Under Acevedo Feliciano

The Supreme Court recently provided guidance regarding requests for *nunc pro tunc* relief in the context of curing jurisdictional defects in a prior proceeding. While the facts of the case were complicated, the underlying principles are relatively straightforward. In *Roman Catholic Archdiocese of San Juan v. Acevedo Feliciano,* 140 S. Ct. 696 (2020), the Office of Superintendent of Catholic Schools of the Archdiocese of San Juan created a trust to administer a pension plan for Catholic school employees. *Acevedo,* 140 S. Ct. at 697. Active and retired employees filed complaints against the legal entity allegedly in charge of all Catholic institutions in Puerto Rico, the Archdiocese of San Juan, the Superintendent of Catholic Schools of the Archdiocese of San Juan, several academies, and the trust in the Puerto Rico Court of First Instance alleging that the trust had improperly terminated the pension plan. *Id.* After litigation concerning a preliminary injunction requiring the payment of benefits rose to the Supreme Court of Puerto Rico, the Supreme Court of Puerto Rico remanded the case to the Court of First Instance to determine who was responsible for continuing to pay the pensions pursuant to the preliminary injunction. *Id.* at 698. The Court of First Instance eventually determined that the Roman Catholic and Apostolic Church in Puerto Rico (the "Church") was the only defendant with separate legal personhood and ordered the Church to pay the employees pursuant to the pension plan. *Id.* The Court issued a second order ten days later requiring the Church to deposit $4.7 million in a court account and a third order requiring the sheriff to seize Church assets in Puerto Rico the day after the second order. *Id.* After the Court of Appeals reversed the Court of First Instance's ruling, the Puerto Rico Supreme Court reversed the Court of Appeals and held that the only defendant with separate legal personhood and the only defendant who could be ordered to pay the employees' pensions was the Church. at 698-99.

The Archdiocese petitioned the Supreme Court for a writ of certiorari arguing that the Free Exercise and Establishment Clauses in the First Amendment entitled the Church to deference on how it structured itself, which meant that the separate legal personalities would exist for each diocese and parish in Puerto Rico. *Id.* at 699. The Solicitor General also filed a brief on behalf of the United States as *Amicus Curiae* arguing that the Puerto Rico Supreme Court violated the Free Exercise Clause. *Id.*

The Supreme Court held that it did not need to address the arguments of the Archdiocese or the Solicitor General because it found that the Court of First Instance lacked jurisdiction to issue the payment and seizure orders in the first place. *Id.* On February 6, 2018, post-remand from the Supreme Court of Puerto Rico, the Archdiocese removed the case to the District Court for the District of Puerto Rico, arguing that the subject trust filed for chapter 11 under the Code and that the dispute was sufficiently related to the bankruptcy for federal jurisdiction to exist. *Id.* at 700. The Bankruptcy Court dismissed the trust's bankruptcy on March 13, 2018. *Id.* Importantly, the three payment and seizure orders were issued March 16, 26, and 27, 2018 even though the District Court did not remand the case to the Court of First Instance until August 20, 2018. The remand order was entered *nunc pro tunc* to March 13, 2018. *Id.* at 700-01.

***4** The Supreme Court found that the Court of First Instance had lost jurisdiction upon removal and that the three subject orders were "absolutely void." *Id.* at 700. Importantly, the Supreme Court held that the *nunc pro tunc* remand order could not save the deficiency. The Supreme Court clarified that a *nunc pro tunc* order may not be used to cure the absence of a decree on a prior date and instead is properly used to correct the record to "reflect the reality of what has already occurred." *Id.* at 700-01 (internal citations and quotations omitted). Although dismissal occurred on March

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13, 2018, the remand order was not entered simultaneously. As such, there was no record to correct "to reflect the reality of what has already occurred." *Id.* Even though the bankruptcy case was dismissed, the jurisdiction of the Court of First Instance was not restored until remand actually occurred, and a *nunc pro tunc* order from a federal court could not retroactively confer jurisdiction upon the state court. As a result, any actions performed by the Court of First Instance in the interim between dismissal and remand were held void and unenforceable. *Id.*

3. Analysis

The Court understands Wilmington's predicament. The Debtor was not a mortgagor, received a 10% interest in the Property days before the May Sale, and filed the First Bankruptcy just in time to stop the May Sale. The circumstances of the transfer are at best suspicious. Further, the Debtor notified neither Wilmington nor the referee of the Second Bankruptcy. The January Sale proceeded while Wilmington had no knowledge of the Second Bankruptcy. [1] The Court is aware of the apparent gamesmanship that accompanied the deeding of the Property to the Debtor and the filing of the Debtor's bankruptcies. No matter the outcome of the Debtor's case, absent granting *nunc pro tunc* relief from the automatic stay, Wilmington's options regarding the Property will be limited. It may be difficult for Wilmington to effectively transfer the Property to a third party because of issues surrounding title to the Property. The Debtor or another tenant may file for bankruptcy relief in an effort to stop another foreclosure sale from taking place, which will cause Wilmington to incur additional costs and expense.

Given the conduct described above, Wilmington seems like a strong candidate for retroactive relief. There is case law within this District which would support of such a finding. *See In re Cunningham,* 506 BR 334, 346 (Bankr. E.D.N.Y. 2014) (granting *nunc pro tunc* relief from the automatic stay after a debtor incorrectly filed a secured creditor's address on the creditor matrix, and the creditor never received notice of the bankruptcy); *In re Jean-Francois*, 516 B.R. 699, 704-07 (E.D.N.Y. 2014) (affirming a Bankruptcy Court's *nunc pro tunc* annulment of the automatic stay after the debtor filed for bankruptcy 20 minutes prior to a foreclosure sale and in light of a finding that the debtor acted in bad faith). Some courts would generally weigh seven factors when deciding whether to annul the automatic stay:

> (1) if the creditor had actual or constructive knowledge of the bankruptcy filing and, therefore, of the stay; (2) if the debtor has acted in bad faith; (3) if there was equity in the property of the estate; (4) if the property was necessary for an effective reorganization; (5) if grounds for relief from the stay existed and a motion, if filed, would likely have been granted prior to the automatic stay violations; (6) if failure to grant retroactive relief would cause unnecessary expense to the creditor; and (7) if the creditor has detrimentally changed its position on the basis of the action taken.

Cunningham, 506 B.R. at 343-44.

While the Court recognizes the factual similarities among these and other decisions, Wilmington's reliance on *Cunningham* and *Jean-Francois* without taking into consideration *Acevedo* is misplaced. The landscape of the law is different post-*Acevedo,* and this Court is bound to follow the precedent set by the Supreme Court. The Supreme Court has clarified that *nunc pro tunc* relief cannot be used to confer jurisdiction where none existed. *Acevedo,* 140 S.Ct. at 700-01. Once a debtor files for bankruptcy, the state court is divested of jurisdiction over property of the estate, and any action taken by the state court with respect to the debtor's property is void. *See Id.* at 700 ("Once a notice of removal is filed, the [s]tate court shall proceed no further unless and until the case is remanded. The state court loses all jurisdiction over the case, and, being without jurisdiction, its subsequent proceedings and judgement are not simply erroneous, but absolutely void.") (internal citations and quotations omitted)

***5** Here, the state court was divested of jurisdiction over the Debtor and the Property upon the filing of the Second Bankruptcy. The January Sale, which occurred two days after the filing of the Second Bankruptcy, was void. [2] *Acevedo,* 140 S.Ct. at 700. The Bankruptcy Court cannot grant the *nunc pro tunc* relief sought by Wilmington because there was never

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a determination by this Court vacating the stay prior to the foreclosure sale. In other words, *nunc pro tunc* relief cannot be used to change the outcome of a void foreclosure sale. As this Court recognized prior to *Acevedo*, a *nunc pro tunc* order cannot bless a state court authorized foreclosure sale where the automatic stay has deprived the state court of such jurisdiction.

This Court is aware of four cases, other than *Benitez*, that have addressed *Acevedo* since its issuance, and none are inconsistent with the Court's finding that it cannot grant *nunc pro tunc* relief from the automatic stay in order to cure a jurisdictional defect in a state court proceeding. *In re Brzowski*, 798 Fed. Appx. 22, 23 (7th Cir. 2020) (quoting *Acevedo* for the assertion that "once a notice of removal is filed, the state court loses all jurisdiction over the case"); *Washington v. Reliance Standard Life Ins. Co.*, No. LA CV-20-01771 (JAK) (MRWx), 2020 U.S. Dist. LEXIS 67083, at *3 (C.D. Cal. Apr. 16, 2020) (quoting *Acevedo* for the assertion that "once a notice of removal is filed, 'the State court shall proceed no further unless and until the case is remanded' "); *In re Berk*, No. DG 17-04498 (SWD), 2020 Bankr. LEXIS 944, at *6, 2020 WL 1651228 (Bankr. W.D. Mich. Apr. 2, 2020) ("The Debtor asks the court to 'vacate' the Dismissal Order, presumably implying that the court and others should treat it as if it never happened, but after the recent decision of the Supreme Court in [*Acevedo*], it is not entirely clear that the court has authority to grant *nunc pro tunc* relief under the circumstances, or at least the court must hesitate before doing so."); *In re Goldberg*, No. 18-03592-5 (JNC), 2020 Bankr. LEXIS 869, at *3 n.1, 2020 WL 1526923 (Bankr. E.D.N.C. Mar. 27, 2020) (Finding that a foreclosure sale that occurred pre-default under a reaffirmation agreement was valid after a consent order lifting the stay was entered roughly two months prior to the sale date and holding that the caption on the order stating *nunc pro tunc* was not in conflict with *Acevedo* because "unlike the order at issue [in *Acevedo*], the FCB consent order did not 'change history,' but rather solidified for the record an actual set of events. Usage of the term nunc pro tunc here is superfluous as the actual effect of the consent order is to protect FCB from needless collateral attack and bolster rather than change history."). The Court's holding does not conflict with its recent holding in *In re Benitez*, No. 19-70230 (REG), 2020 WL 1272258 (Bankr. E.D.N.Y. Mar. 13, 2020). *Benitez* concerned an application by a chapter 7 trustee seeking retention of general counsel *nunc pro tunc* to a date roughly eleven months prior to the filing of the subject motion. *Benitez,* 2020 WL 1272258, at 1. This Court found that *nunc pro tunc* relief was not required under the relevant sections of the Code and case law for the Court to rule on the retention motion. *Id.* at *3-5.

If the Court were to grant the Motion, this ruling would be squarely at odds with *Acevedo* and subject to reversal on appeal. Based on the Supreme Court's decision that *nunc pro tunc* relief cannot be granted to confer jurisdiction on a state court where none existed, the motion must be denied in its entirety. [3]

Conclusion

***6** For the reasons stated above, the Motion is denied. An order consistent with this Memorandum Decision will be entered forthwith.

All Citations

Slip Copy, 2020 WL 2121254

Footnotes

1 It is worth noting Wilmington's failure to perform a PACER search for the Debtor even though the Debtor had already filed a petition to stop a sale once and was a named defendant in the foreclosure action.

2 To hold otherwise would prematurely dispose of rights that the Debtor still possessed in the Property.

3 The Court does not make any findings beyond a circumstance where a movant requests *nunc pro tunc* relief to legitimize an otherwise void action by a state court that lacked jurisdiction over the dispute.

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2020 WL 1272258
United States Bankruptcy Court, E.D. New York.

In re: Hector Benitez, Debtor.

Case No. 8-19-70230-reg
|
Dated: Central Islip, New York March 13, 2020

Chapter 7

DECISION

Robert E. Grossman United States Bankruptcy Judge

***1** Before the Court is a motion by the chapter 7 trustee, Marc A. Pergament, (the "Trustee") for an order approving the retention of Weinberg, Gross & Pergament LLP ("WGP") as general counsel to the Trustee *nunc pro tunc* to February 2, 2019 (ECF No. 18, "Motion to Retain").[1] "*Nunc pro tunc* retentions" are common practice in bankruptcy matters largely resulting from the statutory framework for compensation of estate professionals set forth in sections 327 and 330 of the Bankruptcy Code ("Code"), and Rule 2014 of the Federal Rules of Bankruptcy Procedure ("Rules"); that is, professionals seeking compensation from the estate, such as general counsel retained by a chapter 7 trustee, may not be compensated under section 330 unless they have been retained under section 327. Many courts have interpreted sections 327, 330 and Rule 2014 to mean that estate professionals may not be compensated for services rendered prior to the effective date of the court order approving that professional's retention. However, the delay between commencement of services to the estate, the filing of a motion for court approval and the entry of the order approving the retention may take several weeks.[2] In most cases it is impractical and possibly detrimental to the estate for the professional to delay providing what may be critical services until entry of the order approving their retention. Courts have addressed this situation by, in specific cases, approving *nunc pro tunc* retentions so that the date of approval of the professional's retention dates back to the date of the trustee's application, or in some cases to the date of commencement of the professional's services. In the Motion to Retain before the Court, the Trustee asks this Court to approve his counsel's retention *nunc pro tunc* to February 2, 2019 – approximately eleven months prior to the filing of the Motion to Retain.

The Supreme Court's recent decision in *Roman Catholic Archdiocese of San Juan, Puerto Rico v. Acevedo Feliciano,* __ S.Ct. __, No. 18-921, 2020 WL 878715 (February 24, 2020), requires this Court to, *sua sponte*, review its practice of *nunc pro tunc* retentions. In *Acevedo* the Court held that "[f]ederal courts may issue *nunc pro tunc* orders, or 'now for then' orders, ... to 'reflect [ ] the reality' of what has already occurred .... 'Such a decree presupposes a decree allowed, or ordered, but not entered, through inadvertence of the court.' ... Put colorfully, '[n]unc pro tunc orders are not some Orwellian vehicle for revisionist history – creating 'facts' that never occurred in fact.' " *Id.* at *3-4 (citations omitted). The holding in *Acevedo* raises serious questions about the use of *nunc pro tunc* relief for purposes other than to reflect an event that has already occurred but is not accurately reflected in the court's records. This Court's reading of *Acevedo* is that utilizing *nunc pro tunc* orders to approve the retention of estate professionals retroactive to some date prior to the actual date of court approval is inappropriate.

***2** It is this Court's determination, however, that retroactive approval of the retention of an estate professional, whether it be *nunc pro tunc, post-facto* or any similar nomenclature, is not mandated under the Code or Rules. The Court finds that neither the Code nor the Rules preclude an award of "reasonable compensation" or reimbursement for "actual, necessary expenses" pursuant to section 330 for services rendered prior to an order approving retention of the professional. The only temporal requirement in the Code and Rules is that a professional must have been retained pursuant to section 327 to successfully obtain a court award of compensation. Simply stated, a professional must be retained as required by the statute, but once having been retained, the bankruptcy court is free to compensate him for services rendered to the estate at any time, pre and post-court approval, in accordance with section 330 of the Code.

Based upon its analysis of the law this Court will no longer require or grant *nunc pro tunc* retentions. This does not mean that a professional providing services to the estate should delay in seeking court approval of retention. A late applicant runs the risk that court approval under section 327 may

be withheld on the basis of disinterestedness or some other statutory infirmity, which will preclude compensation under section 330. In addition, it is this Court's view that late-filed retention applications should be subject to heightened scrutiny. Such applications must contain a detailed recitation of: the reasons for the delay in seeking court approval; the services already performed by the proposed professional, and the approximate amount billed up to the date of the application; the results obtained; and any future services that are contemplated. The late applicant runs the risk that court approval may be withheld on the basis that, in hindsight, the services performed by the proposed professional did not benefit the estate.

In the instant Motion to Retain, the Trustee's only stated basis for retaining WGP is to pursue the turnover of assets. The Court's review of the docket reveals that in the nearly one-year period prior to the filing of the Motion to Retain the Trustee and/or WGP filed a notice of discovery of assets, drafted and mailed two one-page letters seeking turnover of assets and information, filed a short motion to compel turnover, and examined the Debtor at a meeting of the creditors pursuant to section 341. With the exception of the motion to compel turnover, these tasks are inherent functions of the Trustee. Even though the motion to compel turnover did, according to the Trustee, lead to the turnover of $1,579.28, without more information the Court is unable to determine whether the WGP's services were necessary or reasonable in light of the results obtained. For this and the reasons that follow, the Motion to Retain is denied without prejudice to further application consistent with this Decision.

Factual Background and Procedural History

Hector Benitez (the "Debtor") filed a voluntary petition for relief under chapter 7 of the Code on January 10, 2019 (the "Petition"). Marc A. Pergament was appointed as the Interim chapter 7 Trustee. Motion to Retain ¶1. The first meeting of creditors pursuant to section 341(a) was held on February 12, 2019. Motion to Retain ¶4. The Trustee filed a notice of discovery of assets on February 21, 2019. The Debtor received a chapter 7 discharge on May 23, 2019.

On January 7, 2020, contemporaneously with the filing of the Motion to Retain, the Trustee filed a motion to compel the Debtor to turnover several documents, the sum of $1,579.28, and the Debtor's 2018 income tax refunds. (ECF No. 19, "Motion to Compel"). Attached to the Motion to Compel were two letters sent to the Debtor's attorney on February 21, 2019 and November 15, 2019 requesting various documents. A hearing was scheduled for March 11, 2020, but the Trustee withdrew the Motion to Compel on February 25, 2020, which he subsequently explained was due to the Debtor's ultimate compliance with his requests.

***3** The Motion to Retain was filed nearly one year post-petition and eleven months after WGP commenced services to the estate. Thus, the Trustee seeks "*nunc pro tunc*" approval of WGP's retention to February 2, 2019. The Trustee alleges that WGP is needed to perform "such legal services for [the Trustee] which may be necessary herein, including pursuing the turnover of assets." Motion to Retain ¶4. The Trustee represented that neither he nor WGP possess any interest adverse to the Debtor and that WGP qualified as a "disinterested person" under section 101 of the Code. *Id.* ¶7. A hearing on the Motion to Retain was held on March 11, 2020. For reasons stated at the hearing, the Court denied the Motion to Retain and advised that this written decision would follow.

Discussion

A. Applicable Provisions of the Code and Rules

Section 327 provides, "[e]xcept as otherwise provided in this section, the trustee, with the court's approval, may employ one or more attorneys, accountants, appraisers, auctioneers, or other professional persons, that do not hold or represent an interest adverse to the estate, and that are disinterested persons, to represent or assist the trustee in carrying out the trustee's duties under this title." 11 U.S.C. § 327(a). Section 330 states in pertinent part:

> **(a)(1)** After notice to the parties in interest and the United States Trustee and a hearing, and subject to sections 326, 328, and 329, the court may award to a trustee, a consumer privacy ombudsman appointed under section 332, an examiner, an ombudsman appointed under section 333, or a professional person employed under section 327 or 1103--

(A) reasonable compensation for actual, necessary services rendered by the trustee, examiner, ombudsman, professional person, or attorney and by any paraprofessional person employed by any such person; and

(B) reimbursement for actual, necessary expenses.

11 U.S.C. § 330(a).

Rule 2014 requires an applicant seeking to employ a professional under section 327 to state, among other things, "the name of the person *to be employed* ... [and] the professional services *to be rendered* ..." Fed. R. Bankr. P. 2014(a) (emphasis added).

B. Neither the Code Nor the Rules Explicitly Require Court Approval of Retention Prior to the Rendering of Compensable Services by an Estate Professional

Sections 327 and 330 collectively contain a single temporal limitation. To be eligible for an award of compensation from the estate, a professional's retention must first have been approved by the court pursuant to section 327. *See Lamie v. U.S. Tr.,* 540 U.S. 526, 538-39 (2004); 11 U.S.C. § 330 (permits the court to award reasonable compensation to "a professional person employed under section 327 or 1103 of this title"). Assuming the court has approved the professional's retention under section 327 prior to an award of compensation, neither the Code nor the Rules state that the professional may not be compensated under section 330 for services provided to the estate prior to court approval of their retention. The Court recognizes that the retention language of Rule 2014 seems to contemplate prospective approval only, i.e., Rule 2014 refers to persons "to be employed" and the services "to be rendered." This has been interpreted by some courts as prohibiting compensation under section 330 for services rendered prior to court approval. *See, e.g.*, *In re McDaniels,* 86 B.R. 128, 129 (S.D. Ohio 1988). This Court does not agree with this interpretation. The better view is that the rule does not explicitly require prior approval for the rendered services to be subject to court review under section 330 and prior approval should not be read into the rule.[3] *See In re Jarvis,* 53 F.3d 416, 419-20 (1st Cir. 1995); *see also Matter of Singson,* 41 F.3d 316, 319 (7th Cir. 1994) (Section 327(a) "does not say that the approval must precede the engagement, and neither does Fed. R. Bankr. P. 2014(a), which implements § 327(a). Prior approval is strongly preferred because it permits close supervision of the administration of an estate, wards off 'volunteers' attracted to the kitty, and avoids duplication of effort. Nothing in the statute forbids or even reproves belated authorization, however; timing is a matter of sound judicial administration rather than legislative command.") (internal citations omitted).

***4** The Court recognizes there are policy concerns that support a requirement of court approval of the retention prior to rendering services to the estate. Prior approval permits the court to maintain control of costs, prevents volunteerism, and serves as a gate-keeper for potentially non-disinterested parties. *See, e.g.*, *Farinash v. Vergos (In re Aultman Enterprises)*, 264 B.R. 485, 490 (E.D. Tenn. 2001) ("Were the law otherwise, there would be no limit to the burden which might be placed upon an estate if attorneys for the bankrupt or individual creditors could, by doing work which it is not their duty to do, by assisting the trustee, without an order of court allowing their special employment, burden the estate with the added cost of performing work which it is the duty of others to perform ... Because professionals employed by the estate must 'not hold or represent an interest adverse to the estate,' and must be 'disinterested persons,' the requirement of prior court approval also prevents unscrupulous individuals from taking advantage of the bankruptcy process to advance their own self-interest."); *In re Met-L-Wood Corp.*, 103 B.R. 972, 975 (Bankr. N.D. Ill. 1989), *aff'd*, 115 B.R. 133 (N.D. Ill. 1990); *McDaniels,* 86 B.R. at 129.

This Court believes that the retention and compensation approval processes built into sections 327 and 330 address these policy concerns. First, volunteers and non-disinterested professionals run the risk that they will fail to obtain court approval of their employment under section 327, and thus they will be unable to seek compensation under section 330.[4] *See Land West, Inc. v. Coldwell Banker Commercial Grp, Inc., (In re Haley),* 950 F.2d 588, 590 (9th Cir. 1991). *See discussion, infra,* part D. Second, assuming the professional is ultimately retained, that professional's fees are still subject to court approval under section 330 which requires that the compensation be "reasonable" and "for actual, necessary services rendered" or "reimbursement for actual, necessary

expenses." 11 U.S.C. § 330(a)(1). Any concerns about the value of services rendered to the estate will be addressed by the Court upon the estate professional's fee application.

C. The Second Circuit's 'Per Se' Rule

Many courts and commentators have stated that the Second Circuit has adopted a *per se* rule that "denies compensation to a professional who renders pre-appointment services to a debtor." *In re Household Merit, Inc.,* No. 94-62969 (SDG), 1995 WL 936707, at *2 (Bankr. N.D.N.Y. 1995); *see Matter of Futuronics Corp.,* 655 F.2d 463, 469 (2d Cir. 1981) ("It has long been the practice in [the Second Circuit] to deny compensation to counsel who fail to comply with the disclosure provisions [of the Bankruptcy laws]"); *In re Progress Lektro Shave Corp.,* 117 F.2d 602 (2d Cir. 1941); *In re Eureka Upholstering Co.,* 48 F.2d 95 (2d Cir. 1931).

In *In re Piecuil*, 145 B.R. 777 (Bankr. W.D.N.Y. 1992), the bankruptcy court reviewed the Second Circuit cases commonly cited for this so-called 'per se' rule and determined that "the harshness of the rule has been exaggerated. *Piecuil*, 145 B.R. at 778-79. The bankruptcy court gleaned that "[c]common, then, to all key decisions of the Second Circuit are the facts that they involved applications by attorneys (as opposed to accountants, auctioneers, appraisers, or other professionals) who represented or were affiliated with other interests in the case apart from representation of the estate" and that

> [i]n no instance that can be found has the Circuit adopted a rigid view of the prior approval requirement in connection with any professional whose only involvement in the case, as attorney or otherwise, was to perform services for the estate which the professional thought would be compensable from the estate and as to which the professional could look to no-one but the estate (for compensation)

***5** *Id.* at 781. Similarly, he found that "most courts that have recited a need for strict adherence to the requirement of prior court approval have typically done so only in dictum or in a context in which either (1) they would have denied approval of the employment had application been made prior to the rendering of services, or (2) the applicant consciously avoided the requirement of prior approval." *Id.* at 779.

This Court similarly finds that the reports of the holdings in the line of Second Circuit cases, including *Futuronics, Lektro,* and *Eureka*, have been misinterpreted to mean that a professional's services rendered pre-court approval are not compensable. For example, *Futuronics* involved the denial of a law firm's application for compensation for services as general counsel, where the firm "exhibited a total and callous disregard for the disclosure provisions of [former Bankruptcy Rule] 215." *Futuronics*, 655 F.2d at 469. The Circuit held that "the violation of the bankruptcy rules' prohibition against illicit fee-sharing involved in this case warranted no less than a total denial of compensation." *Id.* at 470. In *Lektro,* the debtor's attorney sought compensation for rendering services that were "of a character to be rendered by an attorney for the trustee" even though the attorney had not been appointed to serve in such a capacity. *Lektro,* 117 F.2d at 603-04. In addition to failing to obtain a court appointment, the attorney would not have been eligible for appointment because he was not "disinterested." *Id.* at 604.

In *Eureka*, a receiver, later appointed as trustee, availed himself of creditors' attorney's services without applying to the court for the appointment of an attorney. *Eureka*, 48 F.2d at 95. The Circuit affirmed an award of $100 for the "routine" filing of the involuntary petition and denied compensation for other requested services, including arranging the sale of assets, hiring truckmen, and safeguarding property, among other similar services, as they were duties of the trustee, not legal services. *Id.* at 95-96. The Circuit found that further recovery was precluded because the firm either acted on an unauthorized retainer in violation of court procedures or usurped the duties of a receiver without a court order displacing the receiver's duties. *Id.* As noted in *Piecuil*, in these cases, "the policy of preventing the estate's incurring of expense for unnecessary legal services would have required disapproval of the application had prior approval been sought." *Piecuil*, 145 B.R. at 779.

Accordingly, this Court finds that there is no *per se* prohibition, in the statute or precedential caselaw, against awarding reasonable compensation to an estate professional

for actual and necessary services rendered to the estate prior to the date of court approval of retention. As a result, in this Court's view, *nunc pro tunc* or retroactive retention is not necessary.

D. Late-filed Motions to Retain Are Subject to Heightened Standard of Review

Although a professional does not violate the Code or Rules by commencing services prior to court approval, late applicants should understand the consequences of their delay. Section 327(a) requires that a professional employed by a trustee "(1) hold no interest adverse to the estate" and "(2) "be a disinterested person[ ]." *Pryor v. Pontisakos (In re Vouzianas),* 259 F.3d 103, 107 (2d Cir. 2001); *see also* 11 U.S.C. § 101(14) (defining "disinterested person"), and 11 U.S.C. § 101(41) (defining "person"). "When evaluating proposed retention, a bankruptcy court should exercise its discretionary powers over the approval of professionals in a manner which takes into account the particular facts and circumstances surrounding each case and the proposed retention before making a decision." *Vouzianas,* 259 F.3d at 107 (internal quotations and citations omitted). A court should consider "the protection of the interests of the bankruptcy estate and its creditors, and the efficient, expeditious, and economical resolution of the bankruptcy proceeding." *Id.* (internal quotations and citations omitted).

***6** The longer an estate professional waits to seek court approval of its retention, the more the "particular facts and circumstances surrounding [the] case" develop, which means the Court may broaden its analysis to include hindsight consideration of the services already rendered and the professionals who rendered those services. *Id.* Seeking court approval after-the-fact subjects the professional to the possibility that approval of retention may be denied considering the lack of benefit to the estate thus precluding any possibility of compensation under section 330. Where services rendered ultimately provide little or no benefit to the estate, court approval obtained *prior to* the rendering of the services would at least allow the professional to seek compensation and prove the compensation was reasonable and necessary in light of the facts and circumstances of the case.

E. The Trustee's Motion to Retain WGP

The Trustee's delay of nearly a full year in filing the Motion to Retain permits this Court to review the work already performed and determine whether the retention of WGP should be approved considering the facts of this case. In this case thus far the Trustee and/or WGP have filed a motion to compel, a notice of discovery of assets, drafted and mailed two one-page letters, and examined the Debtor at a section 341 meeting. With the exception of the Motion to Compel, these tasks are inherent to the Trustee's duties in a bankruptcy of "collect[ing] and reduc[ing] to money the property of the estate" and "investigat[ing] the financial affairs of the debtor." 11 U.S.C. § 704.

Without more information, the Court cannot evaluate whether it was necessary to retain legal counsel, whether the delay in seeking retention of legal counsel was reasonable and whether, in retrospect, retention of legal counsel provided any net benefit to the estate. Based on the limited information contained in the Motion to Retain, and given the "particular facts and circumstances surrounding [the] case and the proposed retention," *Vouzianas,* 259 F.3d at 107, the Court finds there is no basis to retain WGP at this time.

Conclusion

For all these reasons, the Motion to Retain is denied without prejudice. An Order consistent with this Decision will be entered forthwith.

All Citations

Slip Copy, 2020 WL 1272258, 68 Bankr.Ct.Dec. 140

Footnotes

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1 The Motion to Retain does not actually contain a request for *nunc pro tunc* relief, but the Court presumes this was the Trustee's intention because the proposed order attached to the Motion to Retain contains such relief. Motion to Retain, ECF No. 18-3.

2 For example, the undersigned judge requires motions to approve retention of professionals to be brought before the court by notice of motion and upon a hearing.

3 *Cf. Cushman & Wakefield of Conn., Inc. v. Keren Ltd. P'ship (In re Keren Ltd. P'ship),* 189 F.3d 86, 88 (2d Cir. 1999) (affirming a denial of *nunc pro tunc* retention of professionals "for substantially the reasons stated by the district court"). The district court stated that § 327(a) "anticipates that professionals who contemplate rendering service to estates first demonstrate relevant qualifications including competence, disinterest, efficiency, and document the need for service." *Cushman & Wakefield of Conn., Inc. v. Keren Ltd. P'ship (In re Keren Ltd. P'ship)*, 225 B.R. 303, 306 (S.D.N.Y. 1998). To "anticipate" does not mean the same thing as to "require."

4 Additionally, pursuant to section 328, "... the court may deny allowance of compensation for services and reimbursement of expenses of a professional employed under section 327 or 1103 of this title if ... such person is not a disinterested person, or represents or holds an interest adverse to the interest of the estate with respect to the matter on which such professional person is employed." 11 U.S.C. § 328(c).

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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NEW YORK
----------X
In re:

Cherie Ann Hlady *dba* Hlady Law Firm, PC,

Debtor.

Chapter 7

Case No.: 8-16-74011-las

----------X
Cherie Ann Hlady,

Plaintiff,

against

Key Bank N.A., American Education Services, Citibank, N.A., Citibank Student Loan Company, and New York State Higher Education Services, Corp.,

Defendants.

Adv. Pro. No.: 8-16-08181-las

----------X

MEMORANDUM DECISION AFTER TRIAL

Plaintiff Cherie Ann Hlady commenced this adversary proceeding seeking the discharge of her student loan debt to Educational Credit Management Corporation ("ECMC")[1] under 11 U.S.C. § 523(a)(8)[2]. That section excepts student loan debt from discharge "unless excepting such debt from discharge . . . would impose an undue hardship on the debtor and the debtor's dependents." 11 U.S.C. § 523(a)(8). Plaintiff argues that repayment of the loan, i.e., excepting the debt from discharge, will impose an undue hardship on her. Specifically, plaintiff asserts that she satisfies the three-prong test set forth by the Second Circuit Court of Appeals in *Brunner v. N.Y. Higher Educ. Servs. Corp.*, 831 F.2d 395

[1] ECMC, a federal student loan guarantor in the Federal Family Education Loan Program, holds an interest in one (1) consolidation loan owed by plaintiff. Defendant New York State Higher Education Services Corporation assigns to ECMC for defense its student loan accounts that are in bankruptcy. *See* Answer filed by ECMC, n.1 [dkt. no. 9].

[2] All statutory references to sections of the United States Bankruptcy Code, 11 U.S.C. § 101 *et seq.*, will hereinafter be referred to as "§ (section number)".

(2d Cir. 1987) for determining the existence of "undue hardship", thus establishing that the student loan debt at issue is dischargeable. In brief, under the three-prong *Brunner* test, a claim of "undue hardship" turns on the following questions (i) whether a debtor, based on her current finances, can repay her student loan obligation and still maintain a minimal standard of living, (ii) if she does not have the present ability to repay her student loan obligation and, at the same time, maintain a minimal standard of living, whether that inability will persist for a significant portion of the repayment period, and (iii) whether the debtor has made a good faith effort to repay her student loan obligation. Additionally, under existing Second Circuit precedent, a debtor bears the burden of proving each element of the *Brunner* test by a preponderance of the evidence.

For its part, ECMC contends that plaintiff falls short of satisfying each prong of the *Brunner* test. In its view, plaintiff has not made any effort to maximize her income nor has she taken any steps to minimize her current expenses. Additionally, ECMC maintains that plaintiff is eligible for any of three income-based repayment programs under which her monthly payment would be $0 for a period of 25 years based upon her most recent federal income tax return. Plaintiff does not contest the amount she would be required to pay under the income-based repayment programs, nor does she challenge the nature of the debt owed to ECMC as an educational loan under § 523(a)(8)(A)(i), or the amount owed as of the time of trial.

The Court has subject matter jurisdiction under 28 U.S.C. § 1334 and the Standing Order of Reference entered by the United States District Court for the Eastern District of New York pursuant to 28 U.S.C. § 157(a), dated August 28, 1986, as amended by Order dated December 5, 2012. A proceeding to determine the dischargeability of debt is a core proceeding that the Court may hear and decide. 28 U.S.C. § 157(b)(1) and (b)(2)(I).

Having considered the parties pre and post-trial submissions and the evidence presented at trial, the Court makes the following findings of fact and conclusions of law pursuant to Rule 52(a) of the Federal Rules of Civil Procedure, as made applicable here by Bankruptcy Rule 7052. To the extent a finding of fact includes a conclusion of law, it is deemed a conclusion of law, and vice versa. For the reasons set forth below, the Court finds that plaintiff has failed to carry her burden of establishing that repayment of her student loan debt to ECMC would constitute an undue hardship under § 523(a)(8). Accordingly, the Court enters judgment for ECMC.

PROCEDURAL BACKGOUND

Plaintiff filed for chapter 7 relief on August 31, 2016 and thereafter commenced this adversary proceeding seeking a determination of the dischargeability of her student loan. [dkt. no. 1]. ECMC filed an answer to the complaint. [dkt. no. 9]. In its answer, ECMC stated that it is the proper party in interest in the adversary proceeding and that it would seek to intervene. *See* Answer, n.1 [dkt. no. 9]. That statement is consistent with ECMC's letter [dkt. no. 10] filed pursuant to this Court's Pretrial Conference Order [dkt. no. 4]. ECMC did not move to intervene in the adversary proceeding pursuant to Rule 24 of the Federal Rules of Civil Procedure, made applicable here by Bankruptcy Rule 7024. However, plaintiff has not contested ECMC's standing as the proper party defendant in this adversary proceeding. The parties filed a joint status letter [dkt. no. 14], conducted extensive fact discovery, filed a joint pretrial memorandum [dkt. no. 21] and participated in a two-day trial before the Court, all without a challenge by plaintiff to ECMC's assertion that it is the proper party defendant.

In anticipation of trial, the Court entered a Pre-Trial Order setting forth the deadline for submission of witness lists, a joint exhibit book, and any stipulations or agreed statement of facts or law to which all parties consent. [dkt. no. 18]. In accordance with the Pre-Trial

Order, the parties timely submitted a joint pretrial memorandum which listed plaintiff as the only trial witness, listed the exhibits to be offered by each party on its respective case-in-chief, and set forth the parties' stipulated facts and agreed statements of law. [dkt. no. 21]. The Court conducted a two-day trial at which only plaintiff testified. Following the trial, at the direction of the Court, the parties submitted proposed findings of fact and conclusions of law. [dkt. nos. 30, 35].

FINDINGS OF FACT

The following findings of fact are based on the trial record, which include the trial testimony, exhibits entered into evidence, and the parties' stipulation of certain facts.[3]

A. Stipulated Facts

Plaintiff is an individual residing at 7 Dorothy Street, Hicksville, NY. [JPM ¶ 4.] Plaintiff is 48 years old. [JPM ¶ 5.] Plaintiff is married and has no dependents. [JPM ¶ 6.]

ECMC is a not-for profit corporation duly organized under the laws of the State of Minnesota, with offices located at 111 South Washington Avenue, Suite 1400, Minneapolis, Minnesota 55401. [JPM ¶ 1]. ECMC, a federal student loan guarantor in the Federal Family Education Loan Program ("FFELP"), holds an interest in one unpaid student loan pertaining to plaintiff (the "ECMC Loan"). [JPM ¶ 2]. As of January 23, 2017, the outstanding balance of the ECMC Loan, including principal, interest, fees and costs, was approximately $140,772.91. [JPM ¶ 3]. The ECMC Loan accrues interest at a rate of 6.88% per annum, or $19.69 *per diem*. [JPM ¶ 3].

Plaintiff obtained the ECMC Loan for the purpose of financing her pursuit of a Juris Doctorate degree from Hofstra University, which she obtained in 2006. [JPM ¶ 7]. In addition

[3] The parties stipulated to certain facts in their Joint Pre-Trial Memorandum [dkt. no. 21]. For convenience, the Court will refer to the stipulated facts as "JPM ¶ __". Additionally, "Tr." refers to the transcript of the trial in this matter which appears at dkt. nos. 26 (October 2) and 27 (November 15), and "Ex." refers to the trial exhibits (*see* JPM, Part IV. Trial Exhibits).

to her Juris Doctorate degree, plaintiff also holds a bachelor's degree in Speech from St. John's University. [JPM ¶ 8]. Plaintiff is licensed to practice law in the State of New York [JPM ¶ 9], has worked as an attorney and legal assistant since 2006 [JPM ¶ 10], and is a Notary in the State of New York [JPM ¶ 11]. Plaintiff maintains her own law practice, Hlady Law Firm, PC, where she handles all legal and administrative tasks, and her law practice includes real estate and estate planning. [JPM ¶ 12]. Plaintiff is able to drive. [JPM ¶ 13].

Plaintiff is eligible to enter the William D. Ford Direct Loan Consolidation Program (the "Ford Program") or avail herself of options under the FFELP in order to achieve greater flexibility in repaying the ECMC Loan. [JPM ¶ 14]. If plaintiff entered into the Ford Program, her monthly payment under the Income Based Repayment Program option would be $0, based on her reported household adjusted gross income ("AGI") of $321, as reported in plaintiff's 2016 federal income tax return. [JPM ¶ 15]. If plaintiff entered into the Ford Program, her monthly payment under the Income Contingent Repayment Plan option would be $0 for a period of 25 years, based on her reported AGI of $321, as reported in plaintiff's 2016 federal income tax return. [JPM ¶ 16]. If plaintiff entered the Revised Pay As You Earn Plan, her monthly payment would be $0 for a period of 25 years, based on her reported AGI of $321, as reported in plaintiff's 2016 federal income tax return. [JPM ¶ 17]. Under any of her income-driven repayment options, plaintiff would be required to submit documentation regarding her income every year of the duration of the loan in order to remain in that option. [JPM ¶ 18]. ECMC has apprised plaintiff of her various loan repayment options. To date, plaintiff has declined to accept any of those options. [JPM ¶ 19].

Plaintiff's monthly expenses include cellular phone service for two separate phone numbers, at a cost ranging from $131.07 to $160.43 per month. [JPM ¶ 20]. Plaintiff's monthly expenses also include bundled cable television, telephone, and internet at a cost of $223.07 per month. [JPM ¶ 20].

B. Trial Testimony

Upon graduation from law school in 2006, plaintiff owed approximately $40,000 on her student loans. [10/2 Tr.7:13-14] [dkt. no. 26]. At the time of trial, plaintiff's student loan debt exceeded $130,000. [*Id.* 7:15-17].[4] After graduating from law school, plaintiff worked for the law firm of Fratello & Fox PC in Woodbury, New York as a legal assistant earning $25 an hour. [*Id.* 8:2-7]. After plaintiff passed the bar exam, the firm continued to pay her $25 an hour but did increase plaintiff's responsibilities. [*Id.* 8:9-11]. Plaintiff testified that she would be laid off by the firm whenever the workload for the attorney she worked for was slow or if the attorney's daughters were home from school as they would handle nonlegal aspects of plaintiff's job while the attorney would do all the legal work. [*Id.* 9:1-8].

Plaintiff stopped working for the firm after she was injured in an automobile accident in early June of 2011. [*Id.* 9:13-21]. Plaintiff testified that she used a headhunter, sent out hundreds of resumes and went on a few job interviews. [*Id.* 9:17-19]. Plaintiff did not testify as to the places she sent her resumes, the firms with whom she interviewed, and the time frame of her job search. Nor is there any documentary evidence in the trial record showing the extent of plaintiff's job search.

Plaintiff testified that she used to wait tables and bartend, but she can no longer stay on her feet for an extended period. [*Id.* 19:13-14]. While plaintiff testified that she has chronic issues and thus cannot supplement her income, she did not explain the nature of any chronic issue nor did she offer any documentary evidence to corroborate this claim. [*Id.* 19:14-15]. Plaintiff did, however, testify that "lawyering" is okay. [*Id.* 19:15]. She testified that while she can't sit for an extended period, if she can stand up, she's okay. [*Id.* 19:15-16]. There is

[4] In her Amended Schedule E/F (Creditors Who Have Unsecured Claims), plaintiff listed a debt to the New York State Higher Education Corporation in the amount of $130,305. *See* dkt. no. 13 in the underlying bankruptcy case, *In re Hilady*, Case No. 16-74011. References to docket entries in the main bankruptcy case will be noted as "Bankr. dkt. no. __".

nothing in the record, no testimony or documentary evidence, to support her claim that she is unable to stand or sit for an extended period because of any medical condition. Additionally, plaintiff did not explicitly ask that her unspecified chronic issues be taken into consideration in determining whether her student loan debt should be discharged. As noted above, plaintiff testified that she can practice law [*Id.* 19:15] and, as noted below, plaintiff testified that she shovels snow [*Id.* 26:3-6].

At the end of October 2011, plaintiff decided to start her own law practice. [*Id.* 11:1-2]. In her private practice, she does wills, trusts and estates, and real estate closings. [*Id.* 11: 5-9]. She has not actively pursued legal work and gets business by word of mouth. [*Id.* 19:21-22]. Plaintiff testified that she doesn't have money for a law firm website or advertising. [*Id.* 19:20-21]. She testified that she has not sought employment as a per diem contract attorney as she prefers to either have her own law practice or work for a law firm as a W-2 employee. [*Id.* 64:19-21]. As to the latter, plaintiff did not offer any evidence that she sought alternative employment at a law firm after starting her own practice.

According to plaintiff's 2011 Federal income tax return, she earned $9,658 in gross revenues from her legal practice and, after business expenses, her net business income was $6,188. [Ex. I]. Plaintiff incorporated her legal practice in 2012. [10/2 Tr. 10:23-24.] According to plaintiff's 2012 Federal income tax return, her 2012 gross revenue from her law practice, Hlady Law Firm PC, was $8,867. [*Id.* 33:23-25, 34:4-8; Ex. H]. Her net profit for that year was $5,894. [Ex. H]. Plaintiff reported gross revenue of $1,075 in her 2013 Federal income tax return [*Id.* 33:14-17; Ex. G], and a net profit of $559. [Ex. G]. In her 2014 Federal income tax return, plaintiff reported gross revenue of $34,231 and a net profit of $17,691. [Ex. F]. In her 2015 Federal income tax return, plaintiff reported gross revenue of $29,431 and a net profit of $12,784. [Ex. E]. In her 2016 Federal income tax return, plaintiff reported gross

revenue of $14,152 and a net profit of $321. [Ex. D]. Plaintiff testified that she grossed approximately $1,000 to $1,200 a month in 2017. [10/2 Tr. 15:18].

Plaintiff operates her legal practice from her home. [*Id.* 15:25, 16:1]. She does not own the home, rather the home is owned by plaintiff's mother, Priscilla Hlady, and was inherited by her mother from plaintiff's grandparents. [*Id.* 18:9-10]. Plaintiff's mother used to rent out the house, but plaintiff moved into the house in the summer of 2005 during her third year in law school. [*Id.* 18:8-11]. Plaintiff's parents live a block and a half away. [*Id.* 25:13]. While plaintiff does not pay rent to her mother, she testified that she pays the real estate taxes on the house directly to the town. [*Id.* 24:15-21]. Plaintiff testified that the school taxes are about $22,070 and general taxes are about $1,809 a year. [*Id.* 16:1-2]. That would average about $2,000 a month. However, plaintiff testified that her payment of the real estate taxes results in a "rental" cost of $700 a month. [*Id.* 16:5-6]. Plaintiff did not offer any explanation for the inconsistency in her testimony and did not proffer any documents in support of her living arrangement, nor is there any documentary evidence in the trial record corroborating her payment of the real estate taxes and the amount of the payment. Plaintiff testified that her mother pays for landscaping for the property, but plaintiff does the snow removal on her own by taking out the shovel. [*Id.* 26:3-6]. Plaintiff stated that she pays for utilities and any repairs to the house. [*Id.* 25:18-21]. Her heating bill averages about $200 a month. [*Id.* 16:21-23].

Plaintiff testified that on a monthly basis, she spends about $100 to $150 on food, $25 for housekeeping, $25 on clothing, $25-$40 on personal care such as haircuts, $50-60 for out-of-pocket medical and dental expenses, and $40-$80 for transportation expenses, including car payments, maintenance and gas. [*Id.* 16:24-25; 17:1-21]. Plaintiff also testified that she pays $200 a month for bundled internet, a telephone landline which serves as her office

number, and cable television from Optimum. [*Id.* 16:13-15]. She has not sought to reduce her monthly cable television cost by getting fewer channels. [*Id.* 67:17-20]. If plaintiff removed some of the channels, she would save about $18 a month. [*Id.* 68:1-2]. If plaintiff eliminated her cable television cost and kept just internet and a telephone landline, she would save $30 or $45 a month. [11/15 Tr. 28:7-9, 38:13-15] [dkt. no. 27]. Plaintiff viewed these potential savings as nominal and has not sought to change her subscription with Optimum. [*Id.* 28:1-3].

Plaintiff married in 2014. [10/2 Tr. 19:1-2]. Plaintiff's husband has been living in Colorado since February 1, 2016. [*Id.* 19:23-24]. Her husband does not contribute to plaintiff's household expenses. [*Id.* 19:5-6]. Plaintiff testified that she pays for her husband's car insurance because she has medical coverage under his health plan. [*Id.* 23:15-16; 42:16-17]. No evidence was proffered as to the cost of that medical coverage. In addition to paying for her husband's car insurance, plaintiff has her own car insurance payment of $200 a month. [*Id.* 17:24-15]. Plaintiff also pays for her husband's cellphone plan, again stating that is so because she is covered under his health plan. [*Id.* 42:8-9; 42:21-22]. A review of plaintiff's tax returns shows that in years where plaintiff had enough gross income, she would offset some of her cellphone and on-line computer expenses against her gross revenue as reported on her Federal income tax returns. [Exs. E, F, and H].

Plaintiff maintains a joint checking account and a joint savings account with her mother at TD Bank. [10/2 Tr. 35:17-6, Ex. J; 11/15 Tr. 4:15-21, Ex. K]. She stated that, almost exclusively, the expenses that are listed in the bank statements comprise of her living expenses. [10/2 Tr. 39:8-10]. On cross-examination, plaintiff testified that these expenses include the following. On June 23, 2016, she purchased an Apple watch for $432.33. [*Id.* 78:1-4]. On October 15, 2015, plaintiff purchased a Kate Spade purse for $214 [130:9-12], and on

August 15, 2014, she purchased Kate Spade shoes for $156.42 [*Id.* 135:7-10]. There are also numerous expenses in excess of $100[5] for which plaintiff had no express recollection: (1) $208 debit incurred on May 18, 2016 for Mislanier2 [*Id.* 81:3-5]; (2) $303.00 withdrawn in Denver, Colorado on January 19, 2016, (3) $201.75 withdrawn in Scottsbluff, Nebraska on January 11, 2016 [*Id.* 97:15-21]; (4) $152.36 incurred on Amazon on March 31, 2016 [*Id.* 87:12-15]; (5) $142.62 incurred at Barnes and Noble on December 10, 2015 [*Id.* 103:10-13]; (6) $117.62 debit paid to Honeygirl67 on October 2, 2015 [*Id.* 109:24-25, 110:1]; (7) $635 debit made on January 29, 2015 [*Id.* 122:2-5], (8) $392.15 incurred on January 2, 2015 for wwwfanxchange.com [*Id.* 123:6-8], (9) $207 incurred on November 24, 2014 for RST Restaurant.com [*Id.* 124:9-12], (10) $146 spent on tickets at Nassau Heritage on November 7, 2014 [Id. 127:7-10]; (11) approximately $150 of on-line purchases incurred from October 20 to 21, 2014 at various vendors; (12) $100 paid to Candiebolto on August 18, 2014 [*Id.* 131:9-12], and $120 on August 29, 2014 [*Id.* 131:21-24]; (13) $262 paid to KHarper2003 on July 28, 2014 [*Id.* 133:17-20]; and (14) $146 spent on tickets at Nassau Heritage on April 10, 2014 [*Id.* 138:3-8].

Plaintiff has traveled to Montreal, Canada to attend conferences sponsored by the American Bar Association on international law, an area of law in which she hopes to practice, and to fulfill continuing legal education requirements. [*Id.* 52:6-15, 59:3]. For the conference she attended on October 27, 2015, plaintiff stayed at the Fairmont Hotel in Montreal at a cost of $1,115.77. [*Id.* 104:20-24]. Despite her purported interest in international law, there is nothing in the record evidencing any effort by plaintiff to find employment in this practice area.

[5] While the record made at trial and plaintiff's bank statements show numerous expenses under $100, the Court has listed certain expenditures in excess of $100 as brought out on cross-examination.

In September of 2014, plaintiff flew to Denver, Colorado to attend a wedding for a family friend and stayed at The Ritz Carlton where she incurred hotel costs of about $600. [*Id.* 132:8-24]. Plaintiff testified that she has purchased birthday, Christmas and Valentine's Day gifts for her husband, such as comedy show tickets, and diecast for model cars, which total $100 or more for each occasion. [*Id.* 83:1-25, 103:14-17, 120:16-21, 121:11-17, 136:11-16].

On April 7, 2017, plaintiff made a wire transfer of $5,000 to her husband. [*Id.* 55:6-11]. This amount consisted of $1,000 of plaintiff's own funds and $4,000 she borrowed from neighbors, friends and a cousin. [*Id.* 55:15-22]. Plaintiff did not proffer any evidence as to the terms by which she borrowed these funds. According to plaintiff, the funds she gave to her husband were earmarked towards the purchase of a house in Colorado in her husband's name only. [*Id.* 56:11-23]. When the earnest money for the purchase of the house was released, plaintiff's husband used the released funds to pay back his uncle for monies borrowed and to pay off his own student loans. [*Id.* 57:11-21]. Plaintiff's husband made it clear that he was not repaying the $5,000 borrowed from plaintiff [*Id.* 58:20-23]. However, plaintiff told her husband that he needed to give her a $1,000 check that he received from a third party to pay her back the $1,000 that she had given him, which he did. [11/15 Tr. 13:1-7]. Plaintiff had to repay the $4,000 she borrowed from others out of her own earnings or by providing a credit towards future legal services. [10/2 Tr. 58:4-19]. Plaintiff did not proffer any documentary evidence of how much of the purported $4,000 loan she has paid back or what legal services she performed in lieu of having to pay back the borrowed funds.

At the time of trial, plaintiff's mother was 69 years old [*Id.* 36:22-23], and plaintiff's father was 79 years old [11/15 Tr. 32:20]. Plaintiff testified that her mother does not have the use of a credit card. [*Id.* 20:16-17]. She also testified that her mother does not have a computer and relies upon plaintiff to make on-line purchases with plaintiff's debit or credit card, such

as Christmas and birthday gifts for plaintiff's nieces [10/2 Tr. 38: 12-15], and airline tickets for vacation [*Id.* 30:1-3]. Plaintiff's parents have treated plaintiff to a vacation to Disney World in Florida every November for the past 9 years. In 2015, 2016 and 2017, plaintiff and her parents went twice each year to Disney World, once in March and again in November. [*Id.* 89:13-14; 117:8-24]. Plaintiff testified that she would purchase in advance the park tickets and meal plans. [*Id.* 94:7-18; 101:8-11; 117:21-23]. She stated that her parents asked her to make these purchases because she could get a military discount. [*Id.* 117:11-13]. Plaintiff further testified that her parents always reimbursed her in cash for these purchases without fail. [*Id.* 118:15-17]. Usually, plaintiff would hold the cash to pay her living expenses or a prospective bill instead of depositing the funds into her checking account. [*Id.* 118:18-25]. There is no writing or ledger to reflect or memorialize plaintiff's receipt and retention of cash from her parents. [11/15 Tr. 20:8-11].

Plaintiff's husband also asked her to make on-line purchases for him and he would pay her back for these costs. [*Id.* 82:13-25]. Plaintiff testified that some of the funds paid back by her husband were in the form of cash, which plaintiff kept on hand or deposited to her checking account, or payments made using PayPal. [*Id.* 86:22-25, 88:2-3, 92:17-25, 93:1-4, 95: 18-22]. Notwithstanding plaintiff's practice of not depositing cash she received from her husband and parents as reimbursement of expenses incurred on their behalf into her bank account, none of plaintiff's monthly bank statements admitted into evidence for the period January 2013 through June 1, 2017 show a negative balance. [Ex. J].

Plaintiff applied for deferments when her student loans first became due. [10/2 Tr. 11:17-18; 12:4]. Plaintiff testified that she made her first loan repayment in 2009. [11/15 Tr. 45:22-24]. Plaintiff believes she repaid approximately $5,000 on account of the ECMC Loan. [*Id.* 45:17-19]. Plaintiff admitted that she never made regular monthly payments on her

student loan obligation. [*Id.* 49:14-15]. Plaintiff stated that if she did have extra funds on hand, she would send it to ECMC. [*Id.* 41:24-25]. She found one check in her check register where she sent ECMC $500. [*Id.* 48:3-5]. Other than the check register, she does not have or maintain any other check register that reflects or evidences payments she made on account of the ECMC Loan. [*Id.* 48:24-25, 49:1-3]. Plaintiff calculated that she made loan repayments of about $5,000 based upon what interest deductions she claimed for her student loans on her tax returns in a given tax year figuring that she was only paying interest. [*Id.* 48:5-7, 12-19]. Other than her testimony as to claimed interest deductions on her tax returns, plaintiff did not conduct any independent verification to determine the amount of student loan debt she repaid. [*Id.* 48:20-23]. The record is devoid of any evidence as to when plaintiff made any student loan payments or the actual amount of any such payments.

At first, plaintiff testified that she stopped applying for student loan deferments in 2010 and 2011, [10/2 Tr. 12:6-7], and that she has not made any payments since the beginning of 2011. [11/15 Tr. 46:22-25]. Later, she testified that she deferred payment of her student loans in 2006 but didn't think she deferred payment of her student loans in 2007 or 2008. [*Id.* 49:23-24]. Plaintiff stated that she just didn't pay anything during that time [*Id.* 49:24], and her best guess is that she received the first default letter in 2008 or 2009 [*Id.* 49:24-25, 50:1-2]. She testified that she received further default notices after that, but for a long period of time she didn't open the mail from ECMC. [*Id.* 50:3-6].

Plaintiff declined each of the income-based repayment options offered by ECMC even though her monthly payment would be $0 for a period of 25 years based upon her adjusted gross income as reported in her most recent Federal income tax return. [*Id.* 31:2]. Plaintiff testified that she was going to be 49 years old and 25 years of reporting as required under the income-based repayment programs would make her 75 years old when she was done. [*Id.*

31:2-5]. Plaintiff stated that she just wants her student loan debt to be over. [*Id.* 31:15]. She doesn't see any change on the horizon and doesn't see what is going to be different in 10 years that hasn't been the same for the last 10 years. [*Id.* 31:15-17].

DISCUSSION

As noted above, plaintiff seeks to discharge her student loan debt, i.e., the ECMC Loan, pursuant to § 523(a)(8) on the basis that repayment "will impose an undue hardship" on her. Plaintiff claims that she has satisfied each prong of the three-prong test established by the Second Circuit in *Brunner* to determine the existence of undue hardship and her student loan debt must, therefore, be discharged.[6] The Court disagrees. As set forth below, the Court concludes that plaintiff has failed to carry her burden of proof to present evidence in support of her claim that repayment of her student loan debt will impose an undue hardship on her and to prove that claim by a preponderance of evidence.

A. The Legal Framework Governing Undue Hardship: The *Brunner* Test

"Student loans are presumptively nondischargeable in bankruptcy." *Easterling v. Collecto, Inc.*, 692 F.3d 229, 231 (2d Cir. 2012). However, § 523(a)(8), provides for the discharge of student loan debt if "excepting such debt from discharge . . . would impose an undue hardship on the debtor and the debtor's dependents." 11 U.S.C. § 523(a)(8). "Because any debtor in bankruptcy usually has significant financial problems, a finding of undue hardship will not be based simply on the debtor's difficulty in making payments." *Williams v. N.Y. State Higher Educ. Servs. Corp. (In re Williams)*, 296 B.R. 298, 302 (S.D.N.Y. 2003), *aff'd*, 84 F. App'x 158 (2d Cir. 2004). "A debtor carries a heavy burden when she seeks to establish an undue hardship under [S]ection 523(a)(8)." *Id.* "[Section] 523(a)(8) exhibits a

[6] In their joint pretrial memorandum, the parties agreed that plaintiff's claim that her student loan debt to ECMC is dischargeable turns on the question of whether repayment of the loan "would impose an undue hardship" on her, and that the three-prong *Brunner* test is the applicable standard for determining the existence of undue hardship. *See* JPM Part II, ¶ 1.

'clear congressional intent . . . to make the discharge of student loans more difficult than that of other nonexcepted debt . . . .'" *Traversa v. Educ. Credit Mgmt. Corp. (In re Traversa)*, 444 F. App'x 472, 474 (2d Cir. 2011) (summary order), *cert. denied*, 568 U.S. 817 (2012) (quoting *Brunner*, 831 F.2d at 396).

While the term "undue hardship" is not defined in the Bankruptcy Code, the Second Circuit in *Brunner* established a three-prong test for determining the existence of "undue hardship". Under the *Brunner* test, to succeed in excepting student loan debt from discharge, a debtor must show: (1) that the debtor cannot maintain, based on current income and expenses, a "minimal" standard of living for the debtor and the debtor's dependents if forced to repay the loans; (2) that additional circumstances exist indicating that this current state of affairs is likely to persist for a significant portion of the repayment period; and (3) that the debtor has made good faith efforts to repay the loans. *Brunner*, 831 F.2d at 396. A debtor must prove each prong of the *Brunner* test by a preponderance of the evidence.[7] *Traversa*, 444 F. App'x at 474 (citing *Grogan v. Garner*, 498 U.S. 279, 291 (1991)).

"Courts consider multiple factors when determining whether the three-pronged *Brunner* test is satisfied, including the debtor's gross income, age, health, dependents, and marital status." *Williams*, 296 B.R. at 302. If the debtor fails to satisfy any one of the three prongs of the *Brunner* test, "the bankruptcy court's inquiry must end there, with a finding of no dischargeability." *Id.* (citing *Pa. Higher Educ. Assistance Agency v. Faish* (*In re Faish)*, 72

[7] "The burden of showing something by a preponderance of the evidence . . . simply requires the trier of fact to believe that the existence of a fact is more probable than its nonexistence . . . ." *Metro. Stevedore Co. v. Rambo*, 521 U.S. 121, 137, n.9 (1997) (quoting *Concrete Pipe and Prods. of Cal., Inc. v Constr. Laborers Pension Trust for S. Cal.*, 508 U.S. 602, 622 (1993). "As the finder of fact, the Court is entitled to make credibility findings of the witnesses and testimony." *Merck Eprova AG v. Gnosis S.P.A.*, 901 F. Supp. 2d 436, 448 (S.D.N.Y. 2012), *aff'd*, 760 F.3d 247 (2d Cir. 2014).

F.3d 298, 306 (3d Cir. 1995), *cert. denied*, 518 U.S. 1009 (1996)). *See also Tingling v. U.S. Dep't of Educ.*, 611 B.R. 710, 724 (E.D.N.Y. 2020).

Although application of the three-prong *Brunner* test has been called into question as being overly harsh and not in keeping with what the Second Circuit originally intended, *see, e.g.*, *Rosenberg v. N.Y. State Higher Educ. Servs. Corp. (In re Rosenberg)*, 610 B.R. 454, 459 (Bankr. S.D.N.Y. 2020), it nevertheless remains binding precedent that this Court must follow. Because the Court agrees with Chief Judge Morris that the *Brunner* test should be applied by the courts "as it was originally intended", *Id.*; *Clavell v. U.S. Dep't of Educ.* (*In re Clavell*), 611 B.R. 504 (Bankr. S.D.N.Y. 2020), the question therefore naturally arises: whether, it is consistent with *Brunner*, that a 48-yaer old debtor: (i) who is in good health, (ii) who has no dependents, (iii) who has a solid education - an undergraduate degree in Speech and a Law degree, (iv) who is gainfully employed in her own law practice, (v) who has not presented evidence indicating meager job prospects, (vi) who has not presented concrete evidence from which the Court can, with any degree of certainty, discern her current financial condition, (vii) who has not presented clear evidence of any concerted efforts to maximize her income and minimize her expenses, (viii) who wants to work for just 10 more years (to age 58), (ix) who stopped opening mail regarding her student loan obligation, and (x) who has plainly stated that she "wants her student loan debt to be over," has met her burden of establishing undue hardship so as to receive a discharge of her student loan obligation? Measured against the standard set forth in *Brunner*, the answer is no. While there are cases that warrant the discharge of student loan debt under *Brunner* "as it was originally intended", this is not one of them. The Second Circuit could not have intended that on the record placed before this Court, plaintiff is entitled to a discharge of her student loan debt

based on undue hardship. With this in mind, the Court now turns to a discussion of each prong of the *Brunner* test.

1. Minimal Standard of Living

Under the first prong of the *Brunner* test, a debtor must show that he or she cannot, based on current income and expenses, maintain a "minimal" standard of living if forced to repay student loan debt. "The first element requires a debtor to show that if the debtor, based on current finances, is required to make the monthly student loan payment, the debtor's standard of living will fall below a minimal level." *Thoms v. Educ. Credit Mgmt. Corp.* (*In re Thoms*), 257 B.R. 144, 148 (Bank. S.D.N.Y. 2001) (internal quotations and citations omitted). "To evaluate this element, the [C]ourt must review current income and expenses considering the particular circumstances of the case." *Id.* (citations omitted).

To meet this standard, a debtor need not "live a life of abject poverty, but it does require 'more than a showing of tight finances.'" *Johnson v. Sallie Mae Inc. (In re Johnson)*, 550 B.R. 874, 879 (Bankr. M.D. Ala. 2016) (quoting *McLaney v. Ky. Higher Educ. Assistance Auth. (In re McLaney)*, 375 B.R. 666, 674 (M.D. Ala. 2007)). *See also In re L.K.*, 351 B.R. 45, 53 (Bankr. E.D.N.Y. 2009); *Clavell,* 611 B.R. at 516 ("[A] 'minimal standard of living' does not require that the debtor live in poverty."); *Bene v. Educ. Credit Mgmt. Corp. (In re Bene),* 474 B.R. 56, 68-69 (Bankr. W.D.N.Y. 2012) ("Clearly the Second Circuit did not equate 'minimal standard of living' with 'poverty.' The Circuit unequivocally held that committing a debtor 'to a life of *poverty*' for an extended time into the 'ten-year loan repayment period' would constitute a hardship that is 'undue.'"); *Mosley v. General Revenue Corp. (In re Mosley)*, 330 B.R. 832, 841 (Bankr. N.D. Ga. 2005) (emphasis in original), *aff'd*, 494 F.3d 1320 (11th Cir. 2007); *Faish*, 72 F.3d at 306. Nevertheless, "[a] debtor must demonstrate financial circumstances that [go] beyond the 'garden-variety financial hardship' that most debtors experience." *Jean-Baptist v. Educ. Credit Mgmt. Corp. (In re Jean-Baptiste)*, 584 B.R. 574,

587 (Bankr. E.D.N.Y. 2018) (quoting *Wolph v. U.S. Dept. of Educ. (In re Wolph)*, 479 B.R. 725, 729 (Bankr. N.D. Ohio 2012)). *See also Pincus v. Graduate Loan Ctr. (In re Pincus)*, 280 B.R. 303, 317 (Bankr. S.D.N.Y. 2002). "While it is not the Court's role to impose, *ad hoc*, a certain standard of living on the debtor, or to author his budget, the Court is required to 'review the reasonableness of the Debtor's budget — particularly the allocation of projected expenses in relation to projected income as it determines his capabilities to pay the instant obligations without undue hardship.'" *Lozada v. Educ. Credit Mgmt. Corp.* (*In re Lozada*), 594 B.R. 212, 222 (Bankr. S.D.N.Y. 2018) (emphasis in original), *aff'd*, 604 B.R. 427 (S.D.N.Y. 2019) (quoting *Pincus*, 280 B.R. at 317).

When applying this prong of the *Brunner* test, courts focus on a debtor's household income and expenses to determine what expenses are necessary for the debtor to meet her basic needs, such as food, shelter, clothing, transportation and medical treatment for herself and any dependents before repaying student loan debt. *Pincus*, 280 B.R. at 318. Additionally, courts consider whether a debtor has sought to maximize her ability to earn adequate income to pay for expenses and student loans while minimizing certain discretionary expenses. *Id.* (finding the debtor failed to demonstrate an inability to maintain a minimal standard of living where the debtor lives a comfortable lifestyle that is above the debtor's means such as paying for gym membership when a free gym was available at work, eating out and paying for newspapers, and does not evince efforts to minimize certain discretionary expenses); *Burton v. Educ. Credit Mgmt. Corp. (In re Burton)*, 339 B.R. 856, 870-71 (Bankr. E.D. Vir. 2006) (finding that courts must look at the debtor's income and expenses to determine what is the minimally necessary amount to ensure that the debtor's needs, such as food, shelter, clothing, and medical treatment are met and then look to see whether the debtor has additional funds to make student loan repayments). A minimally necessary standard of living means living "within the strictures of a frugal budget in the foreseeable future." *Chance v.*

United States of America (In re Chance), 600 B.R. 51, 58 (Bankr. S.D. Ind. 2019) (quoting *In re Innes*, 283 B.R. 496, 504 (D. Kan. 2002)). Minimum standard of living does not mean mechanical adherence to the federal poverty guidelines, but the fact that a debtor's income falls below the poverty guidelines does provide strong support that the debtor's standard of living is minimal. *Johnson*, 550 B.R. at 880 n.4; *Mosley*, 330 B.R. at 841.

Where a debtor is eligible to enroll in an income-based repayment program, the debtor must demonstrate how she will be unable to make the limited payments required under the formula and still maintain a minimal standard of living. *Chance*, 600 B.R. at 58 (noting that a court can consider whether the debtor is able to make payments under an income-based repayment plan and still maintain a minimum standard of living); *Lewellen v. Access Group, Inc. (In re Lewellen),* Case No. 07-31666 TEC, Adv. Proc. No. 08-3119 TC, 2010 WL 4975903, at *1 (Bankr. N.D. Cal. Dec. 1, 2010).

Based on the trial record, the Court cannot find that plaintiff presented evidence that she cannot, based on her current income and expenses, maintain both a "minimal" standard of living and repay her student loan debt. A review of plaintiff's Schedule I to her bankruptcy petition shows gross wage income of $1,205, as opposed to net income from an operating a business. [Bankr. dkt. no. 1]. Her Schedule J shows $2,220 of expenses, including monies for rent, utilities, a security alarm and vehicle insurance, leaving a monthly deficit of $1,015. [Bankr. dkt. no. 1]. However, the income and expenses set forth in plaintiff's bankruptcy schedules and her trial testimony do not present a clear picture of plaintiff's current finances.

As a self-employed practitioner, plaintiff's monthly income fluctuates from month to month and from year to year. According to plaintiff's Federal income tax returns, plaintiff generated gross revenues of $8,867 in 2012, $1,075 in 2013, $34,231 in 2014, $29,431 in 2015, and $14,152 in 2016. She testified that in 2017 her practice grosses about $1,000 to $1,200 a month, which would equate to $12,000 to $14,000 for 2017. According to plaintiff's tax

returns, much of plaintiff's expenses are deducted from her gross revenue from operating her law practice as business expenses as reflected in Schedule C (Profit or Loss From Business) to her Federal income tax returns because she uses her residence as an office and some of her expenses are also business-related, such as her telephone landline, internet access, and her utilities.

For the 2016 tax year, plaintiff was married but filed her tax returns separately from her husband. Plaintiff's Schedule C to her 2016 Federal income tax return shows gross receipts of $14,152. [Ex. D]. On her tax return, plaintiff took an $8,000 deduction for rent (at trial, plaintiff testified that although she did not pay rent to her mother, she paid about $700 per month toward payment of the real estate taxes) and a $2,100 deduction for utilities. Plaintiff also deducted $1,591 for legal and professional services. Additionally, she deducted $150 for advertising, although she testified that she cannot afford to pay for advertising. She also deducted $485 for insurance other than health insurance, $500 for office expense, $630 for repairs and maintenance and $375 for taxes and licenses. Her business expenses totaled $13,831, which result in a net profit of $321 for 2016.

Whatever expenses plaintiff did not deduct on her Schedule C as a business expense, plaintiff claimed an employee reimbursement on her 2016 Federal income tax return. The Employee Business Expenses form attached to the tax return shows a vehicle expense of $2,700, $40 for parking fees and tolls, $1,680 for travel expense away from home as an employee, and $1,750 of unreimbursed business expenses. She also included $800 of unreimbursed meals and entertainment from her business. Plaintiff's unreimbursed employee business expenses totaling $6,580 was reported in plaintiff's Schedule A (Itemized Deductions) to her 2016 Federal income tax return and deducted from plaintiff's personal income taxes. This resulted in plaintiff having no taxable income and, therefore, no taxes owed, not even self-employment taxes.

For tax year 2015, plaintiff filed a joint tax return with her husband. [Ex. E]. Plaintiff's Schedule C to the 2015 Federal tax return reflects gross receipts of $29,431 for her legal practice and deductions for advertising, rent, insurance (other than health), taxes and licenses, utilities and $4,583 in expenses for the security alarm, cellphone expenses, professional fees and dues for various organizations and CLEs (continuing legal education classes), computer expenses, and office supplies. Plaintiff did not list unreimbursed business expenses as an itemized deduction for 2015. Rather, as part of her Schedule C, she included $1,006 for car expenses, $1,785 in travel expenses, and $123 for deductible meals and entertainment. Thus, plaintiff deducted certain expenses from her business income because many of her expenses are paid through her business. This resulted in a net profit of $12,784. For 2015, plaintiff did not itemize her deductions. Rather, she claimed a standard deduction for married couples of $12,600. After including the wage income of her husband, plaintiff and her husband owed $2,413 in Federal income taxes for 2015, of which $1,806 represented plaintiff's self-employment taxes.

For the 2014 tax year, plaintiff filed a joint tax return with her husband. [Ex. F]. Plaintiff's Schedule C to her 2014 Federal income tax return shows gross receipts of $34,231 and total deductions of $16,540 for property taxes, travel, meals, utilities, advertising, insurance, supplies, cellphone, on-line expenses, professional groups, registration fees, and her security alarm. In 2014, plaintiff had a net profit of $17,691 for her business. For 2014, plaintiff did not itemize her deductions but took a standard deduction for married couples. With the wage income of her husband, plaintiff and her husband owed $3,939 in Federal income taxes that year of which $2,500 represented plaintiff's self-employment taxes.

For the 2013 tax year, plaintiff's Schedule C to her 2013 Federal income tax return shows gross receipts of $1,075 and expenses of $516, leaving a net profit of $559. [Ex. G]. Plaintiff claimed the standard deduction for 2013 as the amount of the deduction exceeded

her net profit. After deducting expenses, plaintiff's tax obligation was self-employment taxes of $79 for that year.

For the 2012 tax year, plaintiff's Schedule C to her 2012 Federal income tax return shows gross receipts of $8,867 and expenses of $2,973 for her cellphone, on-line expenses, license fees, professional groups, registration fees, review courses, supplies, meals and entertainment, and taxes, leaving net profit of $5,894. [Ex. H]. Plaintiff took a standard deduction for 2012 as the amount of the deduction exceeded her net profit, which resulted in a tax obligation for self-employment taxes of $724 for that year.

Similarly, for the 2011 tax year, plaintiff's Schedule C to her 2011 Federal tax return shows gross income of $9,568 and expenses of $3,470 representing car expenses, supplies, office expenses, taxes and licenses, and other expenses, which resulted in a net profit of $6,188. [Ex. I]. Plaintiff took the standard tax deduction and after deducting her expenses, plaintiff's tax obligation for self-employment taxes totaled $760 for that year.

Although an argument could have been made that plaintiff's tax returns show she had little disposable income after payment of her business expenses, some of plaintiff's personal expenses have already been deducted from her gross revenues because the expenses also have a business component to them. However, when these same business expenses such as rent, security alarm, telephone, cellphone, internet, and cable services are then listed in plaintiff's Schedule J to the bankruptcy petition as personal expenses, the Court cannot comfortably limit its review of plaintiff's financial condition to just her Schedules I and J. For example, if plaintiff pays her "rent" through the business, then how can she then say it is a personal expense under Schedule J that must also be deducted from her gross wages or salary as set forth in Schedule I (Question 2), which seeks to determine a debtor's wages or salary actually paid to her? Even where a debtor receives income from the operation of a business, Schedule I (Question 10) requires the disclosure of "net income" from such business, which is what the

debtor would receive after deducting business-related expenses, and any further deductions against that "net income" to arrive at the debtor's disposable income for bankruptcy purposes should only be the debtor's personal expenses. To list the same expenses on Schedule J that in the past were paid and accounted for as business expenses on prior years' tax returns distorts plaintiff's actual disposable income when such expenses appear to be deducted from plaintiff's gross wages or salary under Schedule I.

Providing information as to her current financial situation should not be a difficult task. It is required by the first prong of the *Brunner* test as the "minimum necessary" to establish undue hardship. *Brunner*, 831 F.2d at 396. It "serve[s] as the starting point . . . since information regarding the debtor's financial situation will be concrete and readily obtainable". *Matter of Robertson*, 999 F.2d 1132, 1135 (7th Cir. 1993). Here, plaintiff has not presented the Court with concrete evidence from which her current financial condition can, with any degree of certainty, be known. As such, the Court is unable to determine on the record before it what expenses listed on plaintiff's bankruptcy Schedule J must be deducted from her income listed on her bankruptcy Schedule I. How then is the Court to make a finding as to plaintiff's disposable income, and whether it allows her to both maintain a minimal standard of living and repay her student loan debt?

What is more problematic is how to accurately account for the indeterminate amount that plaintiff claims she receives throughout the year in the form of cash reimbursements for expenditures she makes on her parents' behalf for on-line or credit card purchases. Similarly, plaintiff testified that when her husband did not have access to the internet, she would make on-line purchases for him and he would reimburse her in cash or through a PayPal transfer to her checking account. Plaintiff testified that although some of the cash reimbursements from her mother and her husband may be deposited into her bank accounts, generally she would just keep the cash on hand to pay upcoming expenses. Plaintiff testified that she does

not keep track of cash she receives from her family, nor did she introduce any documentary evidence showing the expenditures she made on behalf of her family or when she received a reimbursement in whole or in part. Plaintiff's bank statements for the period from 2013 through 2017 show that plaintiff has always maintained a positive bank balance even though plaintiff stated that she rarely deposited the cash she receives from her family into her bank accounts as reimbursement for the purchases debited from the accounts. As noted above, plaintiff's use of cash reimbursements from her family to defray living expenses demonstrates that plaintiff had sufficient funds available in her bank accounts not just for her other general living expenses that were paid directly from her checking account but to make purchases for her family, such as expenses related to vacations to Disney World and gifts for her relatives, and discretionary purchases for herself. Such discretionary expenses included an Apple watch, designer purse and shoes, and numerous purchases in excess of $100 for which plaintiff had no recollection.

In short, there is no evidence in the record from which to conclude that plaintiff is suffering from tight finances, is making sacrifices with respect to discretionary expenses, is living on any sort of restricted budget, and is actively pursuing legal work or taking other steps to maximize her income.

Additionally, because plaintiff is eligible to enter the Ford Program or avail herself of options under the FFELP in order to achieve greater flexibility in repaying the ECMC Loan, plaintiff's payment obligation on the ECMC Loan would be $0 for a period of 25 years based on her reported AGI of $321, as reported in plaintiff's 2016 Federal income tax return. Therefore, it cannot be said that an obligation to pay $0 on the ECMC Loan under the income-based repayment options would cause plaintiff to fall below a minimum standard of living. *Murrell v. Edsouth (In re Murrell)*, 605 B.R. 464 (Bankr. N.D. Ohio 2019) (finding that

debtor's household income and capacity to reduce non-essential expenses would enable debtor to make the payments under an income-based repayment plan).

Based on the trial record, the Court finds that plaintiff has failed to demonstrate by a preponderance of the evidence that she would be unable to maintain a minimum standard of living if required to make payments under the ECMC Loan. Because plaintiff has not met her burden of proof as to the first prong of the *Brunner* test, the Court need not address whether plaintiff has satisfied the remaining two prongs of the *Brunner* test. However, in the interest of completeness, the Court will do so. As set forth below, based on the trial record, the Court finds that plaintiff has similarly failed to meet her burden of proof as to the second and third prong of the three-part *Brunner* test to establish that excepting her student loan debt from discharge will cause her undue hardship.

2. Additional Circumstances Suggesting a Continuing Inability to Repay

"The second prong of the *Brunner* test requires a debtor to show that 'additional circumstances exist indicating that [the debtor's present economic duress] is likely to persist for a significant portion of the repayment period' for the student loans, and that inability to pay is because of factors beyond the debtor's control." *In re Lozada*, 604 B.R. 427, 436 (S.D.N.Y. 2019) (quoting *In re* Crawley, 460 B.R. 421, 438 (Bankr. E.D. Pa. 2011)). "Under this factor, debtors must demonstrate 'unique or exceptional circumstances in their current situations that would clearly limit their future abilities to earn a living, support themselves, and repay their loans.'" *Id.* (citations omitted).

In evaluating this factor, courts may consider a debtor's medical condition, disability, or responsibility for his or her dependents. *King v. Vt. Student Assistance Corp. (In re King)*, 368 B.R. 358, 370 (Bankr. D. Vt. 2007). Courts have also considered a debtor's "assets, career, income or potential for increased career and financial opportunities", *Shenk v. U.S. Dept. of*

Educ. (*In re Shenk)*, 603 B.R. 671, 680 (Bankr. N.D.N.Y. 2019) (internal citations omitted), and whether a debtor has maximized her income potential, has more lucrative job skills, has limited working years left, and whether there are factors that would prevent the debtor from retraining or relocating, *Turturo v. Access Group, Inc. (In re Turturo)*, 522 B.R. 419, 427 (Bankr. N.D.N.Y. 2014) (finding that a 31-year old, consumer bankruptcy attorney had no impairment to preclude his ability to work and no dependents and, with appropriate application and study, could expand to more lucrative areas of practice). *See also Johnson*, 550 B.R. at 880 (finding that the debtor's ability to repay a student loan is not insurmountable even though the debtor lacks a college degree and, at 52 years of age, had limited working years left when the debtor was still in good health).

Where a debtor claims to suffer from a medical or mental condition, the debtor must "precisely identify her problems and explain how her condition would impair her ability to work in the future." *Trudel v. U.S. Dep't of Educ. (In re Trudel)*, 514 B.R. 219, 226 (B.A.P. 6th Cir. 2014) (quoting *Tirch v. Pa. Higher Educ. Assistance Agency (In re Tirch)*, 409 F.3d 677, 681 (6th Cir. 2005)). The debtor must demonstrate "a strong nexus between the medical condition and its adverse effect on the debtor's terms of employment (specifically, a debtor's income)". *Trudel*, 514 B.R. at 226 (quoting *Morrow v. U.S. Dep't of Educ. (In re Morrow)*, 366 B.R. 774, 778 (Bankr. N.D. Ohio 2007)). A debtor's testimony alone is not sufficient to show that the debtor has a limited physical capacity and diminished employment prospect. *Lozada*, 604 B.R. at 436-37. Courts require substantial credible evidence that corroborates a debtor's testimony regarding the nexus between a medical or mental condition and the debtor's inability to earn enough income to repay the educational loan. *Traversa*, 444 F. Appx. at 474-75 (finding debtor failed to prove his alleged medical condition would render him unable to repay his loans over the repayment period when the documentary evidence contained no information about his medical condition); *Gesinde v. U.S. Dep't. of Educ. (In re Gesinde)*,

Case No. 18-10320 (SHL), Adv. No. 18-01434 (SHL), 2019 WL 5090080, at *6 (Bankr. S.D.N.Y. Oct. 10, 2019) (declining to consider debtor's medical conditions where debtor failed to provide an assessment from a medical professional).

Although plaintiff stated that she has "chronic issues" and had knee replacement surgery, she did not explicitly ask that her "chronic issues" or her knee replacement surgery be taken into consideration in determining whether her student loan obligation should be discharged. Further, plaintiff did not testify to, nor did she present any corroborating evidence of, any continuing, underlying medical condition that she suffers from that would interfere with her daily activities, including the practice of law. To the contrary, plaintiff testified that she can shovel snow and, while she said that she cannot earn income by waiting tables because she would be required to be constantly on her feet, her "chronic issues" do not preclude her from engaging in other occupations, including her current one as an attorney. Additionally, the trial record shows that plaintiff is capable of driving, traveling and working, all without issue due to her unspecified chronic issues.

Plaintiff states that she was employed by the law firm Fratello & Fox P.C. as a legal assistant and, upon graduation from law school in 2006, as a lawyer. She worked at the law firm until the middle of June 2011 and opened her own law practice in October 2011. She testified that while at the firm, she would be laid off at times, albeit temporarily, when the firm's legal work slowed down or the attorney whom she worked for had her daughters handle nonlegal tasks. This, however, relates only to plaintiff's past employment history with a single law firm and is not indicative of what transpired after plaintiff opened her own law practice. While plaintiff does not foresee how her current financial situation will change in the next ten years, she has not demonstrated that she cannot earn higher income, or that she is not capable of generating any more revenue. Plaintiff does not lack usable or marketable job skills. Plaintiff mainly receives her business by word of mouth. She did not provide any

testimony or documentary evidence showing any effort to increase her current business base or whether she has actively pursued a position with a law firm to obtain a steady income. Although Plaintiff testified that she cannot afford advertising for her practice, she has taken a tax deduction for advertising and apparently has the discretionary income to advertise her business. As a self-employed individual, plaintiff's own financial future is within her control in terms of how much business she wishes to actively pursue, how many hours she wishes to work each week, and how much she decides to charge for her legal services. As plaintiff's own tax returns demonstrate, her revenue fluctuates from year to year. The trial record in this case does not reveal any impediment to plaintiff's ability to generate more revenue from her business nor any reason why plaintiff should be discharged of her obligation to repay any portion of her student loan obligation, even at a reduced monthly payment, should her earnings increase for a particular year.

Plaintiff's only other "additional circumstance" focuses on her age and the purported number of years left in her working life. Plaintiff was 48 years old at the time of trial and she contends that she intends on working for just 10 more years. While having a goal of retiring at age 58 is a worthy pursuit, plaintiff has not presented any evidence to demonstrate that she is incapable of working beyond age 58. Courts have rejected arguments that age alone satisfies the second prong of the *Brunner* test. *Chance*, 600 B.R. at 59 (rejecting age as a factor where the debtors are in their late fifties); *Tuttle v. Educ. Credit Mgmt. Corp. (In re Tuttle)*, 600 B.R. 783, 801 (Bankr. E.D. Wis. 2019) (rejecting argument that 46 years of age is an "exceptional circumstance" equating to unemployability and a persistent inability to pay). The fact that repayment of plaintiff's student loan obligation will last into her later years in life is a by-product of plaintiff's choice to obtain her law degree in her mid-30's, and it is not a unique or exceptional circumstance that is beyond plaintiff's control. *Little v. U.S. Dep't. of Educ. (In re Little)*, 607 B.R. 853, 861 (Bankr. N.D. Tex. 2019). Plaintiff's argument

that she should be freed of her student loan obligation because she has arbitrarily decided to cease working at age 58 is not sufficient to demonstrate an inability to repay her student loan obligation over an extended period of time.

Under the second prong, a debtor must show circumstances that are "strongly suggestive" of a "continuing inability to repay over an extended period of time." *Brunner*, 831 F.2d at 396. Plaintiff has failed to make that showing here. As noted above, plaintiff is 48 years old, in good health, with no dependents, with a solid education, including a law degree, and she is gainfully employed. While plaintiff argues that she has a continuing inability to repay her student loan obligation, the evidence at trial suggests otherwise. Accordingly, the Court finds that plaintiff has not satisfied her burden of proving by a preponderance of the evidence that she meets the second prong of the *Brunner* test.

3. Good Faith

The third prong of the *Brunner* test considers whether "the debtor has made good faith efforts to repay the loans." *Brunner*, 831 F.2d at 396. Courts look to factors such as a debtor's "efforts to obtain employment, maximize income and minimize expenses, and to undertake all other reasonable efforts to ensure repayment." *Pobiner v. Educ. Credit Mgmt. Corp. (In re Pobiner)*, 309 B.R. 405, 420 (Bankr. E.D.N.Y. 2004) (citation omitted); *Pincus,* 280 B.R. at 316. Repayment efforts can include (1) actual payments made on the loans and (2) attempts by the debtor to seek alternative remedies to discharge, such as deferment of payment. *Pincus,* 280 B.R. at 316. While courts in the Second Circuit do not have a *per se* rule that a debtor's decision to forego an alternative prepayment plan establishes bad faith, courts do consider whether a debtor negotiated or enrolled in an alternative repayment plan as one of the factors for determining good faith efforts. *Benjumen v. AES/Charter Bank (In re Benjumen)*, 408 B.R. 9, 23-24 (Bankr. E.D.N.Y. 2009). *See also Roth v. Educ. Credit. Mgmt. Corp. (In re Roth)*, 490 B.R. 908 (B.A.P. 9th Cir. 2013) (court will consider a debtor's effort or

lack thereof to negotiate a repayment plan but failure to negotiate or accept an alternative repayment plan is not dispositive.).

Aside from the debtor's repayment history, courts also consider whether the debtor's inability to pay was due to circumstances beyond the debtor's control as opposed to lifestyle choices. *Johnson*, 550 B.R. at 881 (finding the absence of good faith where the debtor failed to explain why she purchased a new car when her old car experienced mechanical issues and failed to make higher payments on her student loans when she had the financial wherewithal to increase the amount of her payments). "[T]he debtor may not willfully or negligently cause his own default, but rather his condition must result from factors beyond his reasonable control." *Lozada*, 604 B.R. at 437 (quoting *Pobiner*, 309 B.R. at 420). *See also Faish*, 72 F.3d at 305; *Benjumen*, 408 B.R. at 22. "[A] debtor may not avail himself of [ ] § 523(a)(8) if he is responsible for causing the undue hardship." *Pincus*, at 316.

The only evidence that plaintiff points to regarding her repayment history is her testimony that she repaid a total of $5,000. However, plaintiff only found a single record for one payment of $500, and her testimony that she paid a total of $5,000 is based on the interest deduction she took on her tax returns for student loan repayments. There is no independent or specific evidence in the record that conclusively shows that plaintiff repaid a total of $5,000. Additionally, the last time plaintiff recalls making a payment was in 2010 or 2011. Plaintiff testified that she sought deferments and forbearance on payment of her student loan obligation from the time after she graduated law school until she was no longer able to put off repayment of her loans.

As noted above, there is no evidence in the record that plaintiff tried to maximize her income and economize in order to make payments on her student loan obligations. The trial record shows that plaintiff's legal work comes by referrals, and not by any design of how best to generate business in her practice area. The trial record also shows that plaintiff's checking

account statements reflect various discretionary expenses and purchases in excess of $100 for which plaintiff had no recollection. Plaintiff did not offer any evidence that she has tried to minimize her expenses, and the record placed before the Court shows that she had income in excess of expenses that she could have applied toward repayment of her student loan obligation, at least in part. Additionally, plaintiff chose to attend a conference on international law in Montreal in order to satisfy continuing legal education requirements. Although plaintiff testified that she attended the conference because of an interest in international law, there is no evidence in the trial record that plaintiff has sought to expand her practice to include international law. No reason was given as to why plaintiff could not have found an international law conference within the United States or even in nearby New York City at a lesser cost.

Good faith can be demonstrated where a debtor directs some of her discretionary funds, even if a nominal amount, to pay down the student loans. *In re Shenk*, 603 B.R. at 681. Contrary to plaintiff's testimony that she would pay her student loans whenever she had spare cash to do so, the trial record shows that plaintiff used excess funds for own personal enjoyment or for gifts. The funds plaintiff has on hand in her bank accounts each month is a product of plaintiff's own lifestyle choices and not a result of any effort by her to economize. No evidence was proffered that after accounting for expenses necessary to sustain a minimal standard of living, which would include expenses for shelter, food, transportation, medical and dental expenses, and a reasonable amount for recreation and entertainment, plaintiff sought to limit her discretionary expenses so as to allow for repayment of her student loan obligations.

Other than requesting deferments and forbearance arrangements, plaintiff did not seek to enroll in any alternative repayment programs. While plaintiff is not required to enter into an income-based repayment program, her basis for declining to pursue such an option,

where her future monthly payment under any of the program options would be $0 based upon her 2016 income, is simply the inconvenience of having to report her income annually for 25 years. Plaintiff's unwillingness to be inconvenienced by having to report her annual income for the next 25 years does not provide sufficient justification to discharge her student loan obligation. The courts have found that a debtor's refusal to enter into a reduced loan repayment plan that allows her to remain at her preferred job and maintain her current level of expenditures merely because a debtor wants to retire by a certain age and obtain a fresh start at saving for retirement is "simply shorthand for [a debtor's] lack of interest in repaying the debt." *Augustin v. U.S. Dep't of Educ. (In re Augustin)*, 588 B.R. 141, 153-4 (Bankr. D. Md. 2018) (quoting *Educ. Credit Mgmt. Corp. v. Frushour (In re Frushour)*, 433 F.3d 393, 403 (4th Cir. 2005)).

Further, it is difficult to find good faith based on a record which shows that plaintiff did not even bother to open mail she received regarding her student loan obligations, and plainly states that she just "wants her student loan debt to be over."

Accordingly, based on the record placed before it, the Court concludes that plaintiff has not established that she made good faith efforts to repay her student loan obligation to ECMC. As such, plaintiff has not satisfied her burden of proving by a preponderance of the evidence that she meets the third prong of the *Brunner* test.

CONCLUSION

For the foregoing reasons, plaintiff has failed to demonstrate that she is entitled to a discharge of her student loan debt to ECMC. Accordingly, the Court grants judgment in favor of ECMC dismissing the complaint as against ECMC. ECMC is directed to settle a judgment in accordance with this decision, on no less than five business days' notice to all parties in

interest.

It is so ORDERED.

Dated: April 24, 2020
Central Islip, New York

Louis A. Scarcella
United States Bankruptcy Judge

597 B.R. 725
United States Bankruptcy Court, E.D. New York.

IN RE: Isaac J. GRINSPAN, Debtor.
Isaac J. Grinspan, Plaintiff
v.
Tomor Grinspan and David J. Seidemann, Defendants.

Case No.: 13-76084-las
|
Adv. Pro. No.: 14-8116-las
|
Signed February 8, 2019

Synopsis

Background: Chapter 7 debtor brought adversary proceeding against his ex-wife and her attorney to recover for their allegedly "willful" violations of automatic stay.

Holdings: The Bankruptcy Court, Louis A. Scarcella, J., held that:

[1] contempt motion filed by debtor's ex-wife, based on debtor's nonpayment of sums ordered in prior post-divorce litigation between parties, was in nature of civil contempt motion, which did not come within stay exception for continuation of criminal action against debtor;

[2] attorney fee obligation was not in nature of "domestic support obligation," as that term was used in the Bankruptcy Code;

[3] postpetition contempt motion prosecuted by ex-wife and her attorney to enforce debtor's fee obligation was not action or proceeding for the "collection" of domestic support obligation, of kind excepted from stay;

[4] attorney's stay violation was in nature of "willful" stay violation, though attorney mistakenly believed that his actions came within stay exception; and

[5] debtor was entitled to award of reasonable attorney fees and costs, but not punitive damages.

Ordered accordingly.

Procedural Posture(s): Judgment.

West Headnotes (28)

[1] **Bankruptcy** Enforcement of Injunction or Stay

Burden of proof was on Chapter 7 debtor, as party seeking to recover damages for his ex-wife's and her attorney's violation of automatic stay in continuing to prosecute state court contempt motion after being advised of debtor's bankruptcy filing, to present evidence that defendants willfully violated the automatic stay. 11 U.S.C.A. § 362(k).

[2] **Bankruptcy** Enforcement of Injunction or Stay

Standard of proof, in adversary proceeding to recover damages for allegedly willful violations of automatic stay, was proof by preponderance of the evidence. 11 U.S.C.A. § 362(k).

[3] **Bankruptcy** Evidence; witnesses

To demonstrate something by a "preponderance of the evidence," party simply has to convince the trier of fact that the existence of a fact is more probable than its nonexistence.

[4] **Bankruptcy** Automatic Stay

Automatic stay is one of the most fundamental bankruptcy protections, which provides debtor with breathing spell and prevents creditors from obtaining payment of their claims in preference to, and to the detriment of, other creditors. 11 U.S.C.A. § 362(a).

[5] **Bankruptcy** Automatic Stay

Automatic stay is broadly written and broadly construed. 11 U.S.C.A. § 362(a).

[6] **Bankruptcy** Notice to creditors; commencement

Automatic stay is self-executing, in the sense that it must be complied with, even in absence of any action by debtor or the court, at the risk of sanctions for a violation thereof. 11 U.S.C.A. § 362(a).

[7] **Bankruptcy** Automatic Stay

Onus is on creditor to inform other courts in which it has matters pending of debtor's bankruptcy filing and to discontinue any pending proceedings that run afoul of the stay provisions. 11 U.S.C.A. § 362(a).

[8] **Bankruptcy** Proceedings, Acts, or Persons Affected

Exceptions to automatic stay are construed narrowly in order to secure a broad grant of relief to debtor. 11 U.S.C.A. § 362(b).

2 Cases that cite this headnote

[9] **Bankruptcy** Enforcement of Injunction or Stay

Whether party has knowledge of debtor's bankruptcy filing is immaterial to whether its actions violate automatic stay. 11 U.S.C.A. § 362(a).

[10] **Bankruptcy** Domestic relations claims and proceedings

Conduct of attorney for debtor's ex-wife, after acquiring actual knowledge of debtor's Chapter 7 filing prior to hearing on ex-wife's state court motion to hold debtor in contempt for not making payments required in prior post-divorce litigation between parties, in not taking any action to modify the relief sought by contempt motion or to discontinue contempt motion in its entirety, violated various stay provisions as being in nature, not only of continuation of proceeding against debtor, but of enforcement, against debtor of judgment obtained prior to commencement of case, and of an act to collect, assess, or recover claim against debtor that arose prepetition. 11 U.S.C.A. § 362(a)(1, 2, 6).

[11] **Bankruptcy** Contempt

Contempt motion filed by Chapter 7 debtor's ex-wife, based on debtor's nonpayment of sums ordered in prior post-divorce litigation between parties, was in nature of civil contempt motion brought to compel debtor to comply with obligations that he owed to ex-wife, which did not come within stay exception for the continuation of criminal action against debtor. 11 U.S.C.A. § 362(b)(1).

[12] **Bankruptcy** Construction and Operation

Determination as to what constitutes a "domestic support obligation," as that term is defined in the Bankruptcy Code, is based on principles of federal law and is fact-intensive inquiry. 11 U.S.C.A. § 101(14A).

1 Cases that cite this headnote

[13] **Bankruptcy** Construction and Operation

Chapter 7 debtor's obligation for attorney fees awarded to ex-wife pursuant to language in divorce stipulation of settlement which was located in separate section of stipulation than provisions dealing with spousal maintenance and child support, and which required both parties to comply with their obligations under stipulation on pain of being liable for attorney fees incurred by the other party in successfully bringing enforcement action, was not in nature

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of "domestic support obligation," as that term was used in the Bankruptcy Code; obligation was not imposed to provide for needs of the more needy spouse, but reciprocally on both parties as means of ensuring their compliance with obligations imposed by stipulation of settlement. 11 U.S.C.A. § 101(14A).

[14] **Bankruptcy** Construction and Operation

Attorneys' fees awarded in prepetition matrimonial action may, under certain circumstances, fall within the Bankruptcy Code's definition of a "domestic support obligation." 11 U.S.C.A. § 101(14A).

[15] **Bankruptcy** Domestic relations claims and proceedings

Even assuming that attorney fee obligation imposed on Chapter 7 debtor pursuant to reciprocal, fee-shifting provision of divorce stipulation of settlement between debtor and his ex-wife was in nature of "domestic support obligation," postpetition contempt motion prosecuted by ex-wife and her attorney to enforce debtor's obligation for such fees was not action or proceeding for the "collection" of domestic support obligation, as that term was used in stay exception; term "collection" could not be interpreted so broadly as to include postpetition proceeding to enforce debtor's fee obligation by holding him in contempt. 11 U.S.C.A. § 362(b)(2)(B).

1 Cases that cite this headnote

[16] **Bankruptcy** Construction and Operation

No one provision of the Bankruptcy Code can be viewed in isolation from the others; each provision must be construed in the context of the whole.

[17] **Statutes** Express mention and implied exclusion; expressio unius est exclusio alterius

When Congress includes particular language in one section of statute but omits it in another section of the same act, it is generally presumed that Congress acts intentionally and purposely in this disparate inclusion or exclusion.

[18] **Bankruptcy** Damages and attorney fees

Bankruptcy statute providing that "[a]n individual injured by any willful violation of a stay … shall recover actual damages" creates a private right to sue for damages on behalf of individuals injured by any willful violation of automatic stay. 11 U.S.C.A. § 362(k).

[19] **Bankruptcy** Damages and attorney fees

"Willful" stay violation requires a deliberate act undertaken in violation of the stay, which the violator knows to be in existence. 11 U.S.C.A. § 362(k).

[20] **Bankruptcy** Damages and attorney fees

Specific intent to violate the automatic stay is not required in order for a stay violation to be "willful," and to permit award of damages against the violator; instead, a general intent in taking actions which have the effect of violating automatic stay is sufficient to warrant damages. 11 U.S.C.A. § 362(k).

1 Cases that cite this headnote

[21] **Bankruptcy** Damages and attorney fees

Creditor's good faith belief in its right to property is not relevant to determination of whether its actions with regard to that property are in nature of "willful" violations of automatic stay. 11 U.S.C.A. § 362(k).

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[22] **Bankruptcy** Damages and attorney fees

When stay violation is willful, award of actual damages sustained by debtor is mandatory. 11 U.S.C.A. § 362(k).

[23] **Bankruptcy** Exemplary or punitive damages; fines

Whether to assess punitive damages for "willful" violation of automatic stay lies within discretion of court. 11 U.S.C.A. § 362(k).

1 Cases that cite this headnote

[24] **Bankruptcy** Exemplary or punitive damages; fines

An additional finding of maliciousness or bad faith on part of offending creditor warrants the further imposition of punitive damages for creditor's "willful" violation of automatic stay. 11 U.S.C.A. § 362(k).

[25] **Bankruptcy** Damages and attorney fees

Notification to creditor that a bankruptcy petition "may be" filed is insufficient to constitute actual notice of existence of automatic stay, such as will render any subsequent stay violation by creditor a "willful" stay violation. 11 U.S.C.A. § 362(k).

1 Cases that cite this headnote

[26] **Bankruptcy** Damages and attorney fees

Violation of automatic stay by attorney for Chapter 7 debtor's ex-wife, in continuing to prosecute state court proceeding to hold debtor in contempt for not paying attorney fees awarded by state court even after attorney learned of debtor's bankruptcy filing, was in nature of "willful" stay violation, though attorney mistakenly believed that his actions came within stay exception for actions to collect domestic support obligations from property not included in bankruptcy estate. 11 U.S.C.A. § 362(b)(2)(B), (k).

[27] **Bankruptcy** Damages and attorney fees

As actual damages for willful stay violation by his ex-wife's attorney, for continuing to prosecute state court proceeding to hold debtor in contempt for not paying attorney fees awarded by state court even after attorney learned of debtor's bankruptcy filing, debtor was entitled to award of reasonable attorney fees and costs. 11 U.S.C.A. § 362(k).

[28] **Bankruptcy** Exemplary or punitive damages; fines

Violation of automatic stay by attorney for Chapter 7 debtor's ex-wife, in continuing to prosecute state court proceeding to hold debtor in contempt for not paying attorney fees awarded by state court even after attorney learned of debtor's bankruptcy filing, in mistaken belief his actions came within stay exception for collection of domestic support obligations, was not sufficiently egregious or accompanied by such aggravated circumstances as would warrant award of punitive damages. 11 U.S.C.A. § 362(b)(2)(B), (k).

Attorneys and Law Firms

***729** Richard V. Kanter, Melville, NY, for Plaintiff.

Scott Fleischer, Jordan Pilevsky, LaMonica Herbst & Maniscalco LLP, Wantagh, NY, Paul M. Sod, Lawrence, NY, Marian C. Rice, L'Abbate Balkan Colavita & Contini, Garden City, NY, for Defendants.

MEMORANDUM DECISION AFTER TRIAL

Louis A. Scarcella, United States Bankruptcy Judge

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Plaintiff Isaac Grinspan commenced this adversary proceeding against his ex-spouse, Tomor Grinspan, and her attorney, David J. Seidemann, to recover damages under 11 U.S.C. § 362(k) for an alleged violation of the automatic stay imposed under 11 U.S.C. § 362(a).[1] Plaintiff alleges defendants willfully violated the automatic stay when they continued to litigate a motion to hold plaintiff in contempt in the parties' state court matrimonial action after plaintiff filed his chapter 7 bankruptcy petition. Plaintiff's view is that litigation of the contempt motion, which sought to enforce a money judgment consisting of attorneys' fees awarded to Tomor as a result of plaintiff's alleged default under their divorce agreement, is not exempt from the automatic stay under § 362(b)(2)(B) as an act to collect a domestic support obligation. Plaintiff also asks the Court to permanently enjoin defendants from litigating the contempt motion. In response, defendants argue that while matters were proceeding in state court post-petition, no action was taken by them to enforce the pre-petition money judgment. Additionally, defendants argue that even if their actions in the state court proceeding post-petition are construed as a demand for payment of the money judgment, those actions sought to collect upon a domestic support obligation and are exempt from the automatic stay under § 362(b)(2)(B). Last but not least, defendants contend that if their post-petition conduct is not exempt from the automatic stay, such conduct was not taken in willful violation of the stay.

The Court has jurisdiction over this matter under 28 U.S.C. § 1334 and the Standing Order of Reference entered by the United States District Court for the Eastern District of New York pursuant to 28 U.S.C. § 157(a), dated August 28, 1986, as amended by Order dated December 5, 2012, effective *nunc pro tunc* as of June 23, 2011. This is a core proceeding under 28 U.S.C. § 157(b)(1) in which final orders or judgment may be entered by the Court. *See In re Jean-Francois*, 532 B.R. 449, 451 (Bankr. E.D.N.Y. 2015).

Having considered the parties' pretrial submissions and the evidence presented at trial, the Court makes the following findings of fact and conclusions of law pursuant to Rule 52(a) of the Federal Rules of Civil Procedure, made applicable here by ***730** Bankruptcy Rule 7052. To the extent that a finding of fact includes a conclusion of law, it is deemed a conclusion of law and vice versa.

For the following reasons, the Court finds in favor of plaintiff. Defendants willfully violated the automatic stay and, by statute, are liable for actual damages, including costs and attorneys' fees under § 362(k). The Court reserves judgment on actual damages pending submission of supplemental briefing, and will issue a separate order scheduling a hearing to determine the amount of appropriate damages. The Court declines to award plaintiff punitive damages and dismisses plaintiff's request for permanent injunctive relief as moot.

I. Findings of Fact

The following findings of fact are based on the trial record, which include the trial testimony, exhibits entered into evidence, and the parties' stipulation of certain facts.[2]

A. Pre-Petition State Court Proceedings

Plaintiff and Tomor are former spouses and have two children together. Stip. ¶¶ 2, 3. They entered into a divorce stipulation of settlement (the "Settlement") dated July 27, 2010. Defs.' Ex. A; Stip. ¶ 4. The Settlement provides that if either plaintiff or Tomor failed to comply with their respective obligations under the Settlement, the defaulting party will reimburse the non-defaulting party for legal fees incurred in connection with enforcing the Settlement, so long as the non-defaulting party prevails. Stip. ¶ 5; *see* Defs.' Ex. A at 41 ("[T]he defaulting party ... agrees to indemnify the non-defaulting party against and/or to reimburse him/her for any and all expenses, costs, and reasonable attorneys' fees resulting from or made necessary by the bringing of any suit or other legal proceeding to enforce any of the terms, covenants or conditions of this [Settlement]."). If the non-defaulting party loses, he or she must reimburse the legal fees incurred by the other party. Defs.' Ex. A at 41. On May 3, 2011, a judgment of divorce was entered. Defs.' Ex. B; Stip.¶ 6. The judgment of divorce incorporated the Settlement. Stip. ¶ 6.

In May 2013, Tomor sought to enforce plaintiff's obligations under the Settlement and plaintiff sought to decrease his child support payments. Defs.' Ex. E at 2. Thereafter, Nassau County Supreme Court Judge Edward Maron entered a Consent Order, dated July 1, 2013, that required plaintiff to reinstate his child support payments and to cure any arrears, pay for one of his children's therapy, and restore Tomor as the beneficiary of his life insurance policy. Defs.' Ex. E ¶¶ 2, 12, 19; Stip. ¶ 8. The Consent Order also provided that plaintiff

must pay Tomor $ 18,000 for attorneys' fees she incurred during the enforcement proceeding. Defs.' Ex. E ¶ 25.

Plaintiff defaulted under the Consent Order, and Tomor obtained a money judgment against plaintiff in the amount of $ 18,372.61, which consisted of the attorneys' fees owed to Tomor plus accrued interest (the "Money Judgment"). Defs.' Ex. I; Stip. ¶ 9. On or about September 9, 2013, defendant Seidemann, Tomor's attorney in the post-judgment phase of her state court matrimonial action, served ***731** plaintiff with an "Information Subpoena." Defs.' Ex. J; Stip. ¶¶ 7, 10. Plaintiff did not respond to the Information Subpoena or fulfill his obligations set forth in the Consent Order, which included payment of the Money Judgment. Stip. ¶ 11. As a result, on or about November 14, 2013, Seidemann moved by order to show cause to hold plaintiff in contempt for his alleged non-compliance with the Consent Order and for him to be imprisoned, again seeking to enforce the Money Judgment and obtain answers to the Information Subpoena (the "Contempt Motion"). Pl.'s Ex. 6; Stip. ¶ 11; Tr. 17:14-18:1. The Contempt Motion did not request relief related to custody or visitation rights of plaintiff and Tomor's children. Stip. ¶ 12. The return date of the Contempt Motion was December 5, 2013. Stip. ¶ 13.

On December 2, 2013, plaintiff, by his then-counsel in the state court proceeding, Steven Borofsky, submitted answers to the Information Subpoena. Stip. ¶ 14. However, Seidemann was dissatisfied with plaintiff's answers. Seidemann emailed Borofsky and stated "[he] will give [plaintiff] till [sic] Thursday to answer [the Information Subpoena] again truthfully. Otherwise, [he] will seek his incarceration." Stip. ¶ 15.

B. Plaintiff's Bankruptcy Case and Post-Petition State Court Proceedings

Plaintiff filed a chapter 7 bankruptcy petition on December 3, 2013. Stip. ¶ 1. On the petition date, plaintiff's bankruptcy counsel, Richard Kanter, faxed Seidemann a letter and called Seidemann's cellphone to advise him of plaintiff's bankruptcy filing. Pl.'s Ex. 9; Tr. 133:18-24, 134:7-139:1. However, Seidemann testified that he was not in his office on December 3 to receive the fax, Tr. 135:5-7, and that he was not definitively told by Kanter during the phone call that plaintiff actually filed a bankruptcy petition, Tr. 134:2-6. Although Seidemann claimed he did not have actual knowledge of the bankruptcy filing on December 3, the parties stipulated that both Seidemann and Tomor had actual notice of the filing "at least prior to December 5, the return date of the Contempt Motion." Stip. ¶ 16. Seidemann testified to the same. Tr. 146:14-16.

On December 5, 2013, the parties appeared in state court on the Contempt Motion. Stip. ¶ 18. Debtor arrived in state court on this day under the impression that he would be sent to jail if he did not pay the Money Judgment. Tr. 106:10-107:10. Although it is defendants' position that the Contempt Motion was exempt from the automatic stay, Stip. ¶ 17, Seidemann advised Judge Maron that it's possible that the relief he was seeking in the Contempt Motion was subject to the stay, Tr. 171:6-9. In spite of this awareness, Seidemann continued to prosecute the Contempt Motion in its entirety. Adv. Dkt. No. 34-13 at 24:9-16. Seidemann testified that Judge Maron was going to carry the motion "to the end of time," Tr. 173:12-13, and Borofsky stated it to be "the practice of Judge Mar[o]n to carry ... motions when he's not sure what to do with them," Adv. Dkt. No. 34-13 at 31:8-10. At the December 5 hearing, Judge Maron asked the parties to file briefs on the applicability of the automatic stay to the Money Judgment, and entered an order that directed the parties to appear for a conference on January 4, 2014 and appointed Jeffrey Halberich as the children's attorney. Adv. Dkt. No. 34-13 at 38:7-17, 41:4-7; Stip. ¶ 19; Tr. 265:14-19. Thereafter, Seidemann submitted a brief and a proposed order to Judge Maron. Defs.' Ex. O. Borofsky did not file a brief because he was relieved as plaintiff's counsel shortly after the hearing and replaced by Danielle Seid-Vazana.

***732** Following the December 5 hearing, there were five court appearances by the parties: December 19, January 14, February 6, April 17, and April 29. Stip. ¶ 20; Tr. 256:24-257:2. There are no transcripts or other records of any of these hearings because of more than forty appearances before Judge Maron, the parties were on the record "twice, maybe three times at most." Tr. 174:10-21. Seidemann testified he did not move forward with the Contempt Motion at any of these court proceedings and that there was "zero discussion" of it. Tr. 257:3-6. However, Seidemann's testimony is contradicted by both a letter he wrote to Seid-Vazana on December 16, 2013, which he claims Judge Maron instructed him to send, and Seid-Vazana's testimony. Seidemann's letter advised Seid-Vazana that she was "scheduled to appear before Judge Maron on

the Contempt Motion on January 14, 201[4]," Pl.'s Ex. 15, and Seid-Vazana testified she appeared on January 14 for the Contempt Motion, Tr. 81:8-13. The Contempt Motion and Seidemann's letter caused Seid-Vazana to believe that plaintiff could potentially be incarcerated because she testified that she has had clients in the past who have been arrested and "taken away in handcuffs." Tr. 20:18-21:22.

With respect to the December 19, February 6, and April 17 appearances, there is a lack of evidence to support a finding by this Court that they concerned the Contempt Motion. Seid-Vazana could not recall what matters those court appearances concerned, Tr. 41:22-44:7, and Halbreich had no knowledge of any discussions related to the Contempt Motion on those days because he only attended court conferences related to the children, Tr. 94:17-20.

Seidemann's December 16, 2013 letter to Seid-Vazana not only told her to appear in state court for the Contempt Motion on January 14, 2014, but it sought her opposition papers as well. Plaintiff's opposition to the Contempt Motion was filed in advance of the January 14, 2014 court conference, and Tomor's reply, which included her affidavit and an affirmation signed by Seidemann, was filed in March 2014. Stip. ¶¶ 24, 25. Seidemann's affirmation and Tomor's affidavit both requested that the state court grant the Contempt Motion "in its entirety." Stip. ¶ 26. The Contempt Motion was marked fully submitted on or about April 29, 2014. Stip. ¶ 29. Despite the Contempt Motion being marked fully submitted, on April 29, 2014, Seidemann advised the state court to "hold off decision on any part of the [Contempt Motion], including the request to enforce the Money Judgment or compel answers to the Information Subpoena." Stip. ¶¶ 27, 29. Also on April 29, 2014, Seidemann advised the state court that he was withdrawing the Information Subpoena. Stip. ¶ 27. At no point prior to April 29, 2014 did Seidemann seek to withdraw or modify the Contempt Motion to exclude the demand for payment of the Money Judgment or advise plaintiff not to respond to the Information Subpoena. Stip. ¶¶ 21, 28.

The Money Judgment has since been vacated. Tr. 58:10-13. In August 2014, Seidemann withdrew the Contempt Motion. Tr. 223:4-9. No ruling was made by Judge Maron as to whether the Money Judgment is a domestic support obligation or whether the automatic stay applies to the relief sought in the Contempt Motion. Stip. ¶ 23. Defendants did not move this Court for relief from the automatic stay to allow the Contempt Motion to proceed. Stip. ¶ 22.

II. Conclusions of Law

As noted above, plaintiff alleges that defendants willfully violated the automatic stay imposed under § 362(a) when they ***733** continued to litigate the Contempt Motion in state court after plaintiff commenced his bankruptcy case. Plaintiff asks this Court to assess both actual and punitive damages under § 362(k) for defendants' willful violation of the stay. The Court will first identify the burden of proof for plaintiff's cause of action, and then consider the legal principles applicable to the automatic stay. The Court will then resolve the three primary questions presented at trial: (1) whether defendants violated the automatic stay; (2) if so, whether the Money Judgment is a domestic support obligation and defendants' conduct is therefore exempt from the automatic stay under § 362(b)(2)(B); and (3) if defendants' conduct is not allowed under § 362(b)(2)(B), whether that conduct constitutes a willful violation of the automatic stay.

A. Burden of Proof

[1] **[2]** **[3]** To prevail on his claim, plaintiff has the burden of proof to present evidence in support of the allegations in his complaint that defendants willfully violated the automatic stay and to prove those allegations by a preponderance of the evidence. *In re Manchanda*, No. 16-10222 (JLG), 2016 WL 3034693, at *5 (Bankr. S.D.N.Y. May 19, 2016); *Jean-Francois*, 532 B.R. at 454, 456-57. "The burden of showing something by a preponderance of the evidence ... simply requires the trier of fact to believe that the existence of a fact is more probable than its nonexistence ...." *Metro. Stevedore Co. v. Rambo*, 521 U.S. 121, 137 n.9, 117 S.Ct. 1953, 138 L.Ed.2d 327 (1997) (first alteration in original) (quoting *Concrete Pipe & Prods. of Cal., Inc. v. Constr. Laborers Pension Trust for S. Cal.*, 508 U.S. 602, 622, 113 S.Ct. 2264, 124 L.Ed.2d 539 (1993)). "As the finder of fact, the Court is entitled to make credibility findings of the witnesses and testimony." *Merck Eprova AG v. Gnosis S.p.A.*, 901 F.Supp.2d 436, 448 (S.D.N.Y. 2012), *aff'd*, 760 F.3d 247 (2d Cir. 2014).

B. The Automatic Stay: 11 U.S.C. § 362(a)

[4] **[5]** **[6]** The automatic stay "is one of the most fundamental bankruptcy protections and ... 'give[s] the debtor

a breathing spell' and ... prevent[s] creditors from obtaining payment of their claims in preference to and to the detriment of other creditors." *Sec. Inv'r Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC* (*In re Madoff*), 429 B.R. 423, 430 (Bankr. S.D.N.Y. 2010) (internal quotation marks and citations omitted). Given its fundamental importance to a debtor's bankruptcy case, the automatic stay "is broadly written and broadly construed." *In re NextWave Pers. Commc'ns, Inc.*, 244 B.R. 253, 271 (Bankr. S.D.N.Y. 2000). "Pursuant to section 362(a) of the Bankruptcy Code, the filing of a bankruptcy petition 'operates as a stay, applicable to all entities, of' most actions against the debtor, the debtor's property and any property of the estate." *In re Hale*, 535 B.R. 520, 523 (Bankr. E.D.N.Y. 2015) (quoting 11 U.S.C. § 362(a)); *see In re Ebadi*, 448 B.R. 308, 313 (Bankr. E.D.N.Y. 2011). "The automatic stay most certainly is 'self executing' in the sense that it must be complied with absent any action by the debtor or the court, at the risk of sanctions for violation." *Metromedia Fiber Network Servs. v. Lexent, Inc.* (*In re Metromedia Fiber Network, Inc.*), 290 B.R. 487, 493 (Bankr. S.D.N.Y. 2003); *see also In re Lehman Bros. Holdings*, 433 B.R. 101, 112 (Bankr. S.D.N.Y. 2010) ("Nothing is more basic to bankruptcy law than the automatic stay and nothing is more important to fair case administration than enforcing the stay violation."), *aff'd*, 445 B.R. 130 (S.D.N.Y. 2011).

[7] The onus is on the creditor to inform other courts of a debtor's bankruptcy ***734** filing and to discontinue any pending proceedings that run afoul of the stay provisions. *Soares v. Brockton Credit Union* (*In re Soares*), 107 F.3d 969, 978 (1st Cir. 1997) ("Bankruptcy law forbids creditors from continuing judicial proceedings against bankrupts, and, accordingly, it is the creditor's obligation to inform other courts of the situation." (citations omitted)); *In re Parry*, 328 B.R. 655, 659 (Bankr. E.D.N.Y. 2005) ("It is well settled that a creditor has an affirmative duty under § 362 to take the necessary steps to discontinue its collection activities against a debtor."); *In re Henry*, 328 B.R. 664, 668 (Bankr. E.D.N.Y. 2005) (placing the responsibility to end collection efforts "squarely on the shoulders of the creditor who initiated the action" (quoting *Sucre v. MIC Leasing Corp.* (*In re Sucre*), 226 B.R. 340, 347 (Bankr. S.D.N.Y. 1998))). The burden is on the creditor to cease collection efforts because to force the debtor "to take affirmative legal steps to recover property seized in violation of the automatic stay would subject the debtor to the financial pressures the automatic stay was designed to temporarily abate." *In re Burbano*, No. 16-68396-PMB, 2017 WL 1058219, at *6 (Bankr. N.D. Ga. Mar. 20, 2017) (quoting *Roche v. Pep Boys, Inc.* (*In re Roche*), 361 B.R. 615, 621 (Bankr. N.D. Ga. 2005)).

Section 362(a) lists eight activities – acts and actions – that are stayed by the filing of a bankruptcy petition. Three of the listed activities covered by the automatic stay are relevant to plaintiff's claim that defendants willfully violated the stay by continuing to litigate the Contempt Motion, and in particular, enforcement of the Money Judgment. Plaintiff relies on the provisions that stay: "(1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title; (2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title; ... [and] (6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title." 11 U.S.C. § 362(a). Plaintiff argues that defendants' post-petition conduct in respect of the Contempt Motion transgress these stay provisions because such conduct is nothing short of a continuation of a judicial proceeding, the enforcement of a pre-petition judgment, and an action to collect a pre-petition claim. In response, defendants assert that any action taken by them after plaintiff filed his bankruptcy case is exempt from the automatic stay under § 362(b)(2)(B).

[8] Although the automatic stay brings to a halt virtually all creditor collection activity, § 362(b) contains twenty-eight exceptions to the stay. The exceptions are "read narrowly to secure [a] broad grant of relief to the debtor." *Stringer v. Huet* (*In re Stringer*), 847 F.2d 549, 552 (9th Cir. 1988); *see Pa. Dep't Pub. Welfare v. Davenport*, 495 U.S. 552, 560, 110 S.Ct. 2126, 109 L.Ed.2d 588 (1990) (construing exceptions to stay narrowly). As discussed below, the parties dispute whether the actions taken post-petition by defendants fall under the exception set forth in § 362(b)(2)(B). Section 362(b)(2)(B) provides that the filing of a bankruptcy petition does not operate as a stay against "the collection of a domestic support obligation from property that is not property of the estate." 11 U.S.C. § 362(b)(2)(B). In short, defendants maintain that any acts taken by them post-petition in respect of ***735** the Money Judgment are exempt from the automatic stay under § 362(b)(2)(B) as the collection of a domestic support

obligation. For his part, plaintiff contends that § 362(b)(2)(B) is inapplicable because the Money Judgment is not a "domestic support obligation" as that term is defined in § 101(14A). Additionally, plaintiff asserts that if the Money Judgment is determined to be a domestic support obligation, defendants' conduct still does not fall within the ambit of the exception as defendants sought to enforce, not collect, the Money Judgment.

C. Plaintiff Has Established that Defendants Violated the Automatic Stay

The Money Judgment was entered against plaintiff in August 2013. Pl.'s Ex. 4. In November 2013, Seidemann filed the Contempt Motion in state court to enforce payment of the Money Judgment, with the motion's return date scheduled for December 5, 2013. Adv. Dkt. No. 48 at 3; Pl.'s Ex. 6. Plaintiff filed his bankruptcy petition on December 3, 2013. Adv. Dkt. No. 48 at 1. While the filing of the Contempt Motion itself did not violate the automatic stay because it was filed before plaintiff commenced his bankruptcy case, the evidence in this case reveals that defendants' post-petition conduct violated the automatic stay. Specifically, defendants' conduct in respect of the pending Contempt Motion was prohibited by § 362(a)(1), (2), and (6). Those provisions protect the bankruptcy estate by prohibiting the very acts taken here by defendants, to wit, the continuation of a legal proceeding, the enforcement of a judgment obtained pre-petition, and an act to collect or recover a claim that arose pre-petition.

[9] **[10]** The facts show defendants had actual knowledge of the filing of plaintiff's bankruptcy case "at least prior to December 5, 2013, the return date of the Contempt Motion," Stip. ¶ 16, and Seidemann testified that was the case, Tr. 146:14-16. Even if defendants were unaware of plaintiff's bankruptcy filing, "a party's knowledge of the [bankruptcy] filing is 'immaterial' to a determination of whether the stay was violated." *In re Prusan*, 495 B.R. 203, 207 (Bankr. E.D.N.Y. 2010) (quoting *Siskin v. Complete Aircraft Servs., Inc.* (*In re Siskin*), 231 B.R. 514, 517 (Bankr. E.D.N.Y. 1999)). Despite having actual knowledge of plaintiff's bankruptcy case prior to the December 5 hearing on the Contempt Motion, Seidemann did not take any action to modify the relief sought by the Contempt Motion or discontinue the Contempt Motion in its entirety. Nor did he ask this Court for relief from the automatic stay. In the end, the prudent approach would have been for Seidemann to seek declaratory relief from this Court before taking any action with respect to the pending Contempt Motion. *See Crysen/Montenay Energy Co. v. Esselen Assocs.* (*In re Crysen/Montenay Energy Co.*), 902 F.2d 1098, 1105 (2d Cir. 1990) ("[Section 362(k)] encourages would-be violators to obtain declaratory judgments before seeking to vindicate their interests in violation of an automatic stay, and thereby protect debtors' estates from incurring potentially unnecessary legal expenses in prosecuting stay violations."). Rather than filing a motion for relief from the automatic stay before proceeding in state court against plaintiff, Seidemann concluded that his actions were permissible. That was an incorrect assumption.

Although Seidemann testified that he "did nothing to enforce the [Money Judgment] after December 5" and that "there was no danger of the Contempt Motion being heard" because Judge Maron was going to "carry [the Contempt Motion] to the end of time," Seidemann's testimony is ***736** belied by the events as they actually unfolded. He continued to litigate the motion post-petition. Tr. 173:12-15, 182:1-3. Seidemann's post-petition letter to Seid-Vazana reminded her of the scheduled court appearance before Judge Maron on the Contempt Motion and the date by which plaintiff's opposition to the Contempt Motion must be filed. After plaintiff's opposition was filed, Seidemann filed a reply, which still sought for the Contempt Motion to "be granted in its entirety." Pl.'s Ex. 8; Tr. 47:18-25, 48:1-10. It is hardly the case that Seidemann "did nothing" to enforce the Money Judgment post-petition. The evidence introduced at trial demonstrates that defendants' post-petition conduct falls squarely within the ambit of § 362(a)(1), (2), and (6), and the Court finds that Seidemann's own actions in continuing to prosecute the Contempt Motion after plaintiff commenced his bankruptcy case violated the automatic stay. *See Picard v. Fairfield Greenwich Ltd.*, 762 F.3d 199, 207 (2d Cir. 2014) ("[S]o central is the § 362 stay to an orderly bankruptcy process that actions taken in violation of the stay are void and without effect." (alterations in original) (quoting *FDIC v. Hirsch* (*In re Colonial Realty*), 980 F.2d 125, 137 (2d Cir. 1992))); *see also In re Salov*, 510 B.R. 720, 727 (Bankr. S.D.N.Y. 2014) (stay violated where creditors filed a motion for writ of eviction against the debtor); *Prusan*, 495 B.R. at 206-08 (stay violated where creditor's attorney sent a post-petition letter to the state court in an underlying action requesting a contempt hearing against debtor).

Having established that defendants violated the stay by continuing to prosecute the Contempt Motion, the next question for the Court is whether defendants' actions are exempt from the automatic stay under § 362(b)(2)(B). If so, defendants' excepted conduct is allowed. If not, the Court will address the final question: whether defendants' conduct is subject to sanctions under § 362(k).

D. Applicability of 11 U.S.C. § 362(b)(2)(B)

[11] At trial, defendants took the position that any action taken by them after plaintiff commenced his bankruptcy case is exempt from the automatic stay under § 362(b)(2)(B).[3] Defendants argue that because the Money Judgment is a "domestic support obligation" as that term is defined under § 101(14A), any action by them to collect the Money Judgment is allowed by § 362(b)(2)(B). Plaintiff has a different view. He argues that the Money Judgment was not entered for the purpose of awarding support to Tomor and/or to his children. Plaintiff contends that the Money Judgment is not a domestic support obligation and defendants' conduct is not exempt from the constraints of the automatic stay. Plaintiff also asserts that even if this Court were to conclude that the Money Judgment constitutes a domestic support obligation, defendants' conduct is still not ***737** permitted under § 362(b)(2)(B) because defendants sought to enforce, not collect, the Money Judgment, and while collection is a protected activity, enforcement is not.

Accordingly, the heart of the parties' dispute is not whether defendants took steps after the bankruptcy filing to obtain payment of the Money Judgment, but rather, whether the Money Judgment constitutes a domestic support obligation and whether the term "collection" in § 362(b)(2)(B) includes the enforcement of a domestic support obligation through contempt proceedings.

1. Is the Money Judgment a Domestic Support Obligation?

[12] The determination of what constitutes a domestic support obligation is based on principles of federal law and is a fact intensive inquiry. *Romano v. Romano* (*In re Romano*), 548 B.R. 39, 46 (Bankr. S.D.N.Y. 2016); *Grinspan v. Grinspan* (*In re Grinspan*), No. 13-76084-las, 2015 WL 4450668, at *5 (Bankr. E.D.N.Y. July 20, 2015) (citing *Falk & Siemer, LLP v. Maddigan* (*In re Maddigan*), 312 F.3d 589, 595 (2d Cir. 2002)). Domestic support obligations are defined in § 101(14A), which provides:

> The term "domestic support obligation" means a debt that accrues before, on, or after the date of the order for relief in a case under this title, including interest that accrues on that debt as provided under applicable nonbankruptcy law ... that is:
>
> (A) owed to or recoverable by—
>
> (i) a spouse, former spouse, or child of the debtor or such child's parent ...;
>
> ....
>
> (B) in the nature of alimony, maintenance, or support ... of such spouse, former spouse, or child of the debtor or such child's parent, without regard to whether such debt is expressly so designated;
>
> (C) established or subject to establishment before, on, or after the date of the order for relief in a case under this title, by reason of applicable provisions of—
>
> (i) a separation agreement, divorce decree, or property settlement agreement;
>
> (ii) an order of a court of record;
>
> (iii) a determination made in accordance with applicable nonbankruptcy law by a governmental unit; and
>
> (D) not assigned to a nongovernmental entity ....

11 U.S.C. § 101(14A).

[13] The Settlement states that if either party is in default, the defaulting party will reimburse the non-defaulting party for reasonable attorneys' fees incurred in bringing suit or another proceeding to enforce the Settlement so long as the non-defaulting party prevails. Defs.' Ex. A at 41; Stip. ¶ 5. The facts show that the Money Judgment is based on an award of attorneys' fees pursuant to this default provision. It did not arise by reason of a separate award for alimony, maintenance or support in the parties' matrimonial action. Plaintiff argues therefore that the Money Judgment is not a domestic support obligation, but rather a penalty for not complying with the terms of the Settlement. Adv. Dkt. No.

51 at 11-12. In support of this argument, plaintiff cites *Smith v. Pritchett* (*In re Smith*), 586 F.3d 69 (1st Cir. 2009). In *Smith*, the First Circuit held that a clause in a divorce agreement providing $ 50 per day for late alimony payments was a penalty and not a domestic support obligation. *Id.* at 74-75. The First Circuit reasoned that "the [late] fee was contingent on [the debtor's] tardiness to pay," "was not certain to materialize at all," and was "intended to encourage payment of alimony and was not itself alimony." *Id.* at 75. The $ 50 per diem late fee ***738** in *Smith* was intended to force the debtor to comply with his alimony obligations. Similarly, the reimbursement of legal fees under the default provision in the Settlement was intended to incentivize the parties to fulfill their respective duties under the Settlement. A central fact in *Smith* relevant to plaintiff's argument here was the court's finding that "[l]egal fees incurred in enforcing the agreement, a provision not always contemplated in such contracts, were clearly provided for" by the parties. *Id.* at 75. Thus, the First Circuit distinguished a provision in a divorce agreement that provided for legal fees from a clause that imposes a late payment fee for the failure to timely meet obligations under the agreement. *See id.* The First Circuit's analysis in *Smith* is instructive because the fact that attorneys' fees were separately provided for in the divorce agreement weighed against finding that a late payment fee constituted additional support to the debtor's former spouse. *Id.* Likewise, the default provision in the Settlement that specifically awards Tomor $ 15,000 in attorneys' fees is separate from the provision that provides an award of attorneys' fees under the default provision; the default provision was not designed to support Tomor and/or their children. Defs.' Ex. A at 46. Rather, it was designed to provide the parties with an incentive to timely perform their respective obligations under the Settlement. That fact weighs against a finding that the Money Judgment constitutes a domestic support obligation.

In addition, the Court finds instructive the well-reasoned and thoughtful opinion of Bankruptcy Judge Dorothy Eisenberg in *Gilman v. Golio* (*In re Golio*), 393 B.R. 56 (Bankr. E.D.N.Y. 2008). In *Golio*, the debtor and his former spouse entered into a stipulation of settlement which, among other things, provided that the parties "agree[ ] to indemnify and hold the non-default[ing] party harmless for any and all expenses and/or damage, including reasonable attorneys['] fees and litigation expenses, as a result of his or her breach" of the settlement. *Id.* at 58. The debtor defaulted under his obligations, causing his former spouse to commence proceedings in state court to enforce the agreement. *Id.* at 60. The state court entered a judgment against the debtor awarding his former spouse $ 183,000 in attorneys' fees prior to the debtor filing a chapter 7 bankruptcy petition. *Id.* Judge Eisenberg held that the fees were "clearly incurred in connection with the parties' divorce" and the debtor's ex-spouse was entitled to indemnification under the divorce agreement. *Id.* at 63. In ruling on whether the attorneys' fees were nondischargeable in the debtor's chapter 7 case, Judge Eisenberg found them to be nondischargeable under § 523(a)(15) as a debt incurred in the course of a divorce or separation rather than under § 523(a)(5) as a domestic support obligation. As noted above, the definition of "domestic support obligation" in § 101(14A) includes debts owing to a spouse, former spouse, or child of a debtor that is in the nature of alimony, maintenance, or support. The definition does not include debts arising from a division of marital property under a separation agreement or divorce decree. Those obligations are covered under § 523(a)(15). In a chapter 7 case, § 523(a)(15) excepts from discharge a debt that is not of the kind described in § 523(a)(5) and "owed to a spouse, former spouse, or child of the debtor" that was "incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court record." 11 U.S.C.§ 523(a)(15); *see Golio*, 393 B.R. at 63. Consequently, in holding that the debt at issue was excepted from discharge under § 523(a)(15) as opposed to § 523(a)(5), Judge Eisenberg found that ***739** attorneys' fees awarded to a non-defaulting party pursuant to an indemnification provision in a divorce agreement did not constitute a domestic support obligation. *Golio*, 393 B.R. at 63.

[14] In further support of their argument, defendants cite to cases in which an award for attorneys' fees has been held to be a domestic support obligation. Although the Court agrees with the general premise that attorneys' fees awarded in a pre-petition matrimonial action may under certain circumstances fall within the definition of a domestic support obligation, *see Golio*, 393 B.R. at 61-63, the Court notes that defendants' argument overlooks the basis for the attorneys' fees awarded by the Money Judgment. It is that basis which renders the Money Judgment distinguishable from the case law defendants cite. In *Rogowski*, a debtor's pre-petition obligation to pay his ex-spouse's matrimonial attorneys' fees awarded after a trial concerning various economic issues between the parties was held to be a domestic support obligation. *In re Rogowski*, 462 B.R. 435, 447 (Bankr.

E.D.N.Y. 2011). However, *Rogowski* was rooted in New York Domestic Relations Law. The court in *Rogowski* analyzed New York Domestic Relations Law and found that awards of matrimonial attorneys' fees are only proper if, "at a minimum, ... the former spouse requires financial support." *Id.* at 446. The court found clear evidence the debtor's former spouse required financial support because she had no prospects for work other than part time unskilled jobs and had not worked in her chosen field for over 13 years at the time of divorce, that the debtor was the sole wage earner for the last 12 years of the marriage, and that there was no equitable distribution for either party to leave the marriage with. *Id.* at 446-47. Because New York Domestic Relations Law requires matrimonial attorneys' fees to only be awarded if financial support is required, a proper award of attorneys' fees under that same law "is in the nature of ... support" and satisfies the definition of a domestic support obligation under § 101(14A). *Id.* at 447. That is not the case here. The evidence presented at trial made clear that the attorneys' fees that formed the basis of the Money Judgment were contemplated and agreed upon by Tomor and the plaintiff in the event either of them were to default under the terms of the Settlement; the legal fees at issue were not awarded because they were required for financial support. Defs.' Ex. A at 41; Stip. ¶ 5.

Here, the Court finds no persuasive evidence that the obligation to pay attorneys' fees in this case is in the nature of alimony, maintenance or support. Simply stated, the attorneys' fees awarded to Tomor by reason of plaintiff's noncompliance with his obligations under the Settlement do not come within § 101(14A)'s definition. As noted above, the fees were intended to incentivize the performance by the parties under the Settlement rather than to provide support for Tomor and/or the parties' children.

There are three salient facts that support the Court's finding that plaintiff's obligation to pay attorneys' fees awarded by the Money Judgment is not a domestic support obligation as defined in § 101(14A). First, the default provision in the Settlement was not intended to exclusively benefit Tomor. Rather, the default provision was meant to protect both Tomor and plaintiff in the event either of them defaulted in their respective obligations under the Settlement. In addition, if, hypothetically, Tomor brought suit as the non-defaulting party and did not secure a judgment in her favor, under the terms of the default provision, she would be responsible for plaintiff's attorneys' fees. *See* Defs.' Ex. A at 41. Second, as was the case in ***740** *Smith*, the Settlement contained a separate provision for attorneys' fees incurred by Tomor, not inclusive of those that could potentially be awarded under the default provision. *Smith*, 586 F.3d at 75; Defs.' Ex. A at 46. The fact that the parties already contemplated Tomor's attorneys' fees, irrespective of those in the Money Judgment, weighs against finding the Money Judgment to be a domestic support obligation. *Smith*, 586 F.3d at 75. Lastly, the structure of the Settlement suggests the attorneys' fees are not in the nature of alimony, maintenance, or support because the section in the Settlement that provides for attorneys' fees in the event of a default is separate from the sections that deal with child support, medical coverage, "maintenance/spousal support/alimony," and marital property division. Defs.' Ex. A at 17, 30, 33; *see Romano*, 548 B.R. at 46 (considering the structure of the terms of the final divorce decree to assess whether the parties intended to create a domestic support obligation). As noted, in *Golio*, Judge Eisenberg found an award of attorneys' fees made pursuant to a clause in a divorce agreement similar to the one between plaintiff and Tomor not to be a domestic support obligation for purposes of whether the debt at issue was excepted from discharge under § 523(5). The Court agrees with Judge Eisenberg's rationale and holds that the Money Judgment is not a domestic support obligation, but is instead a debt "incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record." 11 U.S.C. § 523(a)(15); *see Golio*, 393 B.R. at 63.

2. Is Litigating the Contempt Motion "Collection" or "Enforcement"?

[15] Even if the Court had determined that the Money Judgment constitutes a domestic support obligation, the inquiry of whether defendants' conduct is exempt from the automatic stay under § 362(b)(2)(B) would not end there. Identifying the Money Judgment as a domestic support obligation is only the first step in determining whether the exemption applies. The second step is to determine whether the exemption for "the collection of a domestic support obligation" in § 362(b)(2)(B) permits defendants to proceed unimpeded in state court to enforce plaintiff's financial obligation under the Money Judgment. The answer turns on how the term "collection" is construed. In other words, what does the term "collection" mean? Defendants

urge the Court to broadly construe the term "collection" to include proceedings to enforce domestic support obligations, such as contempt proceedings. Adv. Dkt. No. 49 at 4-6. If defendants' reading of the statute is correct, the exception takes hold, and their post-petition conduct with respect to the Contempt Motion is free of the constraints imposed by the automatic stay. Of course, plaintiff disagrees. Plaintiff contends a narrower reading of "collection" is consistent with the express language found in other exceptions to the stay under § 362(b), and that § 362(b)(2)(B) cannot be read to encompass contempt proceedings to enforce domestic support obligations. Adv. Dkt. No. 51 at 5-10. While there is a split of authority on this issue, for the reasons that follow, the Court finds persuasive the reasoning of those courts that adhere to a narrow reading of the term "collection" when determining whether actions to enforce domestic support obligations transgress the automatic stay. The Court agrees with plaintiff's interpretation of § 362(b)(2)(B) that post-petition enforcement of a support obligation through contempt proceedings violates the automatic stay. *See Gorokhovsky v. Ocheretner* (*In re Gorokhovsky*), No. 17-28901-beh, 2018 WL 3325716, at *4 (Bankr. E.D. Wis. July 5, 2018); ***741** *Lori v. Lori* (*In re Lori*), 241 B.R. 353, 354 (Bankr. M.D. Pa. 1999).

[16] **[17]** "No one provision of the Bankruptcy Code can be viewed in isolation from the others; each provision must be construed in the context of the entire statute." *Geron v. Valeray Realty Co., Inc.* (*In re Hudson Transfer Grp., Inc.*), 245 B.R. 456, 460 (Bankr. S.D.N.Y. 2000) (citing *United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assocs.*, 484 U.S. 365, 371, 108 S.Ct. 626, 98 L.Ed.2d 740 (1988)). The Supreme Court has held that "[w]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion." *Russello v. United States*, 464 U.S. 16, 23, 104 S.Ct. 296, 78 L.Ed.2d 17 (1983) (quoting *United States v. Wong Kim Bo*, 472 F.2d 720, 722 (5th Cir. 1972)).

The Court begins its inquiry by looking to the language of § 362(b). *See In re Phillips*, 485 B.R. 53, 56 (Bankr. E.D.N.Y. 2012) (citing *Lamie v. U.S. Trustee*, 540 U.S. 526, 534, 124 S.Ct. 1023, 157 L.Ed.2d 1024 (2004)). Section 362(b)(2)(B)'s exception to the automatic stay applies to "the collection of a domestic support obligation that is not property of the estate." The word "enforcement" is notably omitted from § 362(b)(2)(B), but is included elsewhere in § 362(b). *See* § 362(b)(2)(G), (4), (20), (21), (25)(A), (25)(B). In particular, § 362(b)(2)(G) excepts from the automatic stay "the enforcement of a medical obligation" and § 362(b)(4) excepts "the commencement or continuation of an action or proceeding by a governmental unit ... to enforce such governmental unit's ... police and regulatory power, including the enforcement of a judgment other than a money judgment, obtained in an action or proceeding by the governmental unit." Moreover, § 362(a)(2) clearly stays "the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title" and § 362(a)(4) and (5) stay acts to "enforce" liens against property of the estate and liens that secured claims that arose pre-petition. By omitting "enforcement in § 362(b)(2)(B), but including it in multiple subsections of § 362(a) and (b), it necessarily follows that Congress' exclusion was purposeful and indicative of an intent to differentiate between "collection" and "enforcement." *See Russello*, 464 U.S. at 23, 104 S.Ct. 296; *In re Jenkins*, No. 05-73127, 2011 WL 2619317, at *10 (Bankr. N.D.N.Y. July 1, 2011); *see also* HENRY J. SOMMER & MARGARET DEE MCGARITY, COLLIER FAMILY LAW AND THE BANKRUPTCY CODE ¶ 5.03[3][b][iii] (Matthew Bender) ("Indeed, Congress used the word enforcement specifically in the new section 362(b)(2)(G), relating to medical obligations, which suggests that the failure to broadly permit all other support enforcement was intentional.").

This narrow interpretation of § 362(b)(2)(B) has been followed by numerous courts across the country. *See, e.g.*, *Hass v. Duncan*, No. 1:05cv91(JCC), 2005 WL 5714293, at *2-3 (E.D. Va. July 6, 2005); *Jenkins*, 2011 WL 2619317, at *9-10; *In re Gresham*, No. 06-60027-MHM, 2008 WL 3484318, at *2-3 (Bankr. N.D. Ga. Aug. 12, 2008); *Brooks v. Brooks* (*In re Brooks*), No. 03-3194, 2007 WL 540786, at *3-4 (Bankr. E.D. Tenn. Feb. 15, 2007); *Lori*, 241 B.R. at 354-56. In support of drawing a distinction between "collection" and "enforcement" of domestic support obligations, these courts have looked to *Collier* for guidance.

> Unlike some of the other exceptions to the stay listed in section 362(b), [section 362(b)(2)(B)] did not extend, prior to the 2005 amendments,

> to the commencement ***742** or continuation of proceedings to enforce an obligation. Section 362(b)(2)(B) protects an obligee who receives property that is not property of the estate on a prepetition obligation, for example, through a prior wage attachment, from claims that such receipt is improper. However, this provision did not authorize, prior to the 2005 amendments, enforcement litigation against the debtor without relief from the automatic stay. A separate provision, section 362(b)(2)(A), which grants an exception for the commencement or continuation of an action or proceeding, had been limited to the establishment or modification of an order for alimony, maintenance or support. Proceedings to enforce such orders were conspicuously omitted from the exception and were stayed, except in cases criminal in nature and permitted by section 362(b)(1).

COLLIER ON BANKRUPTCY ¶ 362.05[2] (Richard Levin & Henry J. Sommer eds., 16th ed.) (footnotes omitted). *Collier* further provides that the 2005 amendments to the Bankruptcy Code "added several exceptions permitting the commencement or continuation of certain proceedings related to the enforcement of a domestic support obligation." *Id.* For example, § 362(b)(2)(C) "provides an exception to the stay with respect to the withholding of income that is property of the estate or property of the debtor for payment of a domestic support obligation under a judicial or administrative order or a statute." *Id.*

"Since proceedings to enforce alimony or support orders are normally continuations of earlier proceedings, the absence of language in section 362(b) excepting the continuation of enforcement proceedings from the stay casts significant doubt on whether such proceedings are included in the exception to the automatic stay." COLLIER FAMILY LAW AND THE BANKRUPTCY CODE ¶ 5.03[3][b][iii]. Moreover, *Collier* notes that "[u]nless the word 'collection' is interpreted to encompass the continuation of a proceeding for the purpose of collection, a proceeding to enforce an earlier support or alimony order or agreement is barred by the automatic stay." *Id.* Because other exceptions to the automatic stay "specifically speak of enforcement of judgments, it is unlikely such an interpretation was intended" by Congress regarding § 362(b)(2)(B). *Id.*

However, there are a number of courts that disagree with the *Collier* interpretation of "collection" and interpret "collection" to include "enforcement." *See, e.g.*, *In re Toronto*, No. 15-10663-BAH, 2016 WL 4626108, at *7 n.26 (Bankr. D.N.H. Sept. 2, 2016); *In re Angelo*, 480 B.R. 70, 88-92 (Bankr. D. Mass. 2012); *In re Johnston*, 321 B.R. 262, 276-78 (D. Ariz. 2005); *Lowery v. McIlroy & Millian* (*In re Lowery*), 292 B.R. 645, 649-650 (Bankr. E.D. Mo. 2003). The most thorough analyses of this construction of § 362(b)(2)(B) are set forth in *Johnston* and *Angelo*.

The *Johnston* Court utilized a "plain meaning" interpretation of the word "collection" to critique the *Collier* position—it believed the *Collier* reading of § 362(b)(2)(B) to "stand[ ] or fall[ ]" on whether "collection" is active or passive and if there is any significance to Congress' decision not to use "enforcement" in that subsection. *Johnston*, 321 B.R. at 276-77. Quoting *Webster's Dictionary*, the *Johnston* Court found the plain meaning of "collection" to be the "act of collecting" and "not merely a passive undertaking" as *Collier* suggests. *Id.* at 277. The *Johnston* Court continued, finding it "unlikely that Congress would choose the less common, passive definition [of collection] without making its choice explicit." *Id.*

***743** In a similar vein, the *Angelo* Court fully embraced *Johnston*'s interpretation of § 362(b)(2)(B). *Angelo*, 480 B.R. at 88. The court rejected the argument that collection "means nothing more than 'receiving payment' and does not include contempt process," holding that limiting "collection" to "the passive act of receiving payment is not at all warranted by its ordinary usage." *Id.* at 88-89. Moreover, the court found it to be a misreading of the automatic stay to contend that "collection" and "enforcement" have different meanings and do not overlap. *Id.* at 89. To support its interpretation, the court stated there is intentional overlap in § 362(a) "to put in place a broad and comprehensive stay, one without gaps. To that end, it is comprised not of a single stay but of eight, arrayed in paragraphs (a)(1) through (a)(8), most of

which are themselves comprised of multiple stays. Among the numerous stays that together constitute the automatic stay there exists considerable overlap." *Id.* at 90 (footnotes omitted).

The Court disagrees with the broad interpretation of § 362(b)(2)(B) advanced in *Johnston* and *Angelo*, and adopts the narrow interpretation utilized by *Collier*. "However tempting it may be to unqualifiedly protect a debtor's paramour, spouse, or children, exceptions to the automatic stay must be construed narrowly and relief from the automatic stay is readily available should a creditor choose to pursue that course." *Jenkins*, 2011 WL 2619317, at *10. To read into § 362(b)(2)(B) a broad exception to the automatic stay "would add an exception ... that was clearly not contemplated by Congress." *See In re Weidenbenner*, 521 B.R. 74, 81 (Bankr. S.D.N.Y. 2014) (interpreting § 362(b)(3) narrowly because "[i]t is at odds with the plain language of the Bankruptcy Code to read into the Code an [enormous] exception to the automatic stay ... in the absence of express statutory language"). Congress enumerated 28 exceptions to the automatic stay in § 362(b) and three of those exceptions directly reference domestic support obligations: § 362(b)(2)(A)(ii), (B), and (C). Thus, Congress "knew how to create exceptions to [the] automatic stay and chose not to" create an exception specifically for the enforcement of domestic support obligations. *See id.* For these reasons, a rejection of the plain meaning argument of "collection" advanced in *Johnston* and its progeny is consistent with the statutory scheme of the automatic stay. To hold otherwise would strain the text of § 362(b)(2)(B) and lead to a departure from the traditional methods of collection of domestic support obligations such as wage garnishment and receipt of payments from non-estate property—neither of which Seidemann sought to do. COLLIER FAMILY LAW AND THE BANKRUPTCY CODE 5.03[3][a][i]; Tr. 216:9-13. Accordingly, the Court finds that even if the Money Judgment constitutes a domestic support obligation, defendants violated the automatic stay because litigating the Contempt Motion was the "enforcement" of a domestic support obligation, which is not excepted pursuant to § 362(b)(2)(B) as "collection."

E. Did Defendants Willfully Violate the Automatic Stay?

Having found the automatic stay was violated under § 362(a), and that the exemption under § 362(b)(2)(B) is not applicable, the Court now considers whether sanctions should be imposed against defendants pursuant to § 362(k). In resolving this question, the Court first considers the legal principles applicable to § 362(k), and then addresses plaintiff's arguments that defendants willfully violated the automatic stay.

[18] **[19]** **[20]** **[21]** Section 362(k) creates "a private right to sue for damages on behalf of ***744** an individual injured by a willful violation of the automatic stay." *In re Ampal-Am. Isr. Corp.*, 502 B.R. 361, 370 (Bankr. S.D.N.Y. 2013). "An individual injured by any willful violation of a stay ... shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages." 11 U.S.C. § 362(k)(1). " 'Willful' means 'any deliberate act taken in violation of a stay, which the violator knows to be in existence.' " *In re Sturman*, No. 10 Civ. 6725 (RJS), 2011 WL 4472412, at *2 (S.D.N.Y. Sept. 27, 2011) (quoting *Crysen/Montenay*, 902 F.2d at 1105). "A specific intent to violate the stay is not required; instead, general intent in taking actions which have the effect of violating the automatic stay is sufficient to warrant damages." *Jean-Francois*, 532 B.R. at 454 (quoting *Ampal*, 502 B.R. at 373); *see also Weber v. SEFCU* (*In re Weber*), 719 F. 3d 72, 82 (2d Cir. 2013) ("A creditor willfully violates section 362 when it knows of the filing of the petition (and hence of the automatic stay), and has the general intent simply to perform the act found to violate section 362; no specific intent to violate section 362 is necessary."). "A good faith belief in a right to the property is not relevant to a determination of whether the violation was willful." *In re Gilford*, 567 B.R. 412, 417 (Bankr. E.D.N.Y. 2017) (quoting *Fleet Mortg. Grp. v. Kaneb*, 196 F.3d 265, 268-69 (1st Cir. 1999)).

[22] **[23]** **[24]** Where a violation of the stay is willful, § 362(k) mandates an award of actual damages. Whether to assess punitive damages lies within the discretion of the Court. "An additional finding of maliciousness or bad faith on the part of the offending creditor warrants the further imposition of punitive damages ...." *Crysen/Montenay*, 902 F.2d at 1105; *see also Ebadi*, 448 B.R. at 320 ("Punitive damages ... are only appropriate where the stay violation was conducted in bad faith, with malice, or in a particularly egregious manner." (citing *Prusan*, 495 B.R. at 207)).

[25] At trial, Seidemann disputed that he had actual knowledge of plaintiff's bankruptcy case on December 3,

2013, the date the chapter 7 petition was filed. *See* Tr. 133:15-25, 134:1-6. Seidemann testified he was not in his office that day to receive the letter Kanter sent him via fax which expressly stated that the automatic stay was in effect due to plaintiff's having commenced a bankruptcy case. Pl.'s Ex. 9; Tr. 134:18-135:14. However, Seidemann admitted he did see the letter on December 9. Tr. 255:10-12. Seidemann also testified that he received a telephone call, during which he "was advised that an attorney was retained by Mr. Grinspan to file bankruptcy on his behalf." Tr. 134:2-3. While Seidemann's testimony relating to this phone conversation indicates he had notice that plaintiff intended to file for bankruptcy relief, an indication that a bankruptcy may be filed is insufficient to constitute actual notice for purposes of a willful stay violation. *Prusan*, 495 B.R. at 207.

[26] Even if Seidemann did not have actual knowledge of the bankruptcy petition on its filing date, as mentioned above, Seidemann did have actual knowledge of plaintiff's filing, and consequently the automatic stay, as early as the date of the Contempt Motion hearing on December 5, 2013. He testified that he believed the stay was "inapplicable" from December 3, 2013 onwards because the Money Judgment was a domestic support obligation and that the bankruptcy filing "gave [him] pause as to how to deal with monetary issues" before he proceeded to court on December 5. Tr. 167:21-25, 188:2-8. Seidemann contends that Judge Maron found that the Money Judgment was a domestic support obligation – he testified that Judge Maron ***745** "affirmatively [told him] that [the Money Judgment] is a domestic support order" and that he was asked to submit a proposed order reflecting as such. Adv. Dkt. No. 2-12; Tr. 220:24-221:5. Defendants did not produce a transcript of any hearing at which Judge Maron made such a ruling. Additionally, despite this purported directive, Seidemann knew that Judge Maron did not sign any proposed order nor issue a written opinion concluding that the Money Judgment was a domestic support obligation. Tr. 176:7. The evidence introduced at trial establishes that Seidemann had actual knowledge of the bankruptcy filing and decided to take steps post-petition to enforce the Money Judgment via the Contempt Motion. Despite the bankruptcy filing, he sought to have the Contempt Motion granted in its entirety. Based on the trial record, the Court finds that Seidemann had the requisite general intent to take actions that had the effect of violating the stay under § 362(k). *See Beckford v. Romano* (*In re Beckford*), 572 B.R. 61, 68-69 (Bankr. D. Conn. 2017); *Sucre*, 226 B.R. at 349. That is sufficient to warrant damages under § 362(k). *See Jean-Francois*, 532 B.R. at 454.

[27] Because the Court finds defendants willfully violated the automatic stay, an award of actual damages incurred by plaintiff is mandated by § 362(k)(1). *Gilford*, 567 B.R. at 416; *see also Crysen/Montenay*, 902 F.2d at 1105 ("[A]ny deliberate act taken in violation of the stay, which the violator knows to be in existence, justifies an award of actual damages."). Actual damages include attorneys' fees and costs that are reasonable and necessary. *Prusan*, 495 B.R. at 208. Here, plaintiff was required to appear and act in both this Court and state court to enforce the automatic stay. *But see id.* (holding debtor suffered no actual damages because he did not have to defend himself in state court proceedings regarding a contempt motion and did not have to bring an adversarial proceeding in the bankruptcy court to enforce the automatic stay). The Court reserves judgment on actual damages pending submission of supplemental briefing. [4]

[28] As for plaintiff's request for an award of punitive damages, the evidence presented at trial, including the testimony of Seidemann, does not support a finding that defendants acted with malice or in bad faith. While Seidemann could have prevented this outcome by simply asking this Court for relief from the automatic stay before unilaterally deciding to continue with the state court proceeding, a "callous disregard" for the automatic stay is insufficient to support a finding of bad faith. *Beckford*, 572 B.R. at 68-69. Accordingly, the Court does not find Seidemann's actions constituted "aggravated circumstances that would warrant punitive damages." *In re Velichko*, 473 B.R. 64, 70 (Bankr. S.D.N.Y. 2012); *see Jean-Francois*, 532 B.R. at 457-59; *Ebadi*, 448 B.R. at 320.

F. Plaintiff's Request for a Permanent Injunction

Plaintiff also asks the Court to permanently enjoin defendants from enforcing the Money Judgment and compelling plaintiff to answer the Information Subpoena. Adv. Dkt. No. 51 at 1. The Court need not address plaintiff's request for permanent injunctive relief because Seidemann withdrew the Contempt Motion, plaintiff answered the Information Subpoena, and the Money Judgment was vacated ***746** by the state court. Moreover, there is nothing in the trial record to support a finding that Seidemann will file another contempt motion

seeking to relitigate issues regarding the Money Judgment or Information Subpoena. Tr. 247:20-248:2.

III. Conclusion

For the foregoing reasons, the Court finds that plaintiff has proven by a preponderance of the evidence that defendants willfully violated the automatic stay. Having determined that a willful violation of the stay occurred, the Court reserves judgment on actual damages pending submission of supplemental briefing. The Court will issue a separate order setting forth a briefing schedule and a hearing date on actual damages. No other or further damages are appropriate. Plaintiff's request for a permanent injunction is dismissed as moot.

SO ORDERED.

All Citations

597 B.R. 725

Footnotes

1 All statutory references to sections of the United States Bankruptcy Code, 11 U.S.C. § 101 *et seq.*, will hereinafter be referred to as "§ (section number)".

2 For convenience, the Court will refer to filings in the adversary proceeding as "Adv. Dkt. No. __" and filings in the lead bankruptcy case as "Dkt. No. __". The Court will also refer to the trial transcript [Adv. Dkt. No. 55] as "Tr.", exhibits as "Ex. __", and the parties' stipulated facts set forth in their joint pre-trial memorandum [Adv. Dkt. No. 48] as "Stip. ¶ __".

3 Although not argued by the parties, for the sake of completeness, the Court also considers whether defendants' actions were excepted from the automatic stay pursuant to § 362(b)(1) as the continuation of a criminal action. At trial, the contempt motion was referred to as both civil and criminal in nature. Tr. 21:7-8, 203:18. However, the language appearing on the face of the Contempt Motion is required by N.Y.C.P.L.R. § 756 for civil contempt and the type of relief sought was to vindicate Tomor's private rights under her divorce agreement with plaintiff, which is indicative of civil contempt, as opposed to the vindication of an offense against the public, which is indicative of criminal contempt. *In re White*, 478 B.R. 177, 182 (Bankr. S.D.N.Y. 2012). Accordingly, the Contempt Motion in the instant case is an action for civil contempt, which falls beyond the scope of § 362(b)(1). *See id.* at 183-84.

4 At trial, the parties agreed not to introduce evidence as to whether plaintiff incurred actual damages unless the Court determined that defendants willfully violated the automatic stay. Tr. 61:8-64:24.

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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NEW YORK

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In re

Joseph Yerushalmi,

Debtor.

----------x

Case No.: 8-07-72816-las

Chapter 7

MEMORANDUM DECISION AND ORDER

Introduction

The United States of America, on behalf of the Internal Revenue Service ("IRS"), moved pursuant to 11 U.S.C. § 362(d)(1) for entry of an order vacating the automatic stay imposed in this chapter 7 case under 11 U.S.C. § 362(a)[1] to permit the IRS to commence proceedings in the United States Tax Court ("Tax Court") to fix the amount of the debtor's alleged income tax liability for tax years 1999 and 2000 [dkt. no. 234]. Debtor opposed that motion [dkt. no. 238]. The Court heard oral argument on the motion and entered a conditional order ("Conditional Order") [dkt. no. 240] granting the IRS relief from the automatic stay. In sum, the Conditional Order allowed the IRS to litigate the debtor's alleged income tax liability before the Tax Court unless debtor filed a complaint against the IRS in this Court or otherwise challenged the IRS' proofs of claim within 30 days of the entry of the Conditional Order. In accordance with the Conditional Order, debtor timely filed an objection to claim numbers 2, 10 and 17 filed by the IRS ("Claims Objection") [dkt. no. 241].

In response to the Claims Objection, the United States moved for the entry of an order (i) dismissing the Claims Objection or, in the alternative, (ii) (a) modifying the Conditional Order to remove the provision allowing debtor to commence an adversary proceeding in this

[1] All statutory references to sections of the United States Bankruptcy Code, 11 U.S.C. § 101 *et seq.*, will hereinafter be referred to as "§ (section number)".

Court against the IRS or otherwise challenge the IRS' proofs of claim within 30 days of entry of the Conditional Order, (b) abstaining from hearing the tax dispute in this Court, and (c) vacating the automatic stay imposed under § 362(a) to permit the running of the statutory 150-day period ("150-day Period") under section 6213(f)(1) of the United States Internal Revenue Code of 1986, as amended, 26 U.S.C. § 1 et seq. ("IRC")[2], during which debtor may petition the Tax Court for a redetermination of the IRS' proposed assessment of debtor's alleged income tax liability ("Motion to Dismiss Claims Objection") [dkt. no. 244]. Debtor opposed that motion [dkt. no. 247], and the United States replied [dkt. no. 249]. Shortly after the filing of the Motion to Dismiss Claims Objection, the chapter 7 trustee sought approval of a stipulation between the trustee, on behalf of the debtor's bankruptcy estate, and the IRS vacating the automatic stay to permit debtor's alleged income tax liability to be determined in the Tax Court [dkt. no. 246]. Debtor opposed the stipulation [dkt. no. 250]. The trustee subsequently withdrew his application seeking approval of the stipulation.

In addition to the Motion to Dismiss Claims Objection, the United States separately moved for entry of an order vacating the automatic stay for cause under § 362(d)(1) to allow the running of the 150-day Period whether or not this Court abstains from hearing the tax dispute or decides to hear and determine the tax liability at issue ("Third Stay Relief Motion") [dkt. no. 253]. Debtor also opposed that motion [dkt. no. 254].

Thereafter, the trustee filed a motion objecting to proofs of claim 2, 10 and 17 filed by the IRS [dkt. 304] and moved for approval of a stipulation between the bankruptcy estate and the IRS settling the trustee's claims objection [dkt. no. 318]. The settlement stipulation provided, *inter alia*, for the withdrawal of the trustee' s claims objection, and the joinder by the trustee in the United States' motion for relief from the automatic stay to permit the

[2] All statutory references to the Internal Revenue Code will be hereinafter be referred to as "IRC § (section number)".

running of the 150-day Period. Debtor opposed the trustee's motion to approve the settlement stipulation [dkt. no. 325] and the trustee replied [dkt. nos. 326, 328], as did the United States [dkt no. 327]. After consideration of the parties' submissions, the Court entered an order authorizing the trustee to enter into the settlement stipulation with the IRS [dkt. no. 330].

Currently pending before the Court are the United States' motion to dismiss debtor's objection to the IRS' proof of claim and its motion for relief from the automatic stay to allow commencement of the 150-day Period. The Court heard oral argument over several days and the parties submitted supplemental papers on issues raised at oral argument. The Court has considered carefully all of the arguments and submissions made by the parties in connection with the motions. For the following reasons, the Motion to Dismiss Claims Objection is denied in part and granted in part, and the Third Stay Relief Motion is denied as moot.

Jurisdiction

The Court has jurisdiction over this matter under 28 U.S.C. § 1334(b) and the Standing Order of Reference entered by the United States District Court for the Eastern District of New York pursuant to 28 U.S.C. § 157(a), dated August 28, 1986, as amended by Order dated December 5, 2012, effective *nunc pro tunc* as of June 23, 2011. This is a core proceeding under 28 U.S.C. § 157(b)(2)(A), (B), (G), and (O) in which final orders or judgment may be entered by this Court pursuant to 28 U.S.C. § 157(b)(1).

Background and Procedural History[3]

a. Bankruptcy Filing by Debtor and Yerushalmi & Associates LLP

Debtor, a tax attorney in his late seventies, held a 99% interest in the law firm of Yerushalmi & Associates ("Y&A"). Debtor and Y&A each filed a petition under chapter 11 of

[3] Familiarity with the facts of this long-running bankruptcy case is presumed. Accordingly, the Court recites only those facts that are pertinent to the resolution of the pending motions. Unless otherwise noted, the relevant facts are undisputed.

the Bankruptcy Code on July 25, 2007. Debtor's chapter 11 case was converted to a chapter 7 case on October 2, 2007 [dkt. no. 63] and Marc A. Pergament was appointed the chapter 7 trustee of the debtor's bankruptcy estate [dkt. no. 65]. Y&A's chapter 11 case was converted to a chapter 7 case on October 2, 2007 and was closed on May 16, 2017. *See* bankruptcy case no. 8-07-72817, dkt. nos. 65, 179.

b. IRS Proofs of Claim

On August 23, 2007, the IRS filed a proof of claim in the amount of $16,650 for income taxes owed for the period ending March 31, 2007 ("Claim No. 2"). Claim No. 2 asserts an unsecured priority tax claim under § 507(a)(8) in the amount of $15,000, plus prepetition interest of $1,550, for a total sum of $16,550, and a general unsecured claim of $100 for penalties, including interest thereon.

On November 28, 2007, the IRS filed an amended proof of claim in the amount of $1,425,536.47 ("Claim No. 10"). Claim No. 10 asserted an unsecured priority tax claim under § 507(a)(8) in the amount of $1,286,434.27, and a general unsecured claim of $139,102.20 for penalties and interest. In addition to the $16,500 asserted in Claim No. 2, Claim No. 10 included (1) a tax assessment for the tax period ending March 31, 1999 in the amount of $587,196, plus prepetition interest of $498,076.76, for a total of $1,085,272.76 and (2) a tax assessment for the tax period ending March 31, 2000 in the amount of $107,815, plus prepetition interest of $76,796.51, for a total of $184,611.51.

On October 4, 2008, the IRS filed an amended proof of claim in the amount of $1,459,673.32 ("Claim No. 17"). Claim No. 17, now the operative claim asserted by the IRS, is based on an unsecured priority tax claim under § 507(a)(8) in the sum of $1,319,993.30, and a general unsecured claim of $139,740.02. Under Claim No. 17, the assessments with respect to the 1999 and 2000 tax years remain the same but the taxes due with respect to the

2007 tax year increased from $15,000 to $49,188.25, and the prepetition interest decreased from $1,500 to $860.78.

c. Statutory Notice of Deficiency and Malka Yerushalmi's Tax Proceeding

On December 7, 2007, the IRS issued a statutory notice of deficiency to debtor and his estranged wife, Malka Yerushalmi ("Malka"), for tax years 1999 and 2000 ("Statutory Notice of Deficiency"). In question are certain net operating losses claimed by debtor and Malka in their joint tax returns with respect to debtor's law practice at Y&A. The net operating losses allegedly arose out of a theft by a family friend who had access to debtor's office space at Y&A and debtor's records and financial information even though the friend was not an employee of debtor or Y&A.

Pursuant to IRC § 6213, a taxpayer has 90 days after the IRS mails a statutory notice of deficiency to file a petition with the Tax Court for a redetermination of the deficiency (the "90-day Period"). 26 U.S.C. § 6213(a). By statute, no assessment of a deficiency and no levy or proceeding to collect upon the deficiency shall be instituted or prosecuted until the statutory notice of deficiency has been mailed and the 90-day Period has expired. 26 U.S.C. § 6213(a). If a petition is filed by the taxpayer with the Tax Court within the 90-day Period, then no assessment of a deficiency and no levy or proceeding can be instituted until the Tax Court's decision becomes final. *Id.*

The 90-day Period was affected by the commencement of debtor's bankruptcy case as the filing of a bankruptcy petition triggers the automatic stay under § 362(a). Relevant here is § 362(a)(8) which enjoins:

> the commencement or continuation of a proceeding before the United States Tax Court . . . concerning a tax liability of a debtor that is an individual for a taxable period ending before the date of the order for relief under this title.

11 U.S.C. § 362(a)(8). Because it is only the taxpayer who may petition the Tax Court for a redetermination of a deficiency assessment under IRC § 6213(a), § 362(a)(8) essentially bars an individual debtor from commencing a proceeding before the Tax Court to determine a prepetition tax liability until the automatic stay is no longer in place under § 362(c)(2)[4] or the stay is lifted under § 362(d).[5] As a result of the automatic stay, Congress not only tolled the number of days left within the 90-day Period at the time of the bankruptcy filing but also extended the time for a debtor to petition the Tax Court by an additional 60 days after the automatic stay ends, so as to give a debtor additional time to decide whether to contest the statutory notice of deficiency by filing a petition with the Tax Court. 26 U.S.C. § 6213(f)(1).[6] Thus, where a statutory notice of deficiency is issued during the pendency of a bankruptcy case, as in the case before this Court, a debtor-taxpayer will have a maximum of 150 days, i.e., the 150-day Period, after the automatic stay has been modified or terminated to petition the Tax Court for a redetermination of a deficiency before any assessment, levy or collection by the IRS may be made.

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[4] Section 362(c)(2) provides that the automatic stay continues until the earliest of the closing of the case, the dismissal of the case, or, with respect to an individual chapter 7 debtor, the time a discharge is granted or denied. 11 U.S.C. § 362(c)(2).

[5] A pre-BAPCPA case has held that the automatic stay under § 362 is designed to protect the debtor and provide the debtor with relief from the pressure and harassment by creditors attempting to collect a debt but a debtor's decision to proceed in the Tax Court rather than before the Bankruptcy Court is not covered by the stay under § 362(a)(8). *Thompson v. United States (In re Thompson)*, 241 B.R. 920, 921 (Bankr. S.D. Ga. 1999). However, given that only a debtor-taxpayer can file a petition to commence a proceeding before the Tax Court, arguably § 362(a)(8) would also stay the debtor from filing a petition with the Tax Court.

[6] IRC § 6213(f)(1) provides as follows:

> (f) Coordination with Title 11. –
> (1) Suspension of running of period for filing petition in Title 11 cases. – In any case under Title 11 of the United States Code, the running of the time prescribed by subsection (a) for filing a petition in the Tax Court with respect to any deficiency shall be suspended for the period during which the debtor is prohibited by reason of such case from filing a petition in the Tax Court with respect to such deficiency, and for 60 days thereafter.

Since debtor's bankruptcy filing, the IRS has been stayed from taking any action outside this Court to levy or collect on the taxes allegedly owed by debtor. The bankruptcy case has not been dismissed or closed and as a result of an accounting action between the debtor and his former law partner pending in New York state court, no determination has been made regarding whether debtor is entitled to a discharge[7]. In addition, because debtor has not sought relief from the automatic stay to petition the Tax Court for a redetermination of the tax assessments made by the IRS, the time for debtor to petition the Tax Court in response to the Statutory Notice of Deficiency has yet to run.

Malka, against whom the Statutory Notice of Deficiency was also issued for the same tax debt allegedly owed by debtor, did not file for bankruptcy relief. Therefore, the 90-day Period was not tolled vis-a-vis Malka. On March 4, 2008, within the requisite 90-day Period, Malka commenced an action in Tax Court, *Malka Yerushalmi, Petitioner v. Commissioner of Internal Revenue, Respondent.*, No. 5520-08 ("Malka Tax Proceeding"). In that action, Malka seeks innocent spouse relief pursuant to IRC § 6015 claiming that assessments for the tax years 1999 and 2000 relate mainly to debtor's deductions for net operating losses arising from his law practice. Shortly thereafter, debtor filed a Notice of Intervention in the Malka Tax Proceeding arguing that the automatic stay was in effect by reason of his bankruptcy filing. The Tax Court amended the caption in the Malka Tax Proceeding to read "*Malka Yerushalmi, Petitioner, and Joseph Yerushalmi, Intervenor v. Commissioner of Internal Revenue, Respondent.*"

[7] An adversary proceeding commenced by debtor's former law partner (Amnon Shiboleth) and his former law firm objecting to debtor's discharge under § 727 and dischargeability of debt under § 523 has been held in abeyance pending the outcome of the accounting action. *See* Adv. Pro. No. 8-08-8037. Counsel for debtor and counsel for debtor's former law partner and former law firm have each filed multiple letters reporting on the status of the accounting action.

On January 26, 2009, Malka and the United States moved in Tax Court to continue the Malka Tax Proceeding asserting that the Tax Court should first determine the amount of the deficiency, if any, before addressing the issue of Malka's eligibility for innocent spouse relief. The Tax Court agreed and granted the motion on January 20, 2009. Despite this ruling, the Tax Court could not proceed with a determination of the alleged deficiency because debtor did not file a petition with the Tax Court for a redetermination of the IRS assessment; he just moved to intervene.

From time to time during 2009 and 2010, Malka and the United States renewed their motion to continue the Malka Tax Proceeding. Each time, debtor opposed asserting that while he disagrees with the calculations in the Statutory Notice of Deficiency, he is precluded by the automatic stay under § 362(a)(8) from challenging those assessments in Tax Court. Although debtor could have sought relief from the automatic stay to petition the Tax Court, he did not do so. Since 2010, debtor has provided the Tax Court with periodic updates on his bankruptcy case claiming that he did not foresee it ending any time soon. Thus, because debtor has been steadfast in his refusal to seek stay relief in this Court and petition the Tax Court for a redetermination of the challenged assessments, the Malka Tax Proceeding has been brought to a halt.

d. The United States' First Stay Relief Motion

Given inaction on debtor's part to seek relief from stay, the United States, acting on behalf of the IRS, moved for stay relief under § 362(d)(1) to permit the IRS to determine debtor's income tax liability for tax years 1999 and 2000 in Tax Court and for the Malka Tax Proceeding to continue (the "First Stay Relief Motion") [dkt. no. 210]. Debtor opposed that motion [dkt. no. 214]. In his opposition, debtor asserted that a tax audit by the IRS was pending at the time of his bankruptcy filing, and that he and the IRS were attempting to reach agreement on the outstanding issues before the case would be scheduled for an IRS

administrative appeal. While debtor did not oppose the lifting of the stay to allow the transfer of the audit to the IRS administrative appeal, he did take exception to having his alleged income tax liability determined by the Tax Court. The debtor made clear that this Court was the preferred choice to resolve his income tax liability. As for the United States' request to continue the Malka Tax Proceeding, debtor was not opposed to continuing that proceeding because he claimed that Malka only requested innocent spouse relief and not redetermination of the tax deficiencies and penalties set forth in the Statutory Notice of Deficiency, nor did she raise any defense to the substance of the Statutory Notice of Deficiency. From the debtor's viewpoint, the continuance of the Malka Tax Proceeding itself would not determine debtor's own tax liability.

At the hearing on the First Stay Relief Motion, debtor and the United States informed the Court that the motion was resolved and they subsequently submitted a stipulation (the "Stay Relief Stipulation") agreeing that "the automatic stay pursuant to § 362(d) should be lifted for purposes of permitting the continuation of the Tax Court proceedings in Docket No. 5520-08". The Court approved the Stay Relief Stipulation [dkt. no. 217]. However, because Docket No. 5520-08 relates only to the Malka Tax Proceeding, the Stay Relief Stipulation did not modify the automatic stay to allow debtor to petition the Tax Court for a determination of his tax liability. In sum, the Stay Relief Stipulation did not affect the Malka Tax Proceeding because the Tax Court was not, in the first instance, prohibited from proceeding on Malka's innocent spouse defense.

e. The United States' Second Stay Relief Motion

Because the Stay Relief Stipulation did not permit the IRS to proceed in Tax Court for a determination of debtor's income tax liability, the United States, acting on behalf of the IRS, filed a second motion seeking stay relief for cause to permit debtor to petition the Tax Court to allow for a determination in that forum of both his and Malka's income tax liability

for tax years 1999 and 2000 (the "Second Stay Relief Motion") [dkt. no. 234]. In so moving, the United States anticipates that if debtor petitions the Tax Court, then debtor's tax case and the Malka the Tax Proceeding will be consolidated for trial. In the motion, the United States argued that even though this Court has jurisdiction under § 505 to determine debtor's federal income tax liability for the tax years 1999 and 2000, this Court should abstain (i) in the interest of judicial economy and avoidance of inconsistent rulings by this Court and the Tax Court, and (ii) because of the Tax Court's expertise in the handling the complex tax laws at issue.

Debtor filed opposition to the Second Stay Relief Motion [dkt. no. 238] asserting that the motion was filed in violation, and in contravention, of the Stay Relief Stipulation which settled the United States' First Stay Relief Motion and limited stay relief only to the Malka Tax Proceeding. Debtor also claimed that if the tax dispute were litigated in this Court, he is confident that he will rebut the *prima facie* validity of the IRS' proof of claim and, in debtor's view, the burden would then shift to the United States to prove that debtor's loss deductions were improper. He contrasts this shifting burden of proof with what he perceives would be the allocation of the burden of proof in Tax Court. Debtor asserts that in Tax Court he bears the burden of proof as to the validity of his claimed loss deductions.

The Court heard oral argument on the Second Stay Relief Motion and, after careful consideration of the parties' submissions, determined that debtor cannot hide behind the automatic stay and refuse to address his alleged prepetition income tax liability while the bankruptcy case lingers. Accordingly, the Court entered the Conditional Order granting the United States' Second Stay Relief Motion. As noted above, in sum, the Conditional Order allowed the IRS to commence proceedings before the Tax Court unless debtor filed a complaint against the IRS in this Court or otherwise challenged the IRS' proof of claim within

30 days of the entry of the Conditional Order. Debtor timely filed his objection to the IRS' proof of claim. *See* Claims Objection [dkt. no. 241].

f. The United States' Motion to Dismiss Claims Objection

The United States, acting on behalf of the IRS, moved to dismiss the claims objection [dkt. nos. 244, 245]. In its motion, the United States asserts that only the chapter 7 trustee has the requisite standing to object to claims in the absence of any surplus in estate funds that would be distributed to debtor by reason of a successful objection to the IRS' proof of claim. In the alternative, the United States argues that this Court should (i) abstain from determining debtor's income tax liability in favor of the Tax Court, (ii) remove the provision in the Conditional Order that allowed debtor to file the Claims Objection, and (iii) lift the automatic stay to allow the clock to run on the 150-day Period.

Debtor filed opposition to the Motion to Dismiss Claims Objection [dkt. no. 247] arguing that both the "so ordered" Stay Relief Stipulation that settled the First Stay Relief Motion and the Conditional Order are final orders which the United States failed to appeal or move to reconsider on a timely basis. Debtor also points to the express language of the Conditional Order and contends that by allowing him to otherwise challenge the IRS' proof of claim, this Court tacitly found that it has jurisdiction over his tax liability. As to the issue of standing to file objections to claims in a chapter 7 bankruptcy case, debtor argues that because the trustee failed to object to proofs of claim he has abandoned the right to object to any proofs of claim[8]. In addition, debtor asserts he has standing to object to proofs of claim under § 502 because (1) the bankruptcy estate will likely have a surplus once certain claims are disallowed or reduced and (2) the IRS tax claim may be nondischargeable. Debtor further

[8] As noted above, the trustee subsequently filed various objections to proofs of claim, including the IRS' proof of claim, and reached a settlement with the IRS whereby he agreed to withdraw his objection to the IRS' proof of claim and join the United States' motion to lift the stay with respect to the 150-day Period and for this Court to abstain from determining the tax dispute. The settlement agreement was approved by the Court. [dkt. no. 318].

contends that the IRS has not yet completed its audit and that he is entitled to a refund. Last, but not least, debtor argues that this Court should not abstain because the Tax Court would, allegedly, be biased in favor of the IRS, and a determination by this Court of the purported tax liability would be faster.

The United States replied [dkt. no. 249] arguing that, at minimum, the automatic stay should be modified to permit the 150-day Period to run. By allowing the 150-day Period to run, the IRS can make a final assessment of the taxes even if debtor chooses not to proceed in Tax Court. Although § 362(b)(9)(D) permits a governmental agency to continue making assessments notwithstanding the imposition of the automatic stay, IRC § 6213 prohibits an assessment until the taxpayer has an opportunity to petition the Tax Court. While debtor insists that the stay be lifted only to permit him to continue with an administrative appeal before the IRS, the United States explains that this option is not possible without first submitting to the jurisdiction of the Tax Court. The United States claims that if debtor does not intend to file a petition with the Tax Court, then the 150-day Period should be allowed to run because there is no reason to continue to hold the IRS's final assessment at bay, and the IRS will still be enjoined from any collection activity absent a further modification of the automatic stay by this Court.

The United States also disputes that it conceded to having this Court determine debtor's tax liability when it entered into the Stay Relief Stipulation resolving the First Stay Relief Motion. It always has been the intention of the United States that the tax dispute be heard by the Tax Court. The United States admits that it was mistaken when it thought that the lifting of the stay to continue the Malka Tax Proceeding would also permit the IRS to determine debtor's tax liability for the tax years 1999 and 2000. The United States argues that while the Court may have exclusive jurisdiction over its own orders, the Court does not have exclusive jurisdiction over the outstanding tax issues, and the Stay Relief Stipulation

does not preclude the Court from abstaining in favor of the Tax Court. Moreover, the United States argues that parties cannot, on their own, confer jurisdiction onto a court by agreement.

As to debtor's argument on standing to object to claims, the United States asserts that it is unlikely that the estate will have a surplus given the amount of the claims filed in this bankruptcy case and the judgment entered in New York state court against debtor and in favor of his former law partner. As to debtor's claim of nondischargeability as an alternative basis for standing, the United States contends that certain courts have abstained from determining the amount of a nondischargeable debt where no bankruptcy purpose is served by such litigation. This is especially so, the United States argues, where there will be no surplus funds available for distribution to a chapter 7 debtor. Otherwise, a debtor would be able to engage in forum shopping simply because he or she prefers to litigate tax disputes in the Bankruptcy Court rather than in the Tax Court, the United States District Court, or the Court of Federal Claims, which the United States contends, also have jurisdiction to hear and determine tax disputes.

g. The United States' Third Stay Relief Motion and Supplemental Briefs

While the Claims Objection and the Motion to Dismiss Claims Objection were pending, the United States, acting on behalf of the IRS, filed the Third Stay Relief Motion [dkt. no. 253] again seeking relief from stay, for cause, to permit the 150-day Period to run regardless of whether debtor wishes to avail himself of the Tax Court's jurisdiction and whether this Court exercises jurisdiction over debtor's objection to the allowance of the IRS' proof of claim. Although the United States requested the very same stay relief in its Motion to Dismiss Claims Objection, it nevertheless filed the Third Stay Relief Motion in the event this Court required that a request for stay relief be made by separate motion. In response, debtor filed a letter with the Court [dkt. no. 254] objecting to the Third Stay Relief Motion as an improper fourth attempt by the United States to seek stay relief, and demanded that the

United States withdraw the Third Stay Relief Motion or debtor would seek the imposition of sanctions. In his letter, debtor also reiterated the arguments raised in his opposition to the Motion to Dismiss Claims Objection. Meanwhile, the trustee filed a statement [dkt. no. 255] indicating that he does not oppose the stay relief requested by the United States.

After hearing the arguments of counsel, the Court determined that a further hearing on the Motion to Dismiss Claims Objection and the Third Stay Relief Motion was necessary to consider whether (1) debtor has standing to object to the IRS' proof of claim and (2) the Court should abstain from hearing and determining the tax dispute, and lift the automatic stay for the limited purpose of permitting debtor to petition the Tax Court, i.e., allowing the 150-day Period to commence. The Court also directed the parties to file supplemental papers on issues raised at the hearing.

In its supplemental brief [dkt. no. 274], the United States reiterated many of the same arguments it previously raised in its reply to debtor's opposition to the Motion to Dismiss Claims Objection, including the abstention argument. In his supplemental brief [dkt.no. 284], debtor likewise repeated arguments he previously raised in his opposition to the Motion to Dismiss Claims Objection and in his opposition to the Third Stay Relief Motion regarding, among other things, the finality of both the Stay Relief Stipulation and the Conditional Order, the jurisdiction of this Court to hear and determine the tax dispute, debtor's standing, and why this Court should not abstain.

Following submission of the supplemental papers, the Court held a hearing to consider the parties' arguments on standing, abstention and the United States' motion to lift the stay. At that hearing, the United States advised that an appeal was pending before the Court of Appeals for the Second Circuit in *In re Drake*, Case No. 15-0013, in which the United States took the position that the nondischargeability of a tax debt does not give a chapter 7 individual debtor standing to challenge the IRS' proof of claim. The Court provided debtor an

opportunity to review the papers submitted in the *Drake* appeal and asked the parties to submit additional papers on the issue.

The United States submitted its post-hearing brief [dkt. no. 293] which in the main argues that a debtor's interest in reducing nondischargeable liabilities is insufficient to confer standing on a debtor to object to claims in his or her bankruptcy case. As to debtor's argument that standing is conferred by reason of an anticipated surplus of funds in the estate after payment in full of all creditor claims, the United States contends that resolution of the trustee's objections to various claims may take a substantial amount of time, and therefore, this Court should abstain and lift the stay to allow debtor to petition the Tax Court if he wants to challenge the IRS' proof of claim. If debtor is not going to petition the Tax Court, the United States argues that it is highly prejudicial to continue to stay the running of the 150-day Period. The United States also contends that the burden of proof on the issue of whether the claimed deductions were properly taken by debtor rests with debtor regardless of which court determines the tax dispute. In other words, the United States contends it is the responsibility of debtor as taxpayer to establish that the deductions taken on his and Malka's joint tax returns were proper. Additionally, the United States notes that the cost of filing a petition with the Tax Court is not substantial and therefore, it is not costlier for the debtor to pursue the tax dispute in Tax Court rather than before this Court.

Debtor filed supplemental papers [dkt. no. 306] where he yet again argues that he has standing to object to the IRS proof of claim because the claim is based on a nondischargeable debt. Debtor further argues that the facts and circumstances of this case do not warrant abstention. Additional supplemental papers were thereafter filed by the parties [dkt. nos. 308, 312, 320, 323, 325, 326, 327, 328, 329, 331, 332]. Further, as noted above, both debtor's counsel and counsel for debtor's former law partner and his former law firm continue to file

letters with this Court as to the status of the state court accounting action, the most recent of which was filed by debtor on December 5, 2018 [dkt. no. 342].

h. The Debtor's Health

In addition to filing additional pleadings on the various issues raised by the parties, debtor's counsel submitted a letter advising the Court that debtor had unfortunately suffered a stroke [dkt. no. 316]. Debtor's counsel contends that it is prepared to proceed with debtor's objection to the IRS' proof of claim before this Court, but not before the Tax Court. Counsel maintains that if the Court were to abstain, then debtor would be forced to petition the Tax Court. Debtor's counsel alleges that debtor cannot afford to hire counsel to represent him in Tax Court, and debtor's stroke adversely affects his ability to represent himself. In sum, given the choice of forum in which to litigate the tax dispute, debtor makes clear that it is in this Court where he wishes to proceed and the running of the 150-day Period would appear to be of little relevance to the debtor.

Discussion

The pending motions present the Court with four primary questions: (i) whether the Stay Relief Stipulation, which resolved the First Stay Relief Motion regarding continued prosecution of the Malka Tax Proceeding, and the Conditional Order, which resolved the Second Stay Relief Motion, conferred exclusive jurisdiction on this Court to determine the outstanding tax dispute, (ii) whether debtor has standing to object to claims filed in his bankruptcy case, (iii) whether this Court should abstain from hearing the tax dispute in favor of the Tax Court, and (iv) whether the automatic stay should be modified for the limited purpose of commencing the 150-day Period regardless of whether this Court decides to abstain. The Court resolves each question below.

a. The Stay Relief Stipulation and Conditional Order

Debtor argues that the United States is precluded from seeking stay relief to permit the 150-day Period to run because both the Stay Relief Stipulation and the Conditional Order mandate that debtor's income tax liability be determined by this Court. In support of this argument, debtor points to the following retention of jurisdiction language in the Stay Relief Stipulation: "[t]he Bankruptcy Court shall retain exclusive jurisdiction over the terms, conditions, interpretations, implementations, and any and all disputes which may arise between the parties." This language, debtor argues, is a concession by the United States that the tax dispute must be heard by this Court. The United States has a different view of this language and its import. The United States argues that the language in question is nothing more than the parties' agreement that the Court retains exclusive jurisdiction to interpret and enforce the stipulation. The United States makes clear that the subject language is not a concession by it to the exclusive jurisdiction of this Court nor can it be read or interpreted as conferring exclusive jurisdiction on this Court to hear and determine the tax dispute. The Court agrees with the United States on this point. By statute, the Court does not have exclusive jurisdiction over the tax dispute; and the parties by agreement cannot confer exclusive jurisdiction on this Court.

In brief, the allocation of judicial power over bankruptcy matters is governed by (i) 28 U.S.C. § 151, which provides that the bankruptcy court is a "unit" of the district court, (ii) 28 U.S.C. § 1334(a), which provides that, except as set forth in 28 U.S.C. § 1334(b), district courts shall have original and exclusive jurisdiction over all "cases" under title 11, i.e., the Bankruptcy Code, (iii) 28 U.S.C. § 1334(b), which provides that district courts have original but not exclusive jurisdiction over all civil proceedings "arising under title 11, or arising in or related to cases under title 11" and (iv) 28 U.S.C. § 157(a), which provides that a district court may refer bankruptcy matters, i.e., cases under title 11 and proceedings arising under

title 11 or arising in or related to a case under title 11, to the bankruptcy court. As noted above, the Eastern District of New York has entered a general order of reference pursuant to which all bankruptcy matters are referred to the bankruptcy court. By reason of these three sections in title 28, i.e., § 151, § 1334, and § 157, the Bankruptcy Court is a court of limited jurisdiction. *See Celotex Corp. v Edwards*, 514 U.S. 300, 307 (1995) ("The jurisdiction of the bankruptcy courts, like that of other federal courts, is grounded in, and limited by statute.").

The debtor's tax dispute with the IRS is a civil proceeding arising during the pendency of this bankruptcy case. Accordingly, the jurisdiction of this Court over such proceeding is derived from the district court and falls under 28 U.S.C. § 1334(b) which vests original but not exclusive jurisdiction in the district court over all civil proceedings.[9] As such, under 28 U.S.C. § 157(a) and the standing order of reference in this district, this Court does not have exclusive jurisdiction over the outstanding tax dispute. Jurisdiction lies with the Tax Court as well. *See* 26 U.S.C. § 7442. Debtor does not dispute that the Tax Court has the authority to hear and determine whether debtor improperly claimed a theft loss deduction on his and Malka's joint tax return. Rather, he asserts that the parties by agreement conferred exclusive jurisdiction on this Court. This, debtor says, is made clear from the retention of jurisdiction language set forth in the Stay Relief Stipulation, to wit, "[t]he Bankruptcy Court shall retain exclusive jurisdiction over the terms, conditions, interpretations, implementations, and any and all disputes which may arise between the parties." The Court disagrees.

By the First Stay Relief Motion, the United States sought relief from the automatic stay to allow the Tax Court to hear and determine the outstanding dispute over debtor's and Malka's tax liability. The motion was prompted by the delay in the administration of debtor's

[9] Section 1334(a) and 1334(b) draw a distinction between a "case" which refers to the bankruptcy case in its entirety (here a chapter 7 case), from a "proceeding" which refers to a dispute or controversy that arises during the bankruptcy case. As noted, under § 1334(b), district courts have original but not exclusive jurisdiction over the three types of civil proceedings specified.

bankruptcy case because of the accounting action pending in state court between debtor and his former law partner and debtor's reluctance to seek stay relief to petition the Tax Court for resolution of the tax dispute. The United States did not seek stay relief simply to proceed with the Malka Tax Proceeding. However, as noted above, the Stay Relief Stipulation which resolved the First Stay Relief Motion merely referenced the case number of the Malka Tax Proceeding. Hence, in the end, the Stay Relief Stipulation was a non-event because it did not affect the Malka Tax Proceeding nor did it permit the 150-day Period to run vis-à-vis debtor. That is what prompted the United States to file the Second Stay Relief Motion. In short, the Stay Relief Stipulation did not resolve the parties' disagreement over the choice of forum for a determination of the tax dispute, nor did it confer exclusive jurisdiction on this Court to determine the tax dispute.

Additionally, debtor asserts that the choice of forum for resolution of the tax dispute was determined by the Conditional Order which directed debtor to commence an adversary proceeding or otherwise challenge the IRS' proof of claim in this Court within 30 days of entry of the Conditional Order. This, according to debtor, mandates that the tax dispute be heard and determined by this Court and the United States may not, after the fact, challenge that ruling. The debtor is wrong. The Conditional Order is not a concession by the United States to having this Court hear and determine the tax dispute. That is made clear by the very language of the Conditional Order which gives debtor a choice as to where to commence his challenge to the alleged income tax liability. The Conditional Order was entered because the bankruptcy case was at a standstill and the tax dispute needed to be resolved, either through resolution by the parties or a trial in this Court or in the Tax Court. Debtor chose this Court. That choice does not preclude the United States from asking that this Court abstain in favor of the Tax Court, nor can it be inferred that entry of the Conditional Order constitutes a ruling by this Court on abstention. At the time of its entry, no challenge to the IRS' proof of

claim was pending before this Court or the Tax Court. Simply stated, there was nothing to abstain from at that time.

As for the request by the United States that this Court modify the Conditional Order to remove the directive that debtor commence an adversary proceeding or challenge the IRS' proof of claim in this Court, that request is denied. No authority under Rule 60(b) of the Federal Rules of Civil Procedure, made applicable to this contested matter by Bankruptcy Rule 9024, is offered in support of this argument.

b. Debtor's Standing to Object to Proofs of Claim

Under § 502(a), "[a] claim or interest, proof of which is filed under section 501 of this title, is deemed allowed, unless a party in interest . . . objects." 11 U.S.C. § 502(a). The United States points to this statutory language and asserts that debtor is not a "party in interest" because he does not have a pecuniary interest in the bankruptcy case. This, the United States contends, demonstrates that debtor lacks the requisite constitutional or statutory standing to object to claims. For the following reasons, the Court disagrees.

First, the Second Circuit has held that "whether a Chapter 7 debtor may object to a proof of claim is a question of statutory standing. … Nothing in § 502 refers to jurisdiction or indicates that Congress intended the 'party in interest' limitation to be jurisdictional in nature." *Drake v. United States*, 622 Fed. Appx. 42, 42-43 (2d Cir. 2015) (assumes without deciding that the debtor in the case had standing to object to the IRS' proof of claim, but found that evidence was sufficient to support the bankruptcy court's allowance of the IRS claim).

Second, although the Bankruptcy Code does not define the term "party in interest" in a chapter 7 case, the chapter 7 trustee is a party in interest and may object to proofs of claim. The chapter 7 trustee is charged with administering the bankruptcy estate and the duties of a trustee include examining proofs of claim and objecting to the allowance of any claim that

is improper. 11 U.S.C. § 704(a)(5). *See also In re Fiber Optek Interconnect Corp.*, No. 05-30045, 2010 Bankr. LEXIS 5007, at *6 (Bankr. S.D.N.Y. Jan. 15, 2010). In addition, "[a] party in interest includes those persons with a personal stake or pecuniary interest in the outcome of the controversy." *Normali v. O'Donnell (In re O'Donnell)*, Nos. 04-8054, 04-8056, 2005 Bankr. LEXIS 862, at *14 (B.A.P. 6th Cir. May 19, 2005). In general, a chapter 7 debtor is not considered a "party in interest" because he or she often lacks a pecuniary interest in property of the bankruptcy estate. *Fiber Optek Interconnect Corp.*, No. 05-30045, 2010 Bankr. LEXIS 5007, at *7; *Greene v. Burke* (*In re Burke)*, No. 07-cv-01947-AP, 2008 U.S. Dist. LEXIS 75586, at *10 (D. Colo. Sept. 29, 2008). However, courts have found a pecuniary interest where: (1) the objection would result in a surplus to the debtor, *In re Chaitan*, 517 B.R. 419, 426 (Bankr. E.D.N.Y. 2014) (*citing In re 60 E. 80th St. Equities, Inc.*, 218 F.3d 109, 115-16 (2d Cir. 2000)), or (2) the challenged claim is nondischargeable, and a successful objection to the claim may reduce a debtor's personal liability on the alleged debt, *In re O'Donnell*, Nos. 04-8054, 04-8056, 2005 Bankr. LEXIS 862, at *15.

As to whether there will be any surplus to debtor, that remains to be seen. The trustee has recovered $305,000 for distribution to the holders of allowed claims. Debtor's former law partner and his former law firm have asserted a claim well in excess of the funds currently available for distribution by the trustee. The allowance of that claim hinges on the pending state court accounting action between the parties.

As to the nondischargeability ground, the Second Circuit has not yet decided whether nondischargeability of debt would confer standing upon a debtor to object to proofs of claim.[10]

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[10] The Second Circuit decisions regarding whether a debtor is a "party in interest" have held that "[i]t is well-established that a Chapter 7 debtor is a 'party in interest' and has standing to object to sale of the assets, or otherwise participate in litigation surrounding the assets of the estate, only if there could be a surplus after all creditors' claims are paid." *In re 60 E. 80th St. Equities, Inc.*, 218 F.3d at 115. *See also Licata v. Coan (In re Licata)*, 659 Fed. Appx. 704, 706 (2d Cir. 2016); *Pascazi v. Fiber Consultants, Inc.*, 445 B.R. 124, 127 (S.D.N.Y. 2011). The court in *60 E. 80th St. Equities, Inc.* did not discuss the issue of standing in the context of nondischargeability of

However, lower courts within the Second Circuit and in other jurisdictions have found that a debtor has standing where a debt is nondischargeable and a reduction of such debt, or a debt having higher priority in bankruptcy, would maximize the distribution of estate assets and reduce a debtor's personal liability on the nondischargeable debt. *Drake v. United States*, No. 1:13-CV-1136 (LEK), 2014 WL 6883104, at *3 (N.D.N.Y. Dec. 4, 2014); *In re Chaitan*, 517 B.R. at 426; *McGuirl v. White*, 86 F.3d 1232 (D.C. Cir. 1996) (finding the debtors have standing to challenge the trustee's fee application where all the debts were nondischargeable and reduction of the administrative expenses of the estate will necessarily reduce the amount of nondischargeable claims the debtors would be liable for post-bankruptcy); *In re Ellis*, No. 10-16998-RLM-7A, 2014 WL 1725810, at *5 (Bankr. S.D. Ind. Apr. 30, 2014) (finding debtor has standing to object to administrative expense claims where allowance of the claims as filed would affect the distribution to the holder of a nondischargeable loan and the debtor's post-discharge liability on such loan); *Willard v. O'Neil (In re Willard)*, 240 B.R. 664, 668 (Bankr. D. Conn. 1999) (finding that a debtor holds a direct pecuniary interest and standing to object to the allowance of a creditor's claim where the judgment debt at issue may never be discharged).

Here, debtor would be personally liable for that portion of his tax liability for tax years 1999 and 2000 that is not satisfied by a distribution from the bankruptcy estate. Section 507(a)(8)(A)(iii) confers priority, unsecured status, on claims for taxes "not assessed before, but assessable under applicable law or by agreement, after, the commencement of the case." 11 U.S.C. § 507(a)(8)(A)(iii). Because the deficiency for tax years 1999 and 2000 was assessed post-petition, the tax claim would be entitled to priority under § 507(a)(8), and the United

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debt. The Second Circuit had the opportunity in *Drake*, 622 Fed. Appx. 42, to address whether nondischargeability of a tax debt would also confer a debtor with pecuniary interest, but declined to rule on that issue.

States would argue that the claim is nondischargeable under § 523(a)(1)(A).[11] Because there is no evidence that that the estate is administratively insolvent at this time, debtor has a pecuniary interest as a successful objection to the IRS' proof of claim will reduce his personal liability for such taxes post-bankruptcy.

The United States argues that a complaint filed by a debtor seeking to except a debt from discharge under § 523(a) serves no bankruptcy purpose where the debt is indisputably nondischargeable. According to the United States, a court need not hear a debtor's claim that an amount less than that asserted by the IRS is due and owing, or that no amount is due and owing, where it is clear that the challenged debt is nondischargeable. This argument is unavailing. Here, debtor is not seeking to except the tax debt from discharge under § 523(a) nor has he disputed that any tax debt would be nondischargeable. Rather, he submits that because the amount of such debt has not yet been finalized, the determination of liability and amount owed to the IRS, if any, would directly affect whether general unsecured creditors will receive any distribution from the bankruptcy estate, not just debtor's post-bankruptcy liability. If the tax debt owed exceeds the assets available for distribution, the general unsecured creditors of this bankruptcy estate will receive nothing. Because a determination of debtor's tax liability will have a direct impact on funds available for distribution to creditors, the Court finds that debtor has standing at this time to object to the IRS' proof of claim.

c. Whether this Court Should Abstain from Hearing the Tax Dispute

Although this Court has jurisdiction, the United States asks the Court to abstain from hearing the outstanding tax dispute in deference to the Tax Court. The United States' request

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[11] Section 523(a)(1)(A) provides that a discharge under § 727 does not discharge an individual from any debt:

(1) for a tax or a customs duty –

(A) of the kind and for the periods specified in section 507(a)(3) or 507(a)(8) of this title, whether or not a claim for such tax was filed or allowed.

is for permissive or discretionary abstention under 28 U.S.C. § 1334(c)(1). Section 1334(c)(1) provides that "nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11." 28 U.S.C. § 1334(c)(1). Bankruptcy courts have broad discretion in determining whether abstention is appropriate. *Cody, Inc. v. County of Orange (In re Cody, Inc.)*, 281 B.R. 182, 190 (S.D.N.Y. 2002).

Permissive or discretionary abstention under 28 U.S.C. § 1334(c)(1) "demonstrate[s] the intent of Congress that concerns of comity and judicial convenience should be met, not be rigid limitations on the jurisdiction of federal courts, but by the discretionary exercise of abstention when appropriate in a particular case." *In re Cody, Inc.*, 281 B.R. at 190 (*quoting Zack v. United* States, 224 B.R. 601, 606 (E.D. Mich. 1998)). *See also Luan Inv. S.E. v. Franklin 145 Corp. (In re Petrie Retail, Inc.),* 304 F.3d 223, 232 (2d Cir. 2002); *The Chamberlain Group, Inc. v. Lear Corp. (In re Lear Corp.)*, Adv. No. 09-01441 (ALG), 2009 WL 3191369, at *3 (Bankr. S.D.N.Y. Sept. 24, 2009) (stating that courts have "wide discretion" in deciding whether to abstain). Although 28 U.S.C. § 1334(c)(1) references state law, it "has been widely applied by bankruptcy courts to abstain from hearing tax disputes between debtors and state and/or federal taxing authorities." *Cody, Inc.*, 281 B.R. at 191. *See also In re Motors Liquidation Co.*, 457 B.R. 276, 288 (Bankr. S.D.N.Y. 2011).

In determining whether to abstain under 28 U.S.C. § 1334(c)(1), bankruptcy courts consider the following factors:

> (1) the effect, or lack thereof, of abstention on the estate if a Court recommends abstention;
> (2) the extent to which [non-bankruptcy] law issues predominate over bankruptcy issues;
> (3) the difficulty or unsettled nature of the applicable [non-bankruptcy] law;

> (4) the presence of a related proceeding commenced in state court or other non-bankruptcy court;
> (5) the jurisdictional basis, if any, other than 28 U.S.C. § 1334;
> (6) the degree of relatedness or remoteness of the proceeding to the main bankruptcy case;
> (7) the substance rather than the form of an asserted "core" proceeding;
> (8) the feasibility of severing [non-bankruptcy] law claims from core bankruptcy matters to allow judgment to be entered in [non-bankruptcy] court with enforcement left to the bankruptcy court;
> (9) the burden on [the bankruptcy court's] docket;
> (10) the likelihood that the commencement of the proceeding in a bankruptcy court involves forum shopping by one of the parties;
> (11) the existence of a right to a jury trial; and
> (12) the presence in the proceeding of non-debtor parties.

Motors Liquidation Co., 457 B.R. at 289 (*quoting In re Portrait Corp. of America, Inc.)*, 406 B.R. 637, 641-42 (Bankr. S.D.N.Y. 2009)); *Cody, Inc.*, 281 B.R. at 190-91; *In re Gordon*, No. 09-16230 (AJG), 2011 WL 3878356, at *3 (Bankr. S.D.N.Y. Aug. 30, 2011) (considering similar factors to find that permissive abstention under 28 U.S.C. § 1334(c)(1) in favor of the Tax Court was appropriate); *Liani v. Baker (In re Baker)*, 374 B.R. 498, 505 (Bankr. E.D.N.Y. 2007) (finding permissive abstention under 28 U.S.C. § 1334(c)(1) to be unwarranted where, *inter alia*, no state court case has been commenced and state law issues did not predominate over bankruptcy issues).

Additionally, the issue of whether the Court exercises its jurisdiction to determine the debtor's tax liability implicates § 505(a). Debtor's objection to the IRS claim is analogous to commencement of a proceeding before this Court under § 505(a) to determine the amount or legality of a debtor's tax liability. Section 505(a)(1) provides, in pertinent part, that:

> the court *may* determine the amount or legality of any tax, any fine or penalty relating to a tax, or any addition to tax, whether or not previously assessed, whether or not paid, and whether or not contested before and adjudicated by a judicial or administrative tribunal of competent jurisdiction.

11 U.S.C. § 505(a)(1) (emphasis added). As with 28 U.S.C. § 1334(c)(1), a bankruptcy court's decision to determine a debtor's tax liability under § 505(a)(1) is discretionary. *New Haven Projects Ltd. Liab. Co. v. City of New Haven (In re New Haven Projects Ltd. Liab. Co.)*, 225 F.3d 283, 287-88 (2d Cir. 2000) (observing that the use of the word "may" denotes a grant of authority that is permissive while use of the word "shall" denotes mandatory requirements); *In re 499 W. Warren St. Assocs., Ltd. P'ship*, 143 B.R. 326, 329 (Bankr. N.D.N.Y. 1992); *In re Galvano*, 116 B.R. 367, 372 (Bankr. E.D.N.Y. 1990). The court's discretion under § 505(a) is exercised on a case by case basis. *In re Hunt*, 95 B.R. 442, 445 (Bankr. N.D. Tex. 1989). In deciding whether to exercise its discretion to determine the amount or legality of a tax under § 505(a), bankruptcy courts consider several factors, including:

> (1) the complexity of the tax issue;
> (2) the need to administer the bankruptcy case in an expeditious fashion;
> (3) the burden on the bankruptcy court's docket;
> (4) the length of time necessary to conduct the hearing and to render a decision thereafter;
> (5) the asset and liability structure of the debtor; and
> (6) the potential prejudice to the debtor, the taxing authority, and creditors.

New Haven Projects Ltd. Liab. Co., 225 F.3d at 289; *499 W. Warren St. Assocs., Ltd. P'ship*, 143 B.R. at 329.

Generally, bankruptcy courts decline to exercise jurisdiction to determine a debtor's tax liability under § 505 where the tax litigation would further no bankruptcy purpose. *New Haven Projects Ltd. Liab. Co.*, 225 F.3d at 290 (declining § 505 determination where amount of unsecured debt was *de minimis* and review would only benefit debtor, its affiliates, and insiders); *Gordon*, No. 09-16230 (AJG), 2011 WL 3878356, at *6. As such, the rationale for determining the amount or legality of a tax under § 505 is whether creditors of the estate will benefit. For example, a § 505(a) determination protects creditors from the dissipation of a

bankruptcy estate's assets if the bankruptcy estate was bound by a tax judgment which the debtor failed to contest prior to bankruptcy.[12] *New Haven Projects Ltd. Liab. Co.*, 225 F.3d at 287; *Galvano*, 116 B.R. at 372. This, however, is not an issue here because debtor did not petition the Tax Court prior to commencement of his bankruptcy case and, consequently, no tax judgment was entered against debtor prepetition.

In its motion, the United States makes a compelling argument for abstention under 28 U.S.C. § 1334(c)(1) or for this Court to decline to determine the amount or legality of the tax debt under § 505(a) by calling attention to the following: (a) the tax dispute centers upon whether debtor's theft loss deduction was appropriate — a matter, the United States notes, is an issue of pure tax law and requires a determination as to (i) whether the applicable statute of limitations for deducting losses of a pass-through entity is outcome-determinative, (ii) whether other legitimate expenses claimed by debtor were misunderstood or ignored by the IRS, (iii) whether a theft occurred, and (iv) assuming that a theft occurred, whether the theft loss can be deducted by debtor, and the circumstances where such deduction would be proper; (b) the Tax Court exists as a specialized tribunal created to specifically handle such disputes; (c) Malka's Tax Proceeding is pending before the Tax Court as a related proceeding in which the Tax Court must make a similar determination as to debtor and Malka's tax liability before deciding on Malka's innocent spouse defense; (d) because of the Malka Tax Proceeding, the Tax Court has been ready for several years to preside over the tax dispute; and (e) Malka is a non-debtor party to the tax dispute, and the Court does not have

[12] Section 505, however, does not permit a court to determine the amount or legality of a tax, fine, penalty, or addition to tax if such amount or legality was contested before and adjudicated by a judicial or administrative tribunal of competent jurisdiction before the commencement of the bankruptcy case. 11 U.S.C. § 505(a)(2)(A). *See also Galvano,* 116 B.R. at 374 (affirming bankruptcy court's ruling that the first tax assessment had been "contested and adjudicated" before a tribunal of competent jurisdiction and § 505(a) precluded further determination by the bankruptcy court). As there has been no prior determination of debtor's tax liabilities by the Tax Court, this exception does not apply here.

jurisdiction to hear and determine the amount or legality of Malka's alleged tax liability and the merits of her innocent spouse defense.

While the argument advanced by the United States weighs in favor of abstention, the principles of permissive abstention are traditionally considered when there is a proceeding pending in another forum. Debtor points out that is not the case here. There is no parallel proceeding in Tax Court to determine debtor's tax liability, if any. Although the Malka Tax Proceeding is pending in the Tax Court, albeit held in abeyance, a proceeding to determine debtor's tax liability is not currently before the Tax Court. Debtor deliberately chose not to seek stay relief to petition the Tax Court for a determination of his purported tax liability, and he intervened in the Malka Tax Proceeding solely to assert the automatic stay relative to any claims against him regarding Malka's claim for innocent spouse relief. Moving to intervene in the Malka Tax Proceeding is not the same as petitioning the Tax Court for a determination of debtor's tax liability. If the United States thought otherwise, it would not have sought relief from the automatic stay to allow the running of the 150-day Period.

Although tax law, and not bankruptcy law, would hold sway in any proceeding to determine the amount or legality of debtor's tax liability, the end result would have a direct and significant impact on the distribution to creditors holding general unsecured claims in this bankruptcy case because of the priority in payment accorded the IRS on its tax claim. *See* 11 U.S.C. § 726(a). Hence, resolution of the tax dispute is integral to the administration by the trustee of debtor's bankruptcy case. Unless debtor has a change of heart, or strategy, and elects to file a petition with the Tax Court for a redetermination of the IRS assessment, this Court is the only available forum at this time in which the tax dispute can be determined.

While the Court, based on the record placed before it, believes that the tax dispute is best resolved in Tax Court, the request by the United States for abstention is premature and is hereby denied without prejudice as there is currently no alternative forum where debtor's

tax dispute may be heard. This decision should not be interpreted as the Court's lending any credence to the strategy employed by debtor in avoiding resolution of the outstanding tax dispute.

d. The United States' Request to Lift the Stay

Lastly, the United States contends that if the Court does not defer to the Tax Court, the automatic stay imposed under § 362(a)(8) should be lifted to permit the running of the 150-day Period. The United States argues that no purpose is served by continuing to toll the 150-day Period because debtor has made it clear that the tax dispute should be decided by this Court. In response, debtor contends that (i) the United States has raised this issue four times, and (ii) the Conditional Order, which resolved the Second Stay Relief Motion and directed debtor to decide whether to challenge the IRS' proof of claim in this Court, is a final order that the United States did not appeal nor timely move to reconsider. For these reasons, debtor asserts, the United States is precluded from seeking relief from stay in order to start the clock on the 150-day Period. The Court disagrees. The Conditional Order provided for the lifting of the automatic stay if debtor failed to challenge the IRS claim within 30 days of the entry of the Conditional Order. It did not bar the United States from later seeking relief from stay, which the United States did in the Motion to Dismiss Claims Objection and the Third Stay Relief Motion.

Additionally, debtor argues that lifting the stay to allow the 150-day Period to run compels debtor to petition the Tax Court. This argument is likewise unavailing. First, debtor has repeatedly stated that he has no intention of filing a petition with the Tax Court, alleging both health and financial reasons. The purpose of the 150-day Period is to provide a debtor sufficient time and opportunity to petition the Tax Court, despite an intervening bankruptcy filing. Outside of bankruptcy, if a debtor chose not to proceed before the Tax Court, he or she could not file a petition with the Tax Court after the deadline has passed. Second, if a debtor

decides to proceed in bankruptcy court, a determination of tax liability by the bankruptcy court is final and issue preclusion would prevent a subsequent review by the Tax Court.

> The general principle of res judicata provides that once a court of competent jurisdiction has entered a final judgment on the merits of a cause of action, the parties to the suit AND THEIR PRIVIES are bound as to each matter that sustained or defeated the claim, and as to any other admissible matter that could have been offered for that purpose. *Comm'r of Internal Revenue v. Sunnen*, 333 U.S. 591, 597 (1948).

McQuade v. Comm'r of Internal Revenue, 84 T.C. 137, 141 (Tax Ct. 1985) (emphasis in original). The Tax Court has previously held that "Congress intended that once a bankruptcy court allowed a deficiency for which claim was filed and that court's action became final, the amount and validity of the deficiency was not thereafter to be the subject of a consideration by the Tax Court." *McQuade*, 84 T.C. at 145 (*quoting Comas, Inc. v. Comm'r of Internal Revenue*, 23 T.C. 8, 12 (Tax Ct. 1954)). *See also Freytag v. Comm'r of Internal Revenue*, 110 T.C. 35, 46 (Tax Ct. 1998) (holding that while the Tax Court retained jurisdiction over a tax dispute arising from a petition filed in Tax Court prior to the taxpayers' bankruptcy filing, the Tax Court was bound by the principle of *res judicata* with respect to the Bankruptcy Court's determination of all the factual and legal issues in dispute in the bankruptcy case).[13] Thus, if this Court, as debtor's selected forum, were to rule against him on his claims objection, he could not then file a petition with the Tax Court in the hope of getting a better result. Rather, debtor's recourse on an adverse ruling is an appeal to the District Court.

In short, debtor has not expressed any credible reason as to why the toll on the 150-day Period should continue or how he is prejudiced by the stay being lifted. Given debtor's

[13] While the case before the Court is a chapter 7 case, the Court notes that the doctrine of *res judicata* would not apply to a consent order or settlement resolving a debtor's objection to a proof of claim filed by the IRS in a chapter 11 case for purposes of determining the amount to be allowed in a plan of reorganization where the consent order was not a final determination by the bankruptcy court pursuant to § 505(a) on the merits of a debtor's entire federal tax debt for any given year, and collateral estoppel also would not apply where the issue of a debtor's total federal tax liability was never actually litigated. *Breland v. Comm'r of Internal Revenue*, 152 T.C. No. 9, 2019 WL 1409668, at *10 (Tax Ct. Mar. 28, 2019).

unrelenting position that the outstanding tax dispute must be heard and determined by this Court, no purpose is served by preserving the 150-day Period. Why should debtor, after making clear his choice of forum, now have an option to decide at some point *prior to* final determination of tax liability by this Court, to take a chance in Tax Court. A taxpayer outside of bankruptcy cannot forum shop after the statute of limitations has run and a debtor in bankruptcy should not be able to stay the running of a limitations period to ensure access to an alternative forum if litigation in the chosen forum is not proceeding in his or her favor. The only consequence of lifting of the stay is to put a time limit on debtor's ability to change his strategy regarding in which forum he wishes to litigate the tax dispute. To preserve the 150-day Period under the circumstances present in this bankruptcy case invites a potential for abuse and a waste of judicial resources. It is time for the tax dispute to be resolved, it has been delayed long enough. As debtor noted, his health has declined and he is on in years. He has spent more than a decade in bankruptcy, all the while litigating an accounting action with his former law partner in state court, and more than 15 years have passed since events relevant to tax years 1999 and 2000 occurred. Accordingly, based on the record placed before the Court, the automatic stay imposed under § 362(a)(8) is lifted to allow the running of the 150-day Period.

e. The Burden of Proof in the Tax Litigation

Although the burden of proof need not be addressed until the Court hears the merits of the disputed tax liability, the Court believes it is prudent to discuss the burden of proof at this time as debtor considers his options. One of debtor's principal reasons for insisting that this Court hear and determine the outstanding tax dispute is his unwavering belief that he will successfully rebut the *prima facie* validity of the IRS' proof of claim and the burden then shifts to the United States to prove debtor's tax liability. To support his argument, debtor relies on the burden shifting framework applied to claims objections. *See In re St. Johnsbury*

Trucking Co., Inc., 206 B.R. 318, 323 (Bankr. S.D.N.Y. 1997), *aff'd.*, 221 B.R. 692 (S.D.N.Y. 1998), *aff'd.*, 173 F.3d 846 (2d Cir. 1999). Debtor claims that while in Tax Court the burden is on the taxpayer to prove that deductions taken on his or her tax return were proper, the opposite holds true in bankruptcy court. The burden, he says, rests with the IRS. Debtor is incorrect. As discussed below, a bankruptcy filing does not alter the applicable burden of proof with respect to the tax claim.

In a proceeding before the Tax Court, the burden of proof is on the taxpayer. Tax Court Rule 142(a)(1).[14] "The Commissioner's deficiency determinations are presumed correct and the taxpayer bears the burden of proving otherwise." *Alioto v. Comm'r of Internal Revenue.*, 699 F.3d 948, 952 (6th Cir. 2012) (*quoting Ekman v. Comm'r of Internal Revenue*, 184 F.3d 522, 524 (6th Cir. 1999)); *Jeppsen v. Comm'r of Internal Revenue*, 128 F.3d 1410, 1418 (10th Cir. 1997); *Krahmer v. United States*, 810 F.2d 1145, 1147 (Fed. Cir. 1987). *See also Lombard Bros., Inc. v. U.S.*, 893 F.2d 520, 523 (2d Cir. 1990) (holding that the taxpayer has the burden of proof of establishing by clear and convincing evidence that the loss was caused by larceny or some similar criminal acts).

The taxpayer's bankruptcy filing does not change the burden of proof imposed by substantive law with respect to allowance of a tax claim. *Raleigh v. Ill. Dept. of Revenue*, 530 U.S. 15 (2000). The Supreme Court in *Raleigh* held that "[b]ankruptcy courts are not authorized in the name of equity to make wholesale substitution of underlying law controlling the validity of creditors' entitlements, but are limited to what the Bankruptcy Code provides." *Id.*, at 24-25. Finding the Bankruptcy Code silent on the issue of whether the burden of proof shifts to the government and concluding that the burden of proof in bankruptcy should be no

[14] Tax Court Rule 142(a)(1) provides that "[t]he burden of proof shall be upon the petitioner, except as otherwise provided by statute or determined by the Court; and except that, in respect of any new matter, increases in deficiency, and affirmative defenses, pleaded in the answer, it shall be upon the respondent."

different than the applicable burden of proof outside of bankruptcy, the Supreme Court held that underlying substantive law controlled.

> Given its importance to the outcome of cases, we have long held the burden of proof to be a "substantive" aspect of a claim. That is, the burden of proof is an essential element of the claim itself; one who asserts a claim is entitled to the burden of proof that normally comes with it.
>
> Tax law is no candidate for exception from this general rule, for the very fact that the burden of proof has often been placed on the taxpayer indicates how critical the burden rule is, and reflects several compelling rationales: the vital interest of the government in acquiring its lifeblood, revenue; the taxpayer's readier access to the relevant information; and the importance of encouraging voluntary compliance by giving taxpayers incentives to self-report and to keep adequate records in case of dispute.

Id., at 21 (internal citations omitted).

Although the Supreme Court's decision in *Raleigh* dealt with an Illinois tax claim, "its reasoning can readily be extended to provide that the ultimate burden of proof always rests on the party who would bear it outside of bankruptcy." 9-3001 Collier on Bankruptcy P 3001.09[2] (16th ed. 2019) (*citing In re Vancleef*, 479 B.R. 809, 821 (Bankr. N.D. Ind. 2012) (noting that a "claimant is held to the same standard of proof as if the claimant were establishing its claim in a non-bankruptcy forum"), *rev'd and remanded on other grounds*, *Yoon v. Vancleef*, 498 B.R. 864 (N.D. Ind. 2013)). In applying *Raleigh* to a federal tax claim, the Second Circuit held:

> [f]ederal tax assessments are presumed to be correct and prima facie evidence of liability. *See Welch v. Helvering*, 290 U.S. 111, 115, 54 S. Ct. 8, 78 L. Ed. 212 (1933); *United States v. McCombs,* 30 F.3d 310, 318 (2d Cir. 1994). The taxpayer bears the burden to prove that the assessment was incorrect. *McCombs*, 30 F.3d at 318. This burden applies within bankruptcy proceedings.

Internal Revenue Service v. Worldcom, Inc. (In re Worldcom, Inc.), 723 F.3d 346, 352 (2d Cir. 2013) (*citing Raleigh*, 530 U.S. at 26). Therefore, in resolving the outstanding tax dispute,

the burden of proof lies with debtor, to wit, it is debtor's responsibility to establish that the IRS assessment was incorrect and that deductions on his tax returns were properly taken.

Conclusion

For the foregoing reasons, the United States' motion to dismiss debtor's objection to the IRS' proof of claim is denied in part and granted in part. The motion is (i) denied to the extent it seeks to remove the directive in the Conditional Order that debtor must commence an adversary proceeding or otherwise challenge the IRS' proof of claim in this Court by a date certain, (ii) denied as premature to the extent is seeks to have this Court abstain from hearing the tax dispute in deference to the Tax Court, and (iii) granted to the extent of lifting the automatic stay to permit the 150-day Period pursuant to IRC § 6213(f)(1) to run. Because the Court has granted that portion of the United States' motion for relief from the automatic stay so as to start the running of the clock on the 150-day Period, the United States' separate motion for relief from the automatic stay so as commence the running of the 150-day Period is denied as moot.

The Court will issue a separate order directing the parties to appear at a status conference to discuss the next steps toward resolution of debtor's alleged tax liability.

So Ordered.

Dated: June 5, 2019
Central Islip, New York

Louis A. Scarcella
United States Bankruptcy Judge

COVID 19 AND CHAPTER 13

CARES ACT PASSED MARCH 27, 2020

Passed by Congress in response to the COVID 19 pandemic.

Section. 4022. Foreclosure moratorium and consumer right to request forbearance.

Sec. 4023. Forbearance of residential mortgage loan payments for multifamily properties with federally backed loans.

Sec. 4024. Temporary moratorium on eviction filings. Sec. 4025. Protection of collective bargaining agreement.

CARES ACT Section 4022 provides foreclosure relief for federally backed mortgages on 1 to 4 family residential homes. Federally backed mortgages include those that are insured, owned, guaranteed, or purchased by FNMA, FHLMC, FHA or the VA. (4022(a)(2). This Act does not apply to private investors.

Section 4022(c)(2) states that a servicer of a federally backed mortgage may not initiate a foreclosure, more for a foreclosure judgment, schedule a sale or execute a foreclosure related eviction. NY state has imposed a moratorium on all evictions and foreclosures until August 20 which extends beyond the timeframe imposed by Congress.

In order to take advantage of the CARES ACT, you must demonstrate a financial hardship as a result of COVID 19. This hardship can be direct or indirect. Loss of a job, reduction in income, are examples of a direct impact. However, the hardship can result from an indirect impact as well. For example, an adult child loses their job and moves back home. While the parent's income may remain the same, the expenses have increased as the parent has to now support another individual.

MORTGAGES AND FORBEARANCES

The purpose of the forbearance is to provide short term relief to debtors. A Forbearance Plan is defined as a written agreement defining whether the Borrower may make either reduced or no monthly payments for a specified time. The Forbearance Plan provides a solution for borrowers experiencing hardships such as illness, unemployment, reduction in income, etc. Depending on the investor, different solutions will be available. Many secured creditors offer 90 to 180 day forbearances. Homeowners may request additional 180 days. During forbearance period no fees, interest, penalties shall accrue beyond the amounts borrowers are contractually obligated to pay. The period seems to extend until 12/31/20 or the emergency ends, whichever is earlier.

To receive a forbearance the debtor must contact the servicer and advise that they are experiencing a financial hardship as a result of COVID 19. No additional documentation is required. This does not preclude the trustee from requesting documentation however.

These forbearances do not waive the payments but rather provide the debtor with a period of time in which payments are not required to be made. It does not defer the payments to a future date. Payments must resume at the end of the forbearance period. Further the amount which was forborne must be repaid. A forbearance is not a modification and regular payments are required to resume at the end of the forbearance term.

Options for repayment:

1. Pay in full at end of deferment period
2. Enter into Extended Agreed Order
3. Loss Mitigation
4. Capitalization of payments or adding to end of loan

Bankruptcy Issues

1. Forbearances – Notices filed. Do we need court approval for these? We have been filing the Notices without obtaining court approval. The Southern District and Northern District have forms for these forbearances
2. Impact of Forbearances on future payment changes
   For ex. Escrow changes ..how will that be calculated, may result in escrow shortages and increased payments
3. Motions for Relief not automatically stopped. Lenders may proceed with Motions for Relief. If debtor is on forbearance a MFR will not be filed but may be filed if no repayment plan is worked out.

MODIFICATION OF CONFIRMED PLANS

1329(d)(1) – Modification of Plans Confirmed Prior to 3/27/2020

Plans confirmed prior to 3/27/2020 may be extended for 2 years provided the debtor can demonstrate a material financial hardship due directly or indirectly as a result of COVID 19.

Can a debtor add the post petition payments into the plan modification?

This provision terminates one year after the 3/27/20 so if you are intending to take advantage of this provision it must be done by 3/27/21

WHAT HAPPENS AFTER FORBEARANCE

CARES requires that the lender/servicer work with the debtor to enter into a plan to pay the arrears. This includes:

1. Loss Mitigation
2. Payment through the Chapter 13 Plan
3. Payment through an Agreed Order

REMEMBER LENDERS HAVE THE RIGHT TO FILE A MOTION FOR RELIEF AFTER THE FORBEARANCE SO IT IS IMPORTANT TO WORK OUT SOME TYPE OF REPAYMENT PRIOR TO THE FORBEARANCE PERIOD ENDS.

SEC. 4022. FORECLOSURE MORATORIUM AND CONSUMER RIGHT TO REQUEST FORBEARANCE.

(a) DEFINITIONS.—In this section:

(1) COVID–19 EMERGENCY.—The term "COVID–19 emergency" means the national emergency concerning the novel coronavirus disease (COVID–19) outbreak declared by the President on March 13, 2020 under the National Emergencies Act (50 U.S.C. 1601 et seq.).

(2) FEDERALLY BACKED MORTGAGE LOAN.—The term "Federally backed mortgage loan" includes any loan which is secured by a first or subordinate lien on residential real property (including individual units of condominiums and cooperatives) designed principally for the occupancy of from 1- to 4- families that is—

(A) insured by the Federal Housing Administration under title II of the National Housing Act (12 U.S.C. 1707 et seq.);

(B) insured under section 255 of the National Housing Act (12 U.S.C. 1715z–20);

(C) guaranteed under section 184 or 184A of the Housing and Community Development Act of 1992 (12 U.S.C. 1715z–13a, 1715z–13b);

(D) guaranteed or insured by the Department of Veterans Affairs;

(E) guaranteed or insured by the Department of Agriculture;

(F) made by the Department of Agriculture; or

(G) purchased or securitized by the Federal Home Loan Mortgage Corporation or the Federal National Mortgage Association.

(b) FORBEARANCE.—

(1) IN GENERAL.—During the covered period, a borrower with a Federally backed mortgage loan experiencing a financial hardship due, directly or indirectly, to the COVID–19 emergency may request forbearance on the Federally backed mortgage loan, regardless of delinquency status, by—

(A) submitting a request to the borrower's servicer; and

(B) affirming that the borrower is experiencing a financial hardship during the COVID–19 emergency.

(2) DURATION OF FORBEARANCE.—Upon a request by a borrower for forbearance under paragraph (1), such forbearance shall be granted for up to 180 days, and shall be extended for an additional period of up to 180 days at the request of the borrower, provided that, at the borrower's request, either the initial or extended period of forbearance may be shortened.

(3) ACCRUAL OF INTEREST OR FEES.—During a period of forbearance described in this subsection, no fees, penalties, or interest beyond the amounts scheduled or calculated as if the borrower made all contractual payments on time and in full under the terms of the mortgage contract, shall accrue on the borrower's account.

(c) REQUIREMENTS FOR SERVICERS.—

(1) IN GENERAL.—Upon receiving a request for forbearance from a borrower under subsection (b), the servicer shall with no additional documentation required other than the borrower's attestation to a financial hardship caused by the COVID–19 emergency and with no fees, penalties, or interest (beyond the amounts scheduled or calculated as if the borrower made all contractual payments on time and in full under the terms of the mortgage contract) charged to the borrower in connection with the forbearance, provide the forbearance for up to 180 days, which may be extended for an additional period of up to 180 days at the request of the borrower, provided that, the borrower's request for an extension is made during the covered period, and, at the borrower's request, either the initial or extended period of forbearance may be shortened.

(2) FORECLOSURE MORATORIUM.—Except with respect to a vacant or abandoned property, a servicer of a Federally backed mortgage loan may not initiate any judicial or non-judicial foreclosure process, move for a foreclosure judgment or order of sale, or execute a foreclosure-related eviction or foreclosure sale for not less than the 60-day period beginning on March 18, 2020.