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POST-PETITION CAUSES OF ACTION-PROPERTY OF THE ESTATE, DISPOSABLE INCOME, NEITHER OR BOTH?

By: Sabrina McKinney

Since the implementation of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), the dividend to unsecured creditors has been substantially reduced in many cases. As such, some Trustees have re-doubled their efforts to try to increase the dividend to unsecured creditors to overcome the damage done to unsecured creditors by the new "means test" and the new "910 claim" provision of BAPCPA. One avenue of collection which has increased over the last several years has been in the area of lawsuit collections. Some Trustees view these suits as both property of the estate and disposable income for the benefit of unsecured creditors. With the conflict between §1306, §1327 and the 11th Circuit's ruling in Telfair, many Trustees have been fighting an uphill battle in their efforts to collect these assets for the benefit of unsecured creditors.

In a recent case filed after the implementation of BAPCPA in the Middle District of Alabama (In re Steven and Wendy Baxter, chapter 13 case no. 06-10672), the Court was asked to consider whether a debtor's post-petition cause of action was property of the debtor's estate. After confirmation of the chapter 13 plan, the debtor filed suit against one of their creditors for violation of the Fair Debt Collection Practices Act.

News from the Middle District

On July 1, 2008 new local rules became effective in the U.S. Bankruptcy Court for the Middle District of Alabama. The rules are posted at www.almb.uscourts.gov

For information regarding preparing and submitting proposed orders in the Middle District go to <http://www.almb.uscourts.gov/motographs/index.htm>.

News from Northern District

Douglas E. Wedge has been appointed Chief Deputy Clerk for the United States Bankruptcy Court for the Northern District of Alabama. Doug graduated from the University of Tulsa with a BA in English and from the University of South Carolina with a Masters in English. Doug attended the University of South Carolina for his law degree, graduating with a J.D. in 2001. After law school, he clerked for the Honorable John E. Waites of the United States Bankruptcy Court for South

Carolina. Following this year clerkship, Doug joined the law firm of Moore & VanAllen, PLLC in Charleston, South Carolina. Doug and his wife, Shawn, have four children. Doug will be located primarily in the Southern Division, Birmingham office, of the Northern District of Alabama Bankruptcy Court. His email is Douglas.Wedge@alnb.uscourts.gov and his telephone number is 205-714-4006.

Each divisional office within the Northern District offers CM/ECF refresher training. These sessions are free, and they can be individually tailored in a one-on-one setting. Also, the Northern District's website, www.alnb.uscourts.gov, contains helpful practice pointers under the CM/ECF heading and "Announcements" sub-section. Finally, to consolidate and minimize the down time for CM/ECF, the court schedules system upgrades and maintenance once a month. They complete these upgrades and maintenance tasks the second Tuesday of every month beginning at 5:00 p.m

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Bankruptcy filings for the first two months of this calendar year have increased 50% over the same period last year.

[New Clerk of Court for the U.S. Bankruptcy Court for the Southern District of Alabama](#)

Congratulations and welcome to Leonard "Chip" Maldonado, the newly appointed Clerk of Court for the U.S. Bankruptcy Court for the Southern District of Alabama replacing Geraldine Lester who retired.



and the Foreign Area Officer Program where he served combat tours in Vietnam and Cambodia, duty as the executive officer of an airborne battalion at Fort Bragg, served on the Department of the Army staff at the Pentagon, commanded a signal battalion with the VII Corps in Germany, and was the Defense and Army Attache in San Jose, Costa Rica.

Chip received his bachelor's degree and was commissioned as a Distinguished Military Graduate from the University of Arizona, where he majored in mathematics and minored in chemistry/physics. He also has a master's degree in Latin American Studies from the University of New Mexico. Chip received his law degree from Suffolk University in Boston, Massachusetts.

Chip is admitted to practice in Alabama (Southern, Middle and Northern Districts), Florida (Southern and Northern Districts) and the District of Columbia as well as the 11th Circuit Court of Appeals and the U.S. Supreme Court.

Chip's wife, Melanie Hinson (Maldonado), is also an attorney and the couple have three grown children and one grandchild.

News from the Southern District

Geraldine Lester retired as Clerk of Court the beginning of January. Ms. Lester served the court for many years and will be missed.

On April 20, 2009 new local rules became effective in the U.S. Bankruptcy Court for the Southern District of Alabama. The rules are posted on the courts website.

The Court recently upgraded their CM/ECF software version to ECF version

3.3.1. Any comments, questions or concerns can be submitted telephonically to the court at (251)

Prior to his appointment as Clerk of Court, Chip was an attorney at the law firm of Hinson & Maldonado in Linden, Alabama, where he handled criminal, civil, and bankruptcy matters. Chip's experience also includes working as an attorney in the Public Defender's Office in Shalimar, Florida; working as a program manager with GTE Government Systems Corporation in Massachusetts where he was responsible for the world-wide communications modernization of U.S. Army tactical units under a \$4.3B program; and retiring after twenty-one years as a U.S. Army Officer in the Army Signal Corps

Recent Opinions from the Southern District of Alabama

Orr v. American General Finance, Inc., (In re Orr) Case No. 98-14150, Adv. Proc. No. 00-1036 (Bankr. S.D. Ala. August 1, 2008 and December 19, 2008)

Debtor filed an adversary proceeding alleging violation of the automatic stay and seeking damages under 11 U.S.C. §362(h). He sought to pursue the case as a class action. The security agreement at issue contained an arbitration clause which forbade class-wide proceedings by the arbitrator. The Debtor maintained that the class action waiver was unconscionable, and the arbitrator should decide whether the waiver was unconscionable. The Defendant argued that the bankruptcy court was the proper forum to decide the unconscionability issue. In two separate opinions, the bankruptcy court first held that the bankruptcy court was the proper forum for the unconscionability issue, finding that the issue goes to the validity of the clause. The court then held that the class action waiver was not unconscionable because §362(h) allows attorney fees and costs which would make pursuing an individual action in arbitration affordable for the Debtor. (J.Shulman)

In re McGhee, Case No. 04-15905 (Bankr. S.D. Ala. Dec. 19, 2008)

Debtor filed a motion to turnover funds under 11 U.S.C. §542 which had been garnished by the Poarch Band of Creek Indians (“the Tribe”). The Tribe responded that

Submissions Wanted

Stream of Commerce is continually looking for articles on current topics in the areas of creditors’ rights and bankruptcy law. If you have any article we can review and possibly publish, please contact:

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it had sovereign immunity from suit and had not waived that immunity. Section 106(a)(1) abrogates sovereign immunity for “governmental units” for enumerated code sections, including §542. However, §101(27), which defines “governmental units”, does not specifically include Indian tribes. The bankruptcy court held that the Tribe was immune from suit under §542 because neither §106(a)(1) or §101(27) expressly include Indian tribes in the abrogation of sovereign immunity, and this abrogation cannot be assumed or implied. (J.Shulman)

Adams v. Hainje’s, Inc. (In re Adams), Case No. 08-11138, Adv. Proc. No. 09-1014 (Bankr. S.D. Ala. April 28, 2009)

The Debtor filed an adversary proceeding alleging violations of

TILA in connection with a retail installment contract. When the Defendant filed a motion to dismiss the complaint based on statute of limitations and res judicata, the Debtor amended the complaint to assert the TILA claims for setoff against the Debtor’s proof of claim. Prior to the filing of the adversary proceeding, the bankruptcy court confirmed the Debtor’s chapter 13 plan which provided for full payment of the Defendant’s secured claim. The bankruptcy court granted the Defendant’s motion to dismiss on grounds that the Defendant’s affirmative TILA claim was outside the one year statute of limitations, and the amended complaint was not asserted to set off the Defendant’s secured claim. Further, the TILA claim was barred by the res judicata effect of the confirmation order. (J.Shulman)

Elgin Federal Credit Union v. Michael D. and Irma D. Horlacher (In re Horlacher), (Case No. 3:08CV173/MCR; Bankr. N.D. Fla.; affirmed by U.S. Dist. Ct. N.D. Fla; March 31, 2009):

Debtor’s filed a voluntary chapter 7, no asset case that failed to include the debt owed to Elgin Fed. Credit Union (“Elgin”) due to attorney inadvertence. The debtors received their discharge prior to Elgin receiving any notice of the bankruptcy. Elgin filed an adversary complaint to have its debt declared nondischargeable, and the bankruptcy court declared the debt nondischargeable based on lack of notice to Elgin. The debtors filed a motion for reconsideration arguing that 11 U.S.C. § 726(a)(2)(C), which permits “tardy” claims, would allow Elgin the opportunity to still

file a claim and permit payment to it in the event of any asset distribution, and its debt would be discharged. The bankruptcy court granted reconsideration based on misapplied law and injustice and ruled the debt was dischargeable. Elgin appealed. The U.S. District Court for the Northern District of Florida affirmed the bankruptcy court's decision to reconsider its original order and affirmed the court's decision that § 726(a)(2)(C) allowed Elgin to file a tardy, but timely, claim, and its debt was dischargeable. (J. Mahoney).

[In re Holiday Isle, LLC \(Case No.: 08-14135; Bankr. S.D. Ala.; January 8, 2009\):](#)

The debtor is the owner of 86 of 144 condominiums in a completed condominium structure. Its main secured creditor moved to have the debtor declared a "single asset real estate" debtor. The court held the debtor's operations, while more than passive, were for the sole purpose of selling its condo units, and this activity made the debtor a SARE as defined by 11 U.S.C. § 105(51B). (J. Mahoney).

[In re Alta Marie Broadus; \(Case No.: 02-15358; Bankr. S.D. Ala.; January 7, 2009\):](#)

The debtor was ordered to pay interest on her tax claim at the statutory rate specified in 11 U.S.C. § 511. The exact numerical percentage rate was never stated by the IRS in any document. The IRS was paid the full amount of its filed proof of claim through the plan but objected to the debtor's discharge arguing the interest on the tax claim survived the discharge. The court held the interest on the federal tax liability

survived the discharge and had to be paid. The IRS, in all future cases, was ordered to specify a numerical percentage for the interest rate owed to be stated in a proof of claim (or amended proof of claim), plan (or amended plan), objection to confirmation or

withdrawal of objection to confirmation, or an order; otherwise, the court will deem the interest debt owed intentionally waived and discharged when the case is completed, unless the United States pleads appropriate grounds for relief under Fed. R. Bankr. P. 9023 or 9024. (J. Mahoney).

Special thanks to Susan Powers, law clerk to Judge Shulman, and Deanne Tolbird Dunson, law clerk to Judge Mahoney, for compiling and summarizing these cases.

Article One

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The Trustee became aware of the proceeding and filed a motion to modify the debtor's plan to secure the settlement proceeds to increase the dividend to the debtor's unsecured creditors.

Citing to the 11th Circuit cases of Telfair v. First Union Mortgage Corp., 216 F.3d 1333 (11th Cir. 2000) and Muse v. Accord Human Resources, Inc., 129 Fed. Appx. 497 (11th Cir. 2005) following the estate transformation approach, the debtor objected to the Trustee's motion to modify the plan arguing that the debtor's post-petition claim was not property of the debtor's estate. The Trustee asked the Court to consider an expansion to the 11th Circuit's transformation

approach to modify the plan for the recovery of the lawsuit proceeds to increase the dividend for unsecured creditors.

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It was the Trustee's contention that if the Court were to rule that post-petition assets are not property of the estate in chapter 13, it would allow some debtors to walk away from chapter 13 with a windfall while paying nothing to their unsecured creditors. By ruling that the asset is not property of the estate, the debtor could argue that if the proceeds are merely

disposable income, then all that is required is an increase in the percentage of the plan, but that the debtor would not actually have to turn over the income to the Trustee to fund the plan because the settlement itself is not property of the estate. The debtors could propose to increase the percentage of the plan with payments over time, take the settlement for their own use, and then later dismiss the case when they cannot afford to make the higher payment, thereby, robbing the creditors of the benefit of the settlement.

Post-petition Claims as Property of the Estate – the conflict

In an effort to persuade the Baxter Court to expand the estate transformation approach, the Trustee cited the case of In re Nott, 269 B.R. 250, 257 (Bankr.M.D.Fla.2000) wherein the debtor received a post-confirmation inheritance totaling between \$275,000.00 and \$300,000.00. The Nott Court held

Property of a chapter 13 estate that is in *existence and disclosed as of the date of confirmation* vests in the Debtor pursuant to Section 1327(b). Any property acquired post-confirmation, however, is property of the estate pursuant to Section 1306(a). Id at 564-565. (emphasis added)

The Nott Court, citing the case of In re Holden, 236 B.R.156, 163(Bankr.D.Vt.1999) went on to say

Upon confirmation of a Chapter 13 plan, all property of the estate is

emptied from the estate and revested in the debtors under Section 1327(b). Such property is no longer property of the estate. Immediately after confirmation, the estate begins to be refilled by property acquired by debtors post-confirmation. That property is protected by the automatic stay and remains so until the case is closed, converted or dismissed.

The issue of whether post-confirmation personal injury claims were property of the bankruptcy estate, and subject to capture by the Trustee was before the Court in In re Harvey, 356 B.R. 557 (Bkrcty.S.D.Ga. 2006). The Harvey Court performed an indepth analysis of Telfair, §1306, §1327, and §554. The Court concluded that while post-confirmation assets become property of the estate under §1306, they are not deemed to retroactively vest in the debtor as of confirmation pursuant to §1327. The 11th Circuit ruled that under the estate transformation approach, the plan confirmation “returns” property to the debtors’ control that property which is not necessary for the fulfillment of the plan. Therefore, the property that is necessary for the completion of the plan “remains” in the estate upon confirmation. The Harvey Court held:

This language, primarily the use of the words “returns” and “remains” illustrates that when properly read, Telfair ruled solely on property that existed, and had been revealed, at or before the

confirmation of the debtor’s Chapter 13 plan.

The Harvey Court then examined the provisions of §554 as instructive to resolve the conflict between Sections 1306 and 1327. The Court held that the provisions of Section 554 “tip the scales in resolving the tension between Sections 1306 and 1327 in a case involving post-confirmation assets.” Id at 564. While property that is not “otherwise administered” by the closing of the bankruptcy case is “abandoned to the debtor,” property that is not scheduled is “never deemed abandoned and remains property of the estate.” Id at 564. The Court held

Therefore, post-confirmation causes of action that become property of the estate under Section 1306 remain property of the estate pursuant to Section 554(d), despite Section 1327, if they are not scheduled and made subject to administration or abandonment.

The Bankruptcy Court’s decision in In re Baxter, 374 B.R. 292 (Bankr. M.D. Ala. 2007) declined to expand the estate transformation approach and ordered that the 11th Circuit’s rulings in Telfair and Muse were binding precedent on the issue. The Baxter Court, citing to Telfair, held that the debtors’ post-petition claim was not property of the estate. However, while not property of the estate, the Court went on to hold the settlement was disposable income for the purposes of the Trustee’s motion to modify plan.

Post-petition Claims as Disposable Income

Since the implementation of BAPCPA, one of the prevailing theories on the “new” disposable income test has been that disposable income is determined by the “means test” and as the means test is based upon the six month average prior to the filing of the case, the disposable income test cannot be modified. Furthermore, there is substantial case law which provides that the disposable income test does not apply to post-confirmation modified plans. With the Court’s ruling in Baxter, these theories have been rejected and disposable income test for modified plans has been clarified.

The Baxter Court held that as §1329 makes the provisions of §1325(a) applicable to modified plans and as §1325(a) captures both the provisions of §1325(a) and §1325(b), that the disposable income test is applicable to modified plans.

The Baxter Court went further in its disposable income analysis for modified plans by holding that disposable income may include property which is not property of the estate, and disposable income must be paid into the plan regardless of the debtor’s claimed exemptions. Baxter, citing to In re Salter, 2007 WL 1076686 (Bankr. M.D. Ala. April 6, 2007).

Property of the Estate – Reconciled

The Baxter case was taken up on appeal to the District Court on the issue of property of the estate. While on appeal at the District Court, the 11th Circuit issued its

opinion in the case of Waldron v. Brown (In re Waldron), 536 F.3d 1239 (11th Cir. 2008), the 11th Circuit held that personal injury or other type claims which are acquired by the debtor as a result of actions which occurred after the chapter 13 plan was confirmed were included in property of the estate, which vest in the estate and remain in the estate until the case ends or is converted.

The 11th Circuit in Waldron first recognizes that §1306 is an expansive definition of what is property of the estate in a chapter 13 case. Furthermore, §1306 “does not mention the confirmation of the debtor’s plan as an event relevant to what assets are property of the estate.” *Id.* The Court went on to clarify that its prior estate transformation ruling in the case of Telfair v. First Union Mortgage Corp., 216 F.3d 1333 (11th Cir. 2000) was an “approach to resolve the tension between Sections 1306(a) and 1327(b) regarding property interests that *existed at confirmation.*” *Id.* (emphasis added). In further explanation of the tension between sections 1306 and 1327 and the effect of vesting upon confirmation, the 11th Circuit goes on to state “new assets that a debtor acquires unexpectedly after confirmation by definition do not exist at confirmation and cannot be returned to him then.”

Following other circuits, the 11th Circuit agrees with the position that after confirmation of the chapter 13 plan, the estate continues to be funded by assets acquired by the debtor post petition as set out in §1306.

While the case is pending, the post-petition property

.... [is] added to the estate until confirmation, the event that triggers [section] 1327(b) and “vests” the property of the estate in the debtor. That is, the property interests comprising the pre-confirmation estate property are transferred to the debtor at confirmation, and this “vesting” is free and clear of claims or interests of creditors provided for by the plan. [section] 1327(b), (c). Finally, the property of the estate once again accumulates property by operation of [section] 1306(a) until the case is “closed, dismissed, or converted.”

After finding that the debtor’s post-petition claim was in fact property of the estate which remains in the estate until the completion of the debtor’s plan, the 11th Circuit went on to hold that the bankruptcy court in Waldron did not abuse its discretion by requiring that the debtor amend his schedules to disclose this new asset to his creditors and the Trustee. The court went on to hold that “the disclosure of post confirmation assets gives the trustee and creditors a meaningful right to request, under section 1329, a modification of the debtor’s plan to pay his creditors.” *Id.*

Conclusion

With BAPCPA, the unsecured creditors have suffered at the hands of the “means test” and the hanging “910 claim” paragraph of §1325. With the 11th Circuit’s ruling in Waldron with regard to

property of the estate and the Bankruptcy Court's Opinion in Baxter and Salter with regard to disposable income, the Trustee is better equipped in his attempts to increase the dividend for unsecured creditors.

Sabrina McKinney is a staff attorney with the Chapter 13 Trustee's Office for the Middle District of Alabama.