

## BANKRUPTCY PRACTICE POINTERS

I was asked to use my recent seminar presentation to the Knoxville Bar Association on chapter 7 developments to construct a "Practice Pointers" article for the KBA Newsletter. Therefore, the thrust of the following article relates to chapter 7 bankruptcy cases, but there are several pointers that should have application for the general practitioner. For the infrequent bankruptcy practitioner, please note that the Bankruptcy Court for the Eastern District of Tennessee is scheduled to go to electronic filing on May 17, 2005. At the same time, new local rules of practice will become effective. You can review the local rules by visiting the court's web site at [www.tneb.uscourts.gov/](http://www.tneb.uscourts.gov/) or you can obtain a copy from the clerk's office. You may also go to this website to find the Eastern District of Tennessee bankruptcy cases described below that do not have a Bankruptcy Reporter citation. Please also note that The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 was introduced in the United States Senate on February 1, 2005 and has already been reported out of the Senate Judiciary Committee. There is a big push by some senators to fast track this legislation, but only time will tell. If it passes in its current form, expect substantial changes to the Bankruptcy Code.

### 1. DO NOT OVERLOOK THE IMPORTANCE OF ACKNOWLEDGMENTS:

Typically, the issue of a defective acknowledgment arises in a bankruptcy case when the trustee seeks to avoid a deed of trust because of a defective acknowledgment. Three recent decisions teach several good lessons on deed acknowledgments. First, **use the correct statutory form**. Second, **correctly fill in the blanks on the form**. Third, **make sure the notary affixes his/her notary seal to the acknowledgment**. *Gregory v. Ocwen Federal Bank (In re Biggs)*, 377 F.3d 515 (6th Cir. 2004). *Limor v. Fleet Mortgage Group (In re Marsh)*, 12 S.W. 3d 449 (Tenn. 2000) and *Lemeh v. EMC Mortgage Corp. (In re Crim)*, 81 S.W. 3d 764 (Tenn. 2002). For the most recent decision from the Eastern District of Tennessee, please see *In re Bushee*, 319 B.R. 542 (Bankr. E.D. Tenn. 2004). *Bushee* contains an excellent review of all of the recent cases.

### 2. DO NOT IGNORE RULE 9011 WHEN ELECTRONIC FILING IS IMPLEMENTED:

If you electronically file a bankruptcy petition for a debtor and you do not have the debtor's original signature on the petition, you may be sanctioned for violation of Bankruptcy Rule 9011. In the case of *Briggs v. LaBarge (In re Phillips)*, 317 B.R. 518 (8th Cir. BAP 2004), an attorney was sanctioned for filing a bankruptcy case without the debtor's permission and without a signed petition from the debtor. "[T]here are no circumstances, including a pending foreclosure sale, that justify an attorney filing a petition without the debtor's signature." In filing a petition electronically, the attorney **"represents to the court that he or she has secured an originally executed petition physically signed by the debtor prior to electronically filing the case."** *In re Wenk*, 296 B.R. 719 (Bankr. E.D. Va. 2002) [emphasis added]. The *Wenk* case equated the electronic filing of a petition without an original signature as fraud, forgery, and a flagrant abuse of the bankruptcy process. Read these two cases before you submit your first case through the e-filing system.

Please also note that electronic service is inadequate when the opposing party's attorney (who participated in the court's electronic filing system) is allowed to withdraw from the case. *McKinnie V. Roadway Express*, 341 F. 3d 553 (6th Cir. 2004).

### 3. JOINT PETITIONS CANNOT BE FILED BY SAME SEX COUPLES:

A Lesbian couple, who legally married in Canada, were not "spouses" for purposes of filing a joint petition under section 302 of the Bankruptcy Code. The Defense of Marriage Act (1 U.S.C. § 7) defines "spouse," for purposes of determining the meaning of any Act of Congress, as a person of the opposite sex who is a husband or a wife. Section 302 of the Bankruptcy Code permits a bankruptcy filing by an individual and such individual's spouse. Therefore, a same sex couple is not eligible for a joint bankruptcy case. Further, DOMA does not violate the due process or the equal protection clause of the Fifth Amendment, the Fourth Amendment, or the Tenth Amendment. *In re Kandau*, 315 B.R. 123 (Bankr. W.D. Wash. 2004).

### 4. BE CAREFUL WHAT YOU FILE IF YOU WANT YOUR ATTORNEY FEES:

Interim compensation awarded to an attorney for fees in representing a chapter 11 debtor are subject to **disgorgement** if the case converts to a chapter 7 case if necessary to insure that all administrative claimants receive their pro-rata share of their claims under 11 U.S.C. § 726(b). Such distribution is mandatory under the statute, not discretionary. *Specker Motor Sales Co. v Eisen*, 393 F.3d 659 (6th Cir. 2004). The attorney for the United States Trustee will be aggressively pursuing disgorgement in appropriate cases, so attorneys should take great care in filing chapter 11 petitions, as the wrong case could result in a big financial loss for the attorney.

### 5. A DEBTOR'S ONLY OPTION IN A CHAPTER 7 CASE MAY BE SURRENDER OF SECURED PROPERTY:

The United States Court of Appeals for the Third Circuit recently ruled that a debtor in a chapter 7 case is not limited to redemption/reaffirmation/exemption options, but instead has the option of retention of collateral while staying current on loan payments. *Price v. Delaware State Police Federal Credit Union (In re Price)*, 370 F.3d 362 (3rd Cir. 2004). The Sixth Circuit follows the view that reaffirmation or redemption are the only means of retaining secured property. *General Motors Acceptance Corp. v Bell (In re Bell)*, 700 F.2d 1053 (6th Cir. 1983).

### 6. KNOW YOUR HOMESTEAD EXEMPTION:

Tennessee has amended its homestead exemption for elderly residents. If you are 62 or older, the exemption is now \$12,500 for an individual and \$20,000 for a husband and wife where one of them is 62 or older and \$25,000 where they are both over the magic age. Tenn. Code Ann. § 26-2-301.

### 7. THE LATEST ON SUBSTANTIAL ABUSE AND GOOD FAITH:

In a recent opinion from the United States Court of Appeals for the Sixth Circuit, the Court further clarified the meaning of "substantial abuse" in section 707(b) of the Bankruptcy Code, which allows the Bankruptcy Court to dismiss an individual case for "substantial abuse" upon motion of the United States Trustee. The Sixth Circuit previously ruled in the case of *In re Krohn* that the court should determine from the totality of the circumstances whether the debtor is merely seeking an advantage over his creditors or is honest in the sense that his relationship with his creditors has been marked by essentially honorable and undeceptive dealings and whether he is needy in the sense that his financial predicament warrants the discharge of his debts in exchange for liquidation of his assets. In other words, "substantial abuse" can be predicated upon either lack of honesty or want of need. *Behlke v. Eisen (In re Behlke)*, 358 F.3d 429 (6th Cir. 2004).

(Continued on page 5)

## Practice Tips (Continued from page 4)

A potential alternate basis for dismissal is a dismissal for cause under § 707(a). The Sixth Circuit has previously ruled that a lack of good faith is a valid "cause" for dismissal. *Indus. Servs., Inc. v. Zick* (In re Zick), 931 F.2d 1124 (6th Cir. 1991) and Judge Parsons has recently applied Zick to dismiss a chapter 7 filing by a doctor. *In re Hebert*, Case No. 04-24261 (February 17, 2005).

### 8. SOME RECENT CASES ON AVOIDANCE ISSUES:

- a. **Preferences.** A release executed in connection with a settlement of pending litigation is not "new value" for purposes of the 547(c)(1) & (4) affirmative defenses (contemporaneous exchange exception and the new value exception) to a preference complaint. "New value" for purposes of 11 U.S.C. § 547(a)(2) must be something of tangible economic value. *Phoenix Restaurant Group v. Fuller, Fuller & Associates*, 316 B.R. 671 (Bankr. M.D. Tenn. 2004). For more on "value," see *Phoenix Restaurant Group v. Lawson Software*, 316 B.R. 681 (Bankr. M.D. Tenn. 2004).

A bank's mortgage that was recorded within the 90-day preference period and related to a refinancing of an existing recorded mortgage held by another lender is avoidable as a preference notwithstanding the bank's equitable subrogation argument. *Superior Bank, FSB v. Boyd* (In re Lewis), 2005 U.S. App. LEXIS 2643 (6th Cir. 2005).

- b. **Strong Arm Powers.** The sole method of perfecting a lien against a mobile home is by notation on the certificate of title under Michigan law. *In re Kroskie*, 315 F.3d 644 (6th Cir. 2003). Tennessee has a lien perfection statute functionally similar to the one interpreted in *Kroskie*. Tenn. Code Ann. § 55-3-126. Furthermore, there is a new Tennessee statute that deals with surrendering titles to mobile homes that requires submission, *inter alia*, of an affidavit of fixation before a mobile home can be considered part of the real estate. Tenn. Code Ann. § 55-3-138.

### 9. UNDUE HARDSHIP DISCHARGE FOR STUDENT LOANS BECOMES MORE DIFFICULT:

In a more recent decision, the Sixth Circuit finally adopted the "Brunner test" that had been used, in part, in the analysis of several previous undue hardship cases and has been adopted by several other Circuit Courts of Appeal. *Oyler v. Educational Credit Management Corporation* (In re Oyler), 2005 WL 241268 (6th Cir.), adopting *Brunner v. New York State Higher Educ. Serv. Corp.*, 831 F.3d 395 (2d Cir.1987). That standard is: (1) that the debtor cannot maintain, base current income and expenses, a "minimal" standard of living for him/her and his/her dependents if forced to repay the loan, (2) that additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loan, and (3) the debtor has made good faith efforts to repay the loans. In examining the second prong of the test, the Oyler court noted that the additional circumstances "must be indicative of a 'certainty of hopelessness,' not merely a present inability to fulfill financial commitment" (such as illness, disability, a lack of useable job skills or the existence of a large number of dependents). Most importantly, the circumstances must be beyond the debtor's control and not borne of free choice.

*Miller v. Pennsylvania Higher Education Assistance Agency* (In re Miller), 377 F.3d 616 (6th Cir. 2004) further expounds on the requirements for a partial hardship discharge of student loans under 11 U.S.C. § 523(a)(8).

### 10. KNOW HOW TO PLEAD YOUR CASE:

Several recent decisions highlight the necessity of proper pleading in discharge and dischargeability cases if the creditor wants to survive

a motion to dismiss. See, *Union Planters Bank v. Harris* (In re Harris), Adv. No. 04-3178 (September 17, 2004; Judge Stair) for standards applicable to a Rule 12(b)(6) motion in the discharge (§ 727(a)(5)) and dischargeability (§ 523(a)(2)(A) & (B) (a)(4) & (6)) context, particularly with respect to averments of fraud; *Lewis v. Brobeck* (In re Brobeck), Adv. No. 03-2045 (July 27, 2004; Judge Parsons) as to claims under § 523(a)(2) & (6); and *Sherwood Metal v. Applegate* (In re Applegate), Adv. No. (December 3, 2004; Judge Parsons) as to claims under § 523(a)(2)(A), (a)(4) & (6).

### 11. TRUSTEES CAN RECOVER COSTS IF YOU IGNORE THEM:

The new local rules that become effective on May 17, 2005, allow for a trustee to recover costs (Rule 3001-(b)(2)) if an adversary proceeding has to be pursued to get a creditor's attention with respect to documentation to demonstrate the existence of a perfected lien. This new rule is similar to a local rule in the Middle District of Tennessee and the court has wide discretion to sanction a party for failure to comply with local rules. *Limor V. Wells Fargo Home Mortgage* (In re Crider), 312 B.R. 630 (M.D. Tenn. 2004).

### 12. PAY ATTENTION TO TIME DEADLINES:

The Bankruptcy Court has no discretion to extend the deadline for filing complaints to object to the dischargeability of debts or a debtor's discharge, even for excusable neglect, when the motion to extend is not filed before the deadline. *Lure Launchers v. Spino*, 306 B.R. 718 (1st Cir. BAP 2004). The only exception to this rule is an equitable tolling that can be applied when a creditor reasonably relies on an erroneously set "second deadline" emanating from the bankruptcy court. *In re Perkins*, 271 B.R. 607 (8th Cir. BAP 2002).

### 13. YES, THE AUTOMATIC STAY CAN BE ANNULLED:

Judge Stair recently ruled that the stay could be annulled (i.e., to make void or nullify; cancel) to retroactively validate a foreclosure sale that occurred two minutes after the debtor filed his 6th bankruptcy case. *In re Dupuy*, 308 B.R. 843 (Bankr. E.D. Tenn. 2004).

### 14. EMPLOYMENT TERMINATION FOR BANKRUPTCY FILING MUST BE "SOLELY" BECAUSE OF THE FILING:

Section 522(b) of the Bankruptcy Code prohibits a private employer from terminating the employment of a person solely because that person has been a debtor in bankruptcy. Rejecting a debtor's assertion that the word "solely" was preternaturally ambiguous, the United States Court of Appeals recently ruled that "solely" means what it says; a person seeking damages for an improper termination under this section must prove that the bankruptcy filing was the sole reason for termination. *White v. Kentuckiana Livestock Market, Inc.*, 397 F.3d 420 (6th Cir. 2005).

### 15. DISCHARGEABILITY OF PAYMENTS REQUIRED UNDER A DIVORCE DECREE:

Various payments required by a divorce decree and labeled as spousal support are much harder to discharge in a bankruptcy case since 1998 and the Sixth Circuit's ruling in *Sorah v. Sorah*, 163 F.3d 397 (6th Cir. 1998). *Sorah* established a three-part test for determining if obligations labeled as support can be discharged. Once the burden is met under this three-part test, a conclusive presumption arises which shifts the burden to the debtor to establish that the amount of the divorce obligation is unreasonable. It makes no difference that the payments in question are by property settlement agreement or court order from an actual trial. No extrinsic evidence may be considered when the obligation is labeled as support and bears the traditional indicia of support (when the presumption applies). *Aken v. Aken*, 2005 Bankr. LEXIS 153 (6th Cir BAP 2004).