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Meeting Location	Date	Time	Topic
King County Bar Association 1200 Fifth Avenue - Suite 700 Seattle, WA	Tuesday, November 8, 2016	12:00 PM to 1:15 PM	The Impact on Consumer Bankruptcies from the Five Supreme Court Cases from the 2014-15 Term

AGENDA

- 12:00 PM** Introductions/Lunch
- 12:10 PM** Presentation: ‘The Impact on Consumer Bankruptcies from the Five Supreme Court Cases from the 2014-15 Term’, by Chief Judge Brian D. Lynch, United States Bankruptcy Court, Western District of Washington
- 1:15 PM** Evaluations & Adjourn

SPEAKER BIOGRAPHY:

Brian D. Lynch, United States Bankruptcy Court, Western District of Washington - Brian D. Lynch was sworn in as a United States Bankruptcy Judge for the Western District of Washington, Tacoma Division, on June 1, 2010. He was appointed Chief Bankruptcy Judge of the District on October 1, 2014. He currently serves on the Ninth Circuit IT Committee, and previously served on the Circuit Bankruptcy Judges Education Committee.

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Recent Supreme Court Decisions Regarding Consumer Bankruptcy and Their Consequences

By Hon. Brian D. Lynch¹

A. *Law v. Siegel*

In *Law v. Siegel*, the Supreme Court considered whether bankruptcy courts have the authority to order that a debtor's exempt assets be used to pay administrative expenses incurred as a result of the debtor's misconduct. The Supreme Court held that courts do not have such authority because "federal law provides no authority for bankruptcy courts to deny an exemption on a ground not specified in the Code." *Law v. Siegel*, 134 S. Ct. 1188, 1197, 188 L. Ed. 2d 146 (2014).

The Chapter 7 debtor, Law, valued his residence at \$363,348, alleged consensual liens of \$147,156 and \$156,929, and claimed a \$75,000 exemption under California's homestead statute. *Id.* at 1193. The Chapter 7 trustee, Siegel, avoided the "fictional and fraudulent" second-position lien via adversary proceeding, and prevailed on costly appeals. *Id.* Siegel subsequently filed a motion to surcharge the entirety of Law's \$75,000 homestead exemption to defray Siegel's attorney's fees totaling over \$500,000, which the Bankruptcy Court for the Central District of California granted pursuant to its authority under 11 U.S.C. § 105(a) and its inherent powers. *In re Law*, 401 B.R. 447, 455 (Bankr. C.D. Cal. 2009).

The Bankruptcy Appellate Panel for the Ninth Circuit and the Ninth Circuit Court of Appeals both affirmed the bankruptcy court's decision. *In re Law*, No. BAP.CC-09-1077-PAMKH, 2009 WL 7751415, at *10 (B.A.P. 9th Cir. Oct. 22, 2009); *In re Law*, 435 F. App'x

¹ Judge Lynch is the chief bankruptcy judge for the Western District of Washington. He acknowledges and thanks his former law clerk Jimmy Zack for his assistance in preparing these materials.

697, 698 (9th Cir. 2011). Those appellate decisions relied heavily on Ninth Circuit precedent authorizing bankruptcy courts to surcharge a debtor's exemptions in exceptional circumstances, such as when a debtor engages in inequitable or fraudulent conduct. *Latman v. Burdette*, 366 F.3d 774, 786 (9th Cir. 2004); *In re Onubah*, 375 B.R. 549, 556 (B.A.P. 9th Cir. 2007); *In re Law*, 2009 WL 7751415 at *7. The Ninth Circuit's *Law* decision directly conflicted with the Tenth Circuit's *Scrivner* decision, in which the Tenth Circuit Court of Appeals held that surcharging a debtor's exempt property is beyond the scope of a bankruptcy court's equitable authority under 11 U.S.C. § 105(a). *In re Scrivner*, 535 F.3d 1258, 1265 (10th Cir. 2008). The Supreme Court granted certiorari, ultimately reversing the Ninth Circuit Court of Appeals in a unanimous decision. *Law v. Siegel*, 134 S. Ct. at 1198.

The Supreme Court began its analysis with 11 U.S.C. § 105(a), which provides bankruptcy courts with authority to carry out provisions of the Bankruptcy Code. *Id.* at 1194. The Supreme Court reasoned that "it is quite impossible" to carry out provisions of the Bankruptcy Code by taking action that the Bankruptcy Code prohibits, and that bankruptcy courts' inherent sanctioning powers are likewise subordinate to the Bankruptcy Code's directives and prohibitions. *Id.* The Supreme Court then turned to 11 U.S.C. § 522(k), which generally provides that exempt assets are not liable for payment of any administrative expense, including trustees' attorney's fees. *Id.* at 1195. On that basis, the Supreme Court concluded that the bankruptcy court exceeded the limits of its authority under 11 U.S.C. § 105(a) and its inherent powers because surcharging Law's exemptions was a violation of 11 U.S.C. § 522(k)'s terms. *Id.* The Supreme Court qualified its holding by acknowledging that "when a debtor claims a state-created exemption, the exemption's scope is determined by state law, which may provide that certain types of debtor misconduct warrant denial of the exemption." *Id.* at 1196-1197.

The Supreme Court recognized the negative effect that *Law v. Siegel* may have on trustees and creditors, both within the context of the particular case, where Siegel was forced to “shoulder a heavy financial burden resulting from Law’s egregious misconduct,” and in the broader context, where “it may produce inequitable results for trustees and creditors in other cases.” *Id.* at 1197. The rationale is that “in crafting the provisions of § 522, ‘Congress balanced the difficult choices that exemption limits impose on debtors with the economic harm that exemptions visit on creditors.’” *Id.* at 1197-1198 (quoting *Schwab v. Reilly*, 560 U.S. 770, 791, 130 S.Ct. 2652, 177 L.Ed.2d 234 (2010)). The Supreme Court also offered hypothetical alternatives to surcharging or denying a debtor’s exemptions, including: denial of discharge under 11 U.S.C. § 727(a)(2)-(6), sanctions under Federal Rule of Bankruptcy Procedure 9011, sanctions under the bankruptcy court’s 11 U.S.C. § 105(a) authority or inherent powers that would survive discharge as post-petition debt, and criminal prosecution under 18 U.S.C. § 152 for fraudulent conduct in a bankruptcy case. *Id.* at 1198.

1. Post-*Siegel v. Law* Decisions Further Limiting Exemption Challenges

Appellate courts have generally interpreted *Law v. Siegel* as a broad prohibition against surcharging or denying a debtor’s exemption without specific statutory authority. *In re Elliott*, 523 B.R. 188, 189 (B.A.P. 9th Cir. 2014) (“*Law v. Siegel* has abrogated Ninth Circuit law such that unless statutory power exists to do so, a bankruptcy court may not deny a debtor's exemption claim or bar a debtor's exemption claim amendment on the basis of bad faith or of prejudice to creditors.”); *In re Baker*, 791 F.3d 677, 682 (6th Cir. 2015) (“*Siegel* prohibits the bankruptcy court from disallowing the debtors’ claimed exemptions because of their alleged bad faith and fraudulent conduct.”). Bankruptcy courts have likewise been proactive in acknowledging the effect *Law v. Siegel* will have in circuits that had previously authorized surcharging or denying

exemptions under 11 U.S.C. § 105(a) and bankruptcy courts' inherent powers. *In re Rivera-Cintron*, No. 6:14-BK-12581-KSJ, 2015 WL 4749217, at *4 (Bankr. M.D. Fla. Aug. 12, 2015) (“the continuing validity of that Eleventh Circuit ruling [*Matter of Doan*, 672 F.2d 831 (11th Cir. 1982)] is dubious at best after the Supreme Court’s decision in *Law v. Siegel*.”). However, *Law v. Siegel* does allow bankruptcy courts to overrule an exemption claim based on the law of a state which is the origin of the claimed exemption. *In re Lua*, 529 B.R. 766, 774 (Bankr. C.D. Cal. 2015) (disallowing a debtor’s amended exemption based on California equitable estoppel law) *aff’d*, 2015 WL 7176005 (C.D. Cal. Nov. 10, 2015).

2. *In re Woolner*

One bankruptcy court has resisted *Law v. Siegel*’s broad implications, arguing that “there is a material and decisive difference between the Bankruptcy Court (a) not having the authority to surcharge a previously allowed and unobjected-to exemption and (b) not having the authority to disallow the exemption in the first place because it was initially claimed fraudulently or in bad faith.” *In re Woolner*, No. 13-57269-WSD, 2014 WL 7184042, at *3 (Bankr. E.D. Mich. Dec. 15, 2014). The *Woolner* court considered *Law v. Siegel* as mere dicta, and declined to follow the lead of courts that have held that bankruptcy courts lack the power to disallow exemptions on the grounds of the debtor’s fraud or bad faith. *Id.* at *4. *Woolner* also reasoned that, for the purposes of applying *Law v. Siegel*, Federal Rule of Bankruptcy Procedure 4003(b)(2) should qualify as the legal equivalent of a Bankruptcy Code provision, and that Rule 4003(b)(2) provides an avenue for denying exemptions based on fraud. *Id.* at *2. While there is no appeal pending in *Woolner*, the Sixth Circuit Court of Appeals has cast doubt on *Woolner*, explaining that regardless of whether the *Woolner* court considers *Law v. Siegel* mere dicta, lower courts are still obligated to follow Supreme Court dicta. *In re Baker*, 791 F.3d at 682. The Sixth Circuit Court

of Appeals ultimately held that *Law v. Siegel* “unambiguously abrogates” Sixth Circuit precedent authorizing bankruptcy courts to use their equitable powers to sanction a debtor’s misconduct by disallowing exemptions, and that to the extent Sixth Circuit precedent conflicts with *Law v. Siegel*, “the Supreme Court has effectively overruled it.” *Id.* at 682-683.

B. *Harris v. Viegelahn*

In *Harris v. Viegelahn*, the Supreme Court held that “a debtor who converts to Chapter 7 is entitled to return of any postpetition wages not yet distributed by the Chapter 13 trustee.” *Harris v. Viegelahn*, 135 S. Ct. 1829, 1835, 191 L. Ed. 2d 783 (2015).

The Chapter 13 debtor, Harris, lost his residence to a post-confirmation foreclosure, but continued to make plan payments in the full amount of \$530 per month from his wages, which included \$352 for a mortgage debt that the Chapter 13 trustee, Viegelahn, was no longer paying. *Id.* at 1836. Those wages that were previously reserved for Harris’ mortgage debt accumulated in Viegelahn’s possession, totaling \$5,519.22 when Harris ultimately exercised his statutory right to convert his case to Chapter 7. *Id.* Ten days after Harris’ conversion, Viegelahn disposed of the accumulated wages by giving \$1,200 to Harris’ counsel, paying herself a \$267.79 fee, and distributing the remaining money to various secured and unsecured creditors. *Id.*

Harris filed a motion for an order directing refund of the accumulated wages Viegelahn had given to his creditors. *Id.* The Bankruptcy Court for the Western District of Texas granted Harris’ motion, and the District Court affirmed. *In re Harris*, 491 B.R. 866, 876 (W.D. Tex. 2013). The Fifth Circuit Court of Appeals reversed the lower courts, holding that postconversion the Chapter 13 trustee must distribute a debtor’s accumulated postpetition wages to his creditors. *In re Harris*, 757 F.3d 468, 470 (5th Cir. 2014). The Fifth Circuit Court of Appeals reasoned that “considerations of equity and policy” rendered the creditors’ claim to the undistributed funds

superior to that of the debtor. *Id.* at 478, 481. The Fifth Circuit’s *Harris* decision directly conflicted with the Third Circuit’s *Michael* decision, in which the Third Circuit Court of Appeals held that a debtor’s undistributed postpetition wages “are to be returned to the debtor at the time of conversion [from Chapter 13 to Chapter 7].” *In re Michael*, 699 F.3d 305, 307 (3rd Cir. 2012). The Supreme Court granted certiorari to resolve that conflict, ultimately reversing the Fifth Circuit Court of Appeals in a unanimous decision. *Harris v. Viegelahn*, 135 S. Ct. at 1836.

The Supreme Court began its analysis with 11 U.S.C. § 348(f), which “all agree, makes one thing clear: A debtor’s postpetition wages, including undisbursed funds in the hands of a trustee, ordinarily do not become part of the Chapter 7 estate created by conversion.” *Id.* at 1837. Unless the conversion is in bad faith, 11 U.S.C. § 348(f) limits a converted Chapter 7 estate to property belonging to the debtor “as of the date” the original Chapter 13 petition was filed. *Id.* Although U.S.C. § 348(f) does not provide explicit guidance concerning the disposition of accumulated wages at the time of conversion, the Supreme Court concluded that the most sensible reading of § 348(f) is that “[o]n conversion, accumulated wages go to the debtor.” *Id.* at 1838.

The Supreme Court also found support under 11 U.S.C. § 348(e), which provides that conversion from Chapter 13 to Chapter 7 terminates the service of the Chapter 13 trustee. *Id.* The Supreme Court reasoned that the disbursement of “payments to creditors” is a core service provided by a Chapter 13 trustee pursuant to 11 U.S.C. § 1326(c), and that 11 U.S.C. § 348(e) strips the Chapter 13 trustee of the authority to provide that service “the moment a case is converted.” *Id.* Returning funds to a debtor, however, is not a Chapter 13 trustee service under 11 U.S.C. § 1326(c). *Id.*

Viegelahn argued that 11 U.S.C. §§ 1327(a) and 1326(a)(2) require terminated Chapter

13 trustees to distributed undisbursed funds to creditors. *Id.* Specifically, 11 U.S.C. § 1327(a) provides that a confirmed Chapter 13 plan “bind[s] the debtor and each creditor,” and 11 U.S.C. § 1326(a)(2) instructs the Chapter 13 trustee to distribute “payment[s] in accordance with the [confirmed] plan.” The Supreme Court determined that those provisions were irrelevant to the issue at hand because, pursuant to 11 U.S.C. § 103(i), Chapter 13’s provisions cease to apply when the debtor converts the case to Chapter 7. *Id.* The Supreme Court also noted that continuing to distribute funds to creditors pursuant to the defunct Chapter 13 plan is not an authorized “wind-up” task under Federal Rule of Bankruptcy Procedure 1019. *Id.* at 1839.

The Supreme Court acknowledged the Fifth Circuit Court of Appeals’ concern that debtors would receive a “windfall” if they could reclaim accumulated wages from a terminated Chapter 13 trustee, responding that “[w]e do not regard as a ‘windfall’ a debtor’s receipt of a fraction of the wages he earned and would have kept had he filed under Chapter 7 in the first place.” *Id.* The Supreme Court also acknowledged that a debtor’s chance of having funds returned is dependent on the Chapter 13 trustee’s speed in distributing payments to creditors: “A trustee who distributes payments regularly may have little or no accumulated wages to return. When a trustee distributes payments infrequently, on the other hand, a debtor who converts to Chapter 7 may be entitled to a sizable refund.” *Id.* These outcomes, the Supreme Court concluded, follow directly from Congress’ decisions to enact 11 U.S.C. § 1307(a), which allows a debtor to convert from Chapter 7 to Chapter 13 “at any time,” and 11 U.S.C. § 348(f), which shields postpetition wages from creditors in a converted Chapter 7 case. *Id.* The Supreme Court also advised creditors that the risk of excess accumulations can be limited by including a schedule in the Chapter 13 plan for regular disbursement of funds. *Id.* at 1839-1840.

A majority of bankruptcy courts have extended *Harris v. Viegelahn* to situations where

the Chapter 13 case was converted before a plan was confirmed, holding that the terminated Chapter 13 trustee must return all undistributed funds to the debtor. *In re Beckman*, 536 B.R. 446, 448 (Bankr. S.D. Cal. 2015); *In re Sowell*, 535 B.R. 824, 826 (Bankr.D.Minn.2015); *In re Beauregard*, 533 B.R. 826, 829 (Bankr.D.N.M.2015).

In the context of post-confirmation dismissal, the majority of courts have distinguished *Harris v. Viegelahn* due to its reliance on 11 U.S.C. § 348, the Bankruptcy Code’s conversion provision, instead analyzing the issue under 11 U.S.C. § 349, the Bankruptcy Code’s dismissal provision; however, the result has largely been the same. Notwithstanding a lack of specific language having to do with what happens to property belonging to the estate in Chapter 13 upon dismissal post-confirmation, courts have held that under 11 U.S.C. § 349(b)(3), post-petition property and wages held by the Chapter 13 trustee at the time of a post-confirmation dismissal must be distributed to the debtor. *In re Edwards*, 538 B.R. 536, 541 (Bankr. S.D. Ill 2015). Unlike conversion under 11 U.S.C. § 348, 11 U.S.C. § 349 does hold out an option for the court: “[u]nless the court, for cause, orders otherwise.” While that language provides the bankruptcy court with some discretion to order payment to creditors or debtors’ attorneys, courts have been hesitant to enter a broad standing order to that effect. Instead of such a standing order, some courts have suggested that a solution for debtors’ attorneys, whether facing conversion or dismissal, “might be to include in their engagement letters an assignment of and security interest in the debtor’s post-petition wages held by the standing trustee...” *In re Beauregard*, 533 B.R. 826, 832 (Bankr. D.N.M. 2015); *In re Edwards*, 538 B.R. at 543 n. 5. The issue which courts will have to face is whether the existence of an assignment or similar device equates to “cause” to require the Chapter 13 trustee to disburse funds to the debtor’s attorney before returning funds to the debtors.

Bankruptcy courts considering situations where the Chapter 13 case was dismissed *before* a plan was confirmed have also distinguished *Harris v. Viegelahn* due to the specific Bankruptcy Code provisions regarding what happens to funds when a case is dismissed pre-confirmation. Those courts have unanimously concluded that, in the context of pre-confirmation dismissal, *Harris v. Viegelahn* does not abrogate § 1326(a)(2), which instructs the Chapter 13 trustee to return undistributed funds to the debtor, after deducting any unpaid claim allowed under 11 U.S.C. § 503(b), if a plan is not confirmed. *In re Brandon*, 537 B.R. 231, 235-236 (Bankr. D. Md. 2015) (“The only decisions of which I am aware that consider pre-confirmation dismissal all agree that *Harris* has no impact in such cases.”); *In re Kirk*, 537 B.R. 856, 859 (Bankr. N.D. Ohio 2015) (“*Harris* does not apply in a chapter 13 case that has been dismissed.”); *In re Ulmer*, No. 15-30220, 2015 WL 3955258, at *1 (Bankr. W.D. La. June 26, 2015) (“this Court finds *Harris* applies only in the instance of conversion.”); *Matter of Hightower*, No. 14-30452-EJC, 2015 WL 5766676, at *5 (Bankr. S.D. Ga. Sept. 30, 2015) (“The Debtor’s reliance on [*Harris v. Viegelahn*] is unavailing. Here, the Debtor’s case was neither confirmed, nor converted to Chapter 7.”).

C. *Bank of America v. Caulkett*

In *Bank of America v. Caulkett*, the Supreme Court held that a Chapter 7 debtor may not void a junior mortgage under 11 U.S.C. § 506(d) when the debt owed on senior mortgages exceeds the present value of the property. *Bank of Am., N.A. v. Caulkett*, 135 S. Ct. 1995, 1997, 192 L. Ed. 2d 52 (2015).

Bank of America v. Caulkett involved consolidated appeals with almost identical facts; the debtors, Caulkett and Toledo-Cardona each had two mortgages on their respective residences, with Bank of America holding wholly underwater junior mortgage liens on each

residence. *Id.* Both debtors filed Chapter 7 petitions and moved to void their junior mortgages under 11 U.S.C. § 506(d). *Id.* The Bankruptcy Court for the Middle District of Florida granted their motions, and the district court and Eleventh Circuit Court of Appeals both affirmed, reasoning that under Eleventh Circuit precedent “a wholly unsecured junior lien—such as the one held here by Bank of America—is voidable under section 506(d).” *In re Caulkett*, 566 F. App’x 879, 880 (11th Cir. 2014) (citing *Folendore v. U.S. Small Bus. Admin.*, 862 F.2d 1537, 1538–39 (11th Cir. 1989) and *McNeal v. GMAC Mortg., LLC*, 735 F.3d 1263, 1265–66 (11th Cir. 2012)); *In re Toledo-Cardona*, 556 F. App’x 911, 912 (11th Cir. 2014). The Supreme Court granted certiorari, ultimately reversing the Eleventh Circuit Court of Appeals in a unanimous decision. *Bank of Am., N.A. v. Caulkett*, 135 S. Ct. at 1997.

The Supreme Court began its analysis with 11 U.S.C. § 506(d), which provides “[t]o the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void.” *Id.* Bank of America’s claims were “allowed,” but the Supreme Court questioned whether they were also “secured” within the meaning of 11 U.S.C. § 506(d). *Id.* The Supreme Court reasoned that “if the value of a creditor’s interest in the property is zero—as is the case here—his claim cannot be a ‘secured claim’ within the meaning of § 506(a),” and because 11 U.S.C. § 506(d) used identical language, “[u]nder that straightforward reading of the statute, the debtors would be able to void the Bank’s claims.” *Id.* at 1999.

Notwithstanding this textual analysis, the Court held that it was nonetheless bound by its previous construction of the term “secured claim” in 11 U.S.C. § 506(d) adopted in *Dewsnup v. Timm*: a “secured claim” is a claim supported by a security interest in property, regardless of whether the value of that property would be sufficient to cover the claim. *Id.* (citing *Dewsnup v. Timm*, 502 U.S. 410, 112 S.Ct. 773, 777, 116 L.Ed.2d 903 (1992)). The Supreme Court refused

to limit *Dewsnup* to only partially-underwater liens, reasoning that *Dewsnup* considered several possible definitions of the term “secured claim” in 11 U.S.C. § 506(d) and settled on a definition that was not intended to be limited in that manner. *Id.* at 2000. The Supreme Court further explained that limiting *Dewsnup* by adopting a new definition of “secured claim” based on the value of the collateral could lead to arbitrary results given the constantly shifting value of real property. *Id.* at 2000-2001.

Although the Supreme Court based its decision on precedent set by *Dewsnup*, the decision revealed an internal debate among some of the justices with *Dewsnup*'s result by mentioning on more than one occasion that the Court had not been asked to overrule *Dewsnup*. *Id.* at 1999, 2001. More explicitly, the Supreme Court's decision included a footnote regarding *Dewsnup* that three of the Supreme Court Justices declined to join, which states that “[f]rom its inception, [*Dewsnup*] has been the target of criticism... Despite this criticism, the debtors have repeatedly insisted that they are not asking us to overrule *Dewsnup*.” *Id.* at 2000.

Following *Bank of America v. Caulkett*, there has been some discussion of whether bankruptcy courts should reexamine if debtors may strip off wholly underwater liens in Chapter 13 cases. *See, e.g., Davis v. Springleaf Fin. Servs. (In re Davis)*, No. 15-40069, 2015 WL 5299458, *2 n. 4 (Bankr. S.D.Ga. Sept. 9, 2015). All of the courts that have considered this issue, however, have concluded that *Bank of America v. Caulkett* is limited to the context of Chapter 7 lien-stripping under 11 U.S.C. § 506(d). *In re Travers*, 541 B.R. 639, 642 (Bankr. E.D. Ky. 2015) (collecting cases).

Moreover, there have been decisions subsequent to *Bank of America v. Caulkett* which further support the idea that if a debtor wishes to strip off an unsecured mortgage, Chapter 13 is the best and only option:

1. *In re Blendheim*

Recently, the Ninth Circuit Court of Appeals held that discharge ineligibility does not prohibit Chapter 13 debtors from taking advantage of the lien-avoidance tools available in a typical Chapter 13 proceeding. *In re Blendheim*, 803 F.3d 477, 481 (9th Cir. 2015).

The Blendheims were “Chapter 20” debtors: who filed a Chapter 7 bankruptcy petition and received a discharge of their unsecured debts, then immediately filed a Chapter 13 bankruptcy petition. *Id.* at 480. In their Chapter 13 case, the Blendheims scheduled their primary residence at a value of \$450,000, subject to two liens: a first-position lien securing a debt of \$347,900, and a second-position lien securing a debt of \$90,474. *Id.* at 481. The first-position lienholder, HSBC, filed a proof of claim, which the Blendheims objected to, alleging that HSBC failed to attach the underlying promissory note to its proof of claim, and that a copy of the promissory note they had previously received appeared to bear a forged signature. *Id.* HSBC never responded to the Blendheims’ claim objection, and the Bankruptcy Court for the Western District of Washington ultimately entered an order disallowing HSBC’s claim. *Id.* The Blendheims subsequently filed an adversary complaint seeking to void HSBC’s first-position lien pursuant to 11 U.S.C. § 506(d), arguing that because HSBC’s claim had been disallowed, its lien secured a claim that is “not an allowed secured claim” and thus the lien could be voided. *Id.*

The Blendheims prevailed on summary judgment, with the bankruptcy court reasoning that HSBC’s timely filed and subsequently disallowed claim presents substantially different circumstances than when a secured creditor chooses not to file a claim at all, and ordering that HSBC’s deed of trust would be void and cancelled upon completion of the Blendheim’s Chapter 13 plan. *Id.* at 482-483. Following a contentious confirmation process, the bankruptcy court confirmed the Blendheims’ eleventh amended Chapter 13 plan, which included a provision

permitting the Blendheims to permanently void HSBC's lien upon completion of the plan. *Id.* at 483. The bankruptcy court ultimately found that the Blendheims plan was proposed in good faith, holding that "it is not *per se* prohibited for Debtors to propose a Chapter 13 plan stripping the First or Second Position Lien on their Residence, notwithstanding their lack of eligibility for a Chapter 13 discharge." *Id.*

On appeal, the District Court for the Western District of Washington focused directly on the question of whether the Blendheims could permanently void HSBC's lien under 11 U.S.C. § 506(d) in the absence of a discharge. *Id.* at 484. The district court affirmed the bankruptcy court's decision, holding that lien avoidance can be accomplished through plan completion regardless of whether the debtor is entitled to a discharge, and reasoning that nothing in the Bankruptcy Code prohibits that conclusion. *Id.* By the time the appellate process had advanced to the Ninth Circuit Court of Appeals, the Blendheims had successfully completed their plan payments and were poised to permanently void HSBC's lien upon the closure of their bankruptcy case, which the Ninth Circuit Court of Appeals stayed pending the outcome of its decision. *Id.* The Ninth Circuit Court of Appeals affirmed the lower courts' rulings regarding lien avoidance and plan confirmation, joining the Fourth and Eleventh Circuits in concluding that Chapter 20 debtors may permanently void liens upon the successful completion of their confirmed Chapter 13 plan irrespective of their eligibility to obtain a discharge. *Id.* at 497 (citing *In re Davis*, 716 F.3d 331, 338 (4th Cir. 2013); *In re Scantling*, 754 F.3d 1323, 1329-1330 (11th Cir. 2014)).

The Court of Appeals first determined that the bankruptcy court had properly voided HSBC's lien under 11 U.S.C. § 506(d), then concluded that Chapter 20 debtors may permanently void liens. *Id.* at 491-492. In reaching this conclusion, the Court of Appeals reasoned that there is no rule, either under the Bankruptcy Code or under circuit precedent, requiring a Chapter 13 case

to end in conversion, dismissal, or discharge. *Id.* at 493. Likewise, nothing in the Bankruptcy Code’s discharge provision, 11 U.S.C. § 524, renders discharge necessary for lien avoidance. Discharge, by definition, affects only *in personam* liability, and has never served to ensure that the various mechanisms for modifying or voiding a creditor’s *in rem* rights remain in place at the conclusion of a Chapter 13 plan. *Id.* at 494-495.

The Court of Appeals also examined whether allowing Chapter 20 debtors to permanently void liens upon completion of their Chapter 13 plans subverts Congress’ intent in enacting BAPCPA. *Id.* at 495. The Court of Appeals declined to broaden 11 U.S.C. § 1328(f) beyond its plain language, reasoning that “[h]ad Congress wished to prevent Chapter 7 debtors from having a second bite at the bankruptcy apple, then it could have prohibited Chapter 7 debtors from filing for Chapter 13 bankruptcy entirely.” *Id.* Instead, Congress only rendered Chapter 20 debtors ineligible for discharge; “if Congress had meant to prohibit Chapter 20 debtors from voiding or modifying creditors’ *in rem* rights, it would not have done so by restricting the availability of a mechanism that by definition only affects *in personam* liability.” *Id.* at 496. The Court of Appeals was confident that its interpretation gave full effect to the intent of BAPCPA, “to prevent abusive serial filings and successive discharges,” explaining that Chapter 20 lien avoidances are still conditioned on the successful completion of Chapter 13 plan payments. *Id.* at 496-497.

2. *In re Free*

The Chapter 20 approach to stripoffs has been given even more potential as a result of a decision by the Ninth Circuit Bankruptcy Appellate Panel in *In re Free*, where the panel rejected the Chapter 13 trustee’s argument that secured debts discharged in a prior chapter 7 should be included in calculating a debtor’s eligibility for a subsequent chapter 13, if there is no value in

the collateral securing the discharged debt. *In re Free*, 542 B.R. 492 (B.A.P. 9th Cir. 2015).

D. Bullard v. Blue Hills Bank

In *Bullard v. Blue Hills Bank*, the Supreme Court held that a bankruptcy court's order denying confirmation of a proposed repayment plan, with leave to amend, is not a "final" order that the debtor can immediately appeal. *Bullard v. Blue Hills Bank*, 135 S. Ct. 1686, 1690, 191 L. Ed. 2d 621 (2015).

Blue Hills Bank held a \$346,000 mortgage on a multifamily house owned by the Chapter 13 debtor, Bullard. *Id.* Bullard's plan proposed splitting Blue Hills Bank's debt into a secured claim in the amount of the house's value, estimated at \$245,000, and an unsecured claim for the remaining balance, approximately \$101,000. *Id.* at 1690-1691. The plan would then pay the secured portion of the claim as a regular mortgage payment surviving discharge, while treating the unsecured portion of the claim the same as any other unsecured debt, receiving approximately \$5,000 over the life of the plan with the remaining balance discharged upon completion of the plan. *Id.* at 1691.

Blue Hills Bank objected to the plan and, after a hearing, the bankruptcy court entered an order denying confirmation of the plan and ordering Bullard to submit a new plan within thirty days. *In re Bullard*, 475 B.R. 304 (Bankr. D. Mass. 2012). Bullard appealed, and the Bankruptcy Appellate Panel for the First Circuit concluded that the order denying confirmation was not a "final order," but nonetheless exercised its discretion to hear the appeal under § 158(a)(3), which allows interlocutory appeals "with leave of the court," ultimately affirming the bankruptcy court's ruling that Bullard's plan could not be confirmed due to the treatment proposed for Blue Hills Bank's claim. *In re Bullard*, 494 B.R. 92, 95 (B.A.P. 1st Cir. 2013). The First Circuit Court of Appeals, however, dismissed the subsequent appeal for lack of jurisdiction, reasoning that the

Bankruptcy Appellate Panel had not certified the appeal under § 158(d)(2), and the order denying confirmation was not a “final order” as required under § 158(d)(1). *In re Bullard*, 752 F.3d 483, 485 (1st Cir. 2014). The Supreme Court granted certiorari, ultimately affirming the First Circuit Court of Appeals in a unanimous decision. *Bullard v. Blue Hills Bank*, 135 S. Ct. at 1696.

The Supreme Court began its analysis with 28 U.S.C. § 158(a), the bankruptcy appeals statute authorizing appeals as of right from “final judgments, orders, and decrees... in cases and proceedings.” *Id.* at 1692. Bullard urged the Supreme Court to adopt a plan-by-plan approach, where each time a bankruptcy court considers a Chapter 13 plan would constitute a separate “proceeding.” Blue Hills Bank advocated for a broader approach, where the relevant “proceeding” encompasses the entire process of considering plans, and only terminates when a plan is confirmed or the case is dismissed for failure to confirm a plan. *Id.*

The Supreme Court agreed with Blue Hills Bank, concluding that “[t]he relevant proceeding is the process of attempting to arrive at an approved plan that would allow the bankruptcy to move forward.” *Id.* The Supreme Court reasoned that only confirmation or dismissal “alters the status quo and fixes the rights and obligations of the parties.” *Id.* Confirmation renders the terms of the plan binding, the preclusive effect of which forecloses relitigation of any issue litigated by the parties and determined by the confirmation order. *Id.* Likewise, dismissal for failure to confirm a plan results in similarly significant consequences: the Chapter 13 debtor loses the possibility of discharge and other benefits, and the automatic stay is lifted and likely limited in a subsequent bankruptcy case. *Id.* at 1692-1693.

In contrast, the effect of denial of confirmation with leave to amend the plan is minimal. *Id.* at 1693. The automatic stay persists, the parties’ rights and obligations remain unsettled, the

trustee continues to collect funds in anticipation of an amended plan's eventual confirmation, and the possibility of discharge lives on. *Id.* The Supreme Court concluded that those circumstances do not fit the description of "final," comparing this stage in the confirmation process to negotiating the purchase of a vehicle: "It ain't over till it's over." *Id.*

In support of this common-sense analysis, the Supreme Court also considered 28 U.S.C. § 157(b)(2)(L), which includes "confirmations of plans" in the list of "core proceedings" statutorily entrusted to bankruptcy judges. *Id.* While not determinative of the ultimate appealability issue, the Supreme Court noted that the absence of any reference to denials of confirmation "suggests that Congress viewed the larger confirmation process as the 'proceeding,' not the ruling on each specific plan." *Id.*

From a policy standpoint, the Supreme Court considered the length of time consumed by appealing a denial of confirmation, often over a year, and concluded that "[a]voiding such delays and inefficiencies is precisely the reason for a rule of finality." *Id.* Furthermore, an appeal would extend the automatic stay, creating an incentive for debtors to appeal denials of confirmation for the purpose of retaining property. *Id.* On the other hand, debtors operating with the knowledge that a denial of confirmation is not appealable may be incentivized to work with creditors and the Chapter 13 trustee to develop a confirmable plan as promptly as possible. *Id.* at 1694.

The Supreme Court also considered an amicus brief filed by the Solicitor General on behalf of the United States. *Id.* The Solicitor General advocated for each plan denial being treated as final, primarily arguing that all orders resolving "contested matters" under Federal Rule of Bankruptcy Rule 9014 should be considered final and immediately appealable. *Id.* The Supreme Court determined that such a broad approach would be implausible, as "the list of contested matters is 'endless' and covers all sorts of minor disagreements." *Id.* The Solicitor

General also argued that the Supreme Court’s rule creates unfair asymmetry, where confirmation allows creditors to appeal immediately, whereas denial leaves the debtor with only the option of drafting an amended plan and seeking confirmation again. *Id.* at 1694-1695. The Supreme Court noted that it is not uncommon for the finality of a decision to depend on which way the decision goes, citing motions for summary judgment as an example, and that creditors in support of a denied plan would be similarly situated to the debtor regarding an interest in appealing the denial of confirmation. *Id.*

Acknowledging that its decision leaves debtors with limited options for obtaining appellate review of denial orders, the Supreme Court conceded that “our litigation system has long accepted that certain burdensome rulings will be ‘only imperfectly reparable’ by the appellate process.” *Id.* at 1695. The Supreme Court was not overly concerned with this outcome, however, because of its “confidence that bankruptcy courts, like trial courts in ordinary litigation, rule correctly most of the time,” and because the amount of money at stake in the plan confirmation process often fails to justify the costs that a system of universal immediate appeals would entail. *Id.*

The Supreme Court concluded its opinion by discussing instances where interlocutory appeals would remain possible when confirmation is denied. *Id.* If the issue preventing confirmation is important enough that it should be addressed immediately, a district court or bankruptcy appellate panel may grant leave to hear an interlocutory appeal pursuant to 28 U.S.C. § 158(a)(3), and a debtor who does not prevail in district court may seek certification to the court of appeals under 28 U.S.C. § 1292(b), the general interlocutory appeals statute. *Id.* Interlocutory appeals to the court of appeals are also possible under 28 U.S.C. § 158(d)(2), which provides the court of appeals discretion to hear the matter when a bankruptcy court, district court, bankruptcy

appellate panel, or the parties acting jointly, certify a bankruptcy court's order to the court of appeals. *Id.* at 1696. Although there is no guarantee that lower courts will certify and accept interlocutory appeals from plan denials, the Supreme Court reiterated its expectation that those courts will do so in appropriate cases. *Id.*

The Supreme Court's reasoning could be applied to a myriad of other orders entered throughout the bankruptcy process. One district court has declined to extrapolate and apply *Bullard v. Blue Hills Bank* beyond the narrow context of appealing a denial of confirmation of a Chapter 13 plan with leave to amend. *In re S. & Headley Associates, Ltd.*, No. BR 14-28225 MBK, 2015 WL 5112725, at *2 (D.N.J. Aug. 31, 2015) (citing *In re Brown*, 916 F.2d 120, 123–124 (3rd Cir.1990) (concluding that an order denying a motion to dismiss is a final appealable order based on circuit precedent, despite agreeing that “much of the reasoning of [*Bullard v. Blue Hills Bank*], extrapolated to the instant context, provides support for the position that the instant appeal is not of a final order.”). Other courts have extended the reasoning of *Bullard v. Blue Hills Bank* to the context of Chapter 11 plan confirmation. *In re R & S St. Rose, LLC*, 621 F. App'x 505, 506 (9th Cir. 2015). *Bullard v. Blue Hills Bank* has also been relied upon as a general reiteration of the binding nature and preclusive effect of plan confirmation. *In re Blendheim*, 803 F.3d 477, 486 (9th Cir. 2015); *In re Schupbach*, 607 F. App'x 831, 835 (10th Cir. 2015); *In re Stewart*, 536 B.R. 273, 276 (Bankr. D. Minn. 2015).

Bullard v. Blue Hills Bank raises the interesting question of whether a debtor, after a court denies confirmation of the debtor's original plan, could acquiesce to confirmation of an unfavorable plan, while reserving the right to appeal that confirmation order. Some support for that can be found in *Baud v. Carroll*, a pre-*Bullard v. Blue Hills Bank* case where the bankruptcy court refused to confirm the debtors' thirty-six-month plan because the above-median-income

debtors' applicable commitment period was sixty months; and the debtors eventually submitted a sixty-month plan in order to avoid dismissal, which the bankruptcy court confirmed. *Baud v. Carroll*, 415 B.R. 291, 296 (E.D. Mich. 2009) *aff'd in part, rev'd in part*, 634 F.3d 327 (6th Cir. 2011). The debtors appealed the confirmation order to the district court, which determined that the debtors were "aggrieved parties" with appellate standing because they had been "directly and adversely affected pecuniarily by the order." *Id.*