**Avoidance Powers In Chapter 13©**

By John P. Gustafson, United States Bankruptcy Judge, Northern District of Ohio, Western Division.

**I. Some Perspective: Chapter 7, Chapter 11 and Chapter 12.**

In Chapter 7 cases, the avoidance rights are generally under the exclusive control of the Chapter 7 Trustee. Debtors have rights under §522(f), because those avoidance rights are specifically given to the debtors by statute. For exemptible property, Chapter 7 debtors also have the limited rights granted by §522(h).

Historically, many courts have limited §506 avoidance actions to the “reorganization” Chapters, based on the holding in *Dewsnup v. Timm*, 502 U.S. 401, 112 S.Ct. 773 (1992). The Supreme Court affirmed *Dewsnup* in *Bank of America, N.A. v. Caulkett*, 135 S. Ct. 1995, 192 L.Ed.2d 52 (2015), but noted that its holding relied, in part, on the fact that the *Caulkett* debtors had not asked the court to overrule *Dewsnup.*  Thus, the scope of §506 avoidance actions in liquidation proceedings could change should the issue come before the Supreme Court again.

In contrast, in Chapter 11 cases, the Debtor-In-Possession (“DIP”) is statutorily defined as having most of the rights and duties of a “trustee”. *See*, §1107(a). Thus, the DIP is able to use all of the avoidance rights that a “trustee” could use - at least until an actual trustee is appointed by the court. *See*, §1101(1); §1107(a).

Similarly, in Chapter 12, Section 1203 confers avoidance powers on debtors by making a Chapter 12 debtor the equivalent (except for certain investigatory duties) to a debtor-in-possession in Chapter 11.

There is less statutory clarity in Chapter 13. “[N]either the trustee nor the debtor have explicit authority under Chapter 13 to bring avoidance actions.” *In re Hansen*, 332 B.R. 8, 14 (10th Cir. BAP 2005). It has been held that a Chapter 13 Trustee “is no mere disbursing agent”. *Matter of Maddox*, 15 F.3d 1347, 1355 (5th Cir. 1994). Instead, “Congress has given the chapter 13 trustee a broad array of powers and duties”. *Id*.; *see* *also*, *In re Andrews*, 49 F.3d 1404, 1408 (9th Cir. 1995). But the exact relationship, and division of powers, between the Chapter 13 Trustee and Debtors is less clear than in Chapter 7 and Chapter 11 cases.  *See*, *In re Keenan*, 364 B.R. 786, 807 (Bankr. D.N.M. 2007)(holding that *Hansen* only prohibits debtor use of the trustee’s strong arm powers under §544 and that debtors can still bring avoidance actions under §522).

Behind all of the issues discussed below is a fundamental question: “What are all these statutory avoidance rights for, if there is no one to enforce them in Chapter 13?”

**II. Looking At The Provisions Of Chapter 13.**

**A. Section 1302(b) - Chapter 13 Trustee Duties**.

Section 1302(b) states:

(b) The trustee shall--

(1) perform the duties specified in sections 704(a)(2), 704(a)(3), 704(a)(4), 704(a)(5), 704(a)(6), 704(a)(7), and 704(a)(9) of this title;

The subsections of §704 listed in §1302(b) do not specifically grant a Chapter 13 trustee the power, or impose upon the trustee a duty, to prosecute avoidance actions. Arguably, that provision would be found in §704(a)(1), which makes it a duty of a Chapter 7 trustee to “collect and reduce to money the property of the estate ...”. Section 1302(b) does not make this one of the duties of a Chapter 13 Trustee – because it is simply omitted from the §1302(b) list.

Instead, the trustee’s power to bring avoidance actions comes from the language of the avoidance provisions themselves, as will be discussed below.

**B. Arguments For And Against Debtors’ Standing: Section 1303 - Debtor’s Rights And Powers “Exclusive Of The Trustee”.**

Section 1303, which defines the rights and powers of a Chapter 13 debtor, lists very specific provisions where debtors have exclusive rights.

Section 1303 states:

Subject to any limitations on a trustee under this chapter, the debtor shall have, exclusive of the trustee, the rights and powers of a trustee under sections 363(b), 363(d), 363(e), 363(f), and 363(l), of this title.

Courts look at Section 1303 from two different perspectives:

1. **The Argument For Debtors Having Standing To Bring Avoidance**

**Actions.**

Section 1303 lists the Debtor as having the exclusive right to “use, sell or lease…property of the estate” under Section 363(b). Courts have held that litigation, and litigation rights, are property of the estate. So, arguably, shouldn’t the right to “use” property of the estate include “litigation rights”, and aren’t avoidance actions just a subset of a Debtor’s litigation rights?

There is also legislative history: “‘[A] floor comment in the legislative history of Section 1303 suggests that this section “does not imply that the debtor does not also possess other powers concurrently with the trustee.’ 124 Cong. Rec. H. 11106 (daily ed. Sept. 28, 1978) (remarks of Rep. Edwards); S17423 (daily ed. Oct 6, 1978) (remarks of Sen. DeConcini).” *In re Binghi*, 299 B.R. 300, 302 (Bankr. S.D.N.Y. 2003).

Furthermore, Section 1306(b) provides that the Chapter 13 Debtor remains in possession of all property of the estate during the case. In Chapter 13, property of the estate not only includes property as defined by §541, but also property acquired after the commencement of the case - like bankruptcy-specific avoidance rights. *See*, §1306(a). Litigation assets are property of the estate, and what does “possession” of these assets mean if it does not allow the Debtor to pursue these avoidance rights through litigation?

This argument is also bolstered by the fact that a Chapter 13 Trustee’s duties do not include a duty, under Section 704(a)(1), to “collect and reduce to money the property of the estate.” Further, courts have noted that policy concerns also support a Chapter 13 debtor’s ability to utilize strong-arm avoidance powers. *See*, *In re Smith*, 2014 WL 1404722, 2014 Bankr. LEXIS 1538 (Bankr. W.D. Ky. April 10, 2014).

1. **The Argument Against Debtors Having Standing To Bring Avoidance**

**Actions.**

“Section 1303, which defines the rights and powers of a Chapter 13 debtor, lists very specific provisions where debtors have exclusive rights. Avoiding powers are not among them.” *In re Hansen*, 332 B.R. 8, 12 (10th Cir. BAP 2005).

“In *Hartford Underwriters Ins. Co. v. Union Planters Bank*, the United States Supreme Court held that, in the context of the bankruptcy code, where a statute ‘names the parties granted the right to invoke its provisions,…such parties only may act.’ 530 U.S. 1, 6, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000).” *In re Lee*, 432 B.R. 212, 215 (D.S.C. 2010); *see also*, *In re Wood*, 301 B.R. 558, 562 (Bankr. W.D. Mo. 2003)(“Significantly, under the rule of *inclusio unius est exclusio alterius*, the plain language of § 547(b) states the “trustee may avoid” preferential transfers—no mention is made in the statute about the debtor having similar rights.”).

The way that Congress gave debtors the power to exercise the avoidance rights of a trustee in Chapter 11 and Chapter 12 were much more direct than the “inference” argument that can be made for debtor standing using §1303. Thus, these indirect arguments are insufficient to overcome the avoidance statutes’ use of the term “trustee”.

Finally, because the rights of a Chapter 13 Debtor under §1303 are “exclusive of the trustee” - does a finding of Debtor standing to exercise avoidance powers based upon causes of action being “property of the estate” that the Chapter 13 Debtor controls, mean that Chapter 13 trustees do NOT have avoidance powers?

**III. Working Backward From The Rest Of The Code To Chapter 13 - Section 103(a) And The Chapter 13 Trustee’s Standing To Exercise Avoidance Powers.**

Section 103(a) states:

(a) Except as provided in section 1161 of this title, ***chapters 1, 3, and 5 of this title apply in a case under chapter*** 7, 11, 12, or ***13 of this title***, and this chapter, sections 307, 362(o), 555 through 557, and 559 through 562 apply in a case under chapter 15.

The argument from §103(a) is: the avoidance sections state that they may be used by the “trustee”. Nothing in Chapter 13 itself limits that power. And, §103(a) specifically makes the provision of Chapter 5 - such as §§544, 547 and 548 - applicable in Chapter 13 cases.

For example: “Section 544(a) of the Bankruptcy Code empowers trustees with the capability to avoid liens that are unperfected as of the date of the bankruptcy petition. 11 U.S.C. § 544(a). Section 103(a) applies chapter 5 in chapter 13 cases, thereby imbuing chapter 13 trustees with the § 544 powers. 11 U.S.C. § 103(a). Avoided transfers are preserved for the benefit of the estate. 11 U.S.C. § 551. Therefore, the Trustee has the capacity to challenge what she alleges is an unperfected lien.” *In re Guiles*, 580 B.R. 466, 469 (Bankr. W.D. Tex. 2017).

This argument from Section 103(a) appears to be the dominant factor in the majority of case law that holds that Chapter 13 Trustees have standing to use avoidance powers.

**IV. Case Law On Chapter 13 Trustees’ Avoidance Powers.**

**A. Chapter 13 Trustees Have The Power To Avoid Transfers Using 544-**

**549.**

“There is general agreement that the Chapter 13 trustee has standing to avoid transfers and recover property under §§ 544 (strong-arm power), 547 (preferences), 548 (fraudulent conveyance) and 549 (postpetition transfers).”

Keith M. Lundin & William H. Brown, *Chapter 13 Bankruptcy*, 4th Edition, §60.1, at ¶ 1, Sec. Rev. June 10, 2004, www.Ch13online.com.

Similarly, Corpus Juris states:

“[T]he omission of 11 U.S.C.A. §704(a)(1) from the Chapter 13 trustee's duties, as enumerated in 11 U.S.C.A. §1302(b)(1), cannot be read so far as to preclude the use of the Chapter 5 avoidance powers by the trustee, and it is left to the Chapter 13 trustee's judgment to determine when it is feasible and efficient to exercise the avoidance powers. The exercise of avoidance powers is consistent with a Chapter 13 trustee's duty, pursuant to statute, to advise and assist the debtor in performance under a plan. Thus, a Chapter 13 trustee may avoid transfers of property or obligations of the debtor under 11 U.S.C.A. § 544, may avoid a preference under 11 U.S.C.A. §547(b), and may recover a fraudulent transfer under the provisions of 11 U.S.C.A. §548.”

8A Corpus Juris Secundum, Bankruptcy, §103 (March, 2015).

Courts have generally held that a Chapter 13 Trustee can exercise avoidance powers:

*In re McCarthy*, 501 B.R. 89, 91 (8th Cir. BAP 2013)(“Generally, a Chapter 13 trustee has standing to bring certain avoidance actions, such as actions under Bankruptcy Code §545(2)”); *In re Geraci*, 507 B.R. 224, 230 n.6 (Bankr. S.D. Ohio 2014)(Section 544(a) is “unambiguous and grants the trustee, not debtors, the powers and rights of a bona fide purchaser” to avoid a transfer of an interest in property or to defeat a mortgage.); *In re Ramsey*, 356 B.R. 217, 227 (Bankr. D. Kan. 2006)(“the Chapter 13 Trustee is empowered to exercise Chapter 5 avoiding powers”); *Hamilton v. Washington Mutual Bank, FA (In re Colon)*, 345 B.R. 723, 726 (Bankr. D. Kan. 2005)(Chapter 13 Trustee’s powers are fixed as of the commencement of the case, and are not lost when the Chapter 13 Plan prevents the property in issue from revesting in the Debtor); *In re Ryker*, 315 B.R. 664, 670 (Bankr. D.N.J. 2004)(“Equally clear is the ability of the Chapter 13 trustee to employ the avoidance powers.”); *In re Huntzinger*, 268 B.R. 263, 265-266 (Bankr. D. Kan. 2000)(“only the trustee could file the complaint under § 544.”); *In re Griner*, 240 B.R. 432, 438 n.3 (Bankr. S.D. Ala. 1999)(“only chapter 13 trustees may exercise the avoiding powers in 11 U.S.C. §§544, 545, 547, 548, and 549.”); *In re Bonner*, 206 B.R. 387, 388 (Bankr. E.D. Va. 1997)(“That the avoidance powers of §544 extend to trustees in Chapter 13, however, has become well settled.”); *Lucero v. Green Tree Fin. Serv. Corp. (In re Lucero)*, 199 B.R. 742, 744–45 (Bankr.D.N.M.1996), *rev'd on other grounds*, 203 B.R. 322 (10th Cir. BAP 1996); *In re Bell*, 194 B.R. 192 (Bankr. S.D. Ill. 1996); *In re Driver*, 133 B.R. 476, 478 (Bankr. S.D. Ind. 1991)(standing Chapter 13 trustee, not the debtor, holds the lien avoiding powers); *Matter of Ware*, 99 B.R. 103, 105 (Bankr. M.D. Fla. 1989)(“[T]he Chapter 13 debtor may exercise the avoiding powers of the trustee enumerated in Section 547.”); *In re Johnson*, 26 B.R. 381 (Bankr. Colo. 1982)(court disagreed with Chapter 13 trustee’s argument that she did not have the power to avoid a transfer under §548).

**B. When should Chapter 13 Trustees consider using their avoidance powers?**

**1.** Situations where the avoidance action will benefit the estate.

**2.** When the avoidance action will assist the Debtor in performance under the Plan.

**3.** Where avoidance is necessary if the Debtor is going to meet the requirements of the Best Interest Test.

**4.** In cases where a security interest is not properly perfected.

**5.** When the Debtor has no incentive to act, or is actively adverse to the avoidance action.

**6.** Others?

**C. Problems In Creating A Benefit To The Estate Through Avoidance Actions In Chapter 13.**

“The value of the avoided lien is automatically preserved for the benefit of the estate. However, Chapter 13 does not authorize the Trustee to liquidate property. Thus, the Chapter 13 Trustee may not recover the value of the lien by selling it. Instead, the Chapter 13 Trustee's avoidance of an unperfected lien, specifically under §544, benefits the estate by either one of two ways allowed under the Code. First, avoidance of the lien nullifies the security transaction. Accordingly, the portion of the debtor's income (or allocation in the plan) to pay the secured claim is no longer required to be paid to the defendant creditor. The resulting increase in disposable income available to pay creditors holding allowed claims under the Chapter 13 plan is a benefit to the estate. The second way the Chapter 13 Trustee may realize the benefit of an avoided lien for the estate is triggered by the debtor's desire to retain the property. Under the "best interests of creditors" test, the Code assures that unsecured creditors will receive at least as much as they would receive if the case were liquidated under Chapter 7. Thus, if a Chapter 13 debtor elects to retain property subject to an avoided and preserved lien now held by the Trustee, the debtor must pay into the plan the value of the lien.”

*In re Ramsey*, 356 B.R. 217, 227 (Bankr. D. Kan. 2006).

There is case law specifically holding that a Chapter 13 Trustee may use avoidance powers, even when doing so may disadvantage the Debtor:

[T]he Trustee's ability to exercise her avoidance power does not hinge on the avoidance's effect on the Debtor. The Trustee's avoidance of a lien is not at odds with her §1302(b)(4) duty to “advise ... and assist the debtor in performance under the plan.” *See* *Ferrell v. Countryman*, 398 B.R. 857, 867 (E.D. Tex. 2009) (explaining that chapter 13 trustees are not disinterested bystanders post-confirmation, but instead should advise the debtor about matters including payment reductions or suspensions, credit problems, collection efforts, and executory contracts). This duty does not mandate that a trustee refrain from the exercise of other powers; a trustee's primary duty is to maximize the value of the estate, not to serve as additional debtor's counsel. *Commodity Futures Trading Comm'n v. Weintraub*, 471 U.S. 343, 352, 105 S.Ct. 1986, 85 L.Ed.2d 372 (1985). The Code does not require that a trustee weigh every action against its potential impact on the debtor, to the possible detriment of the estate. Therefore, when avoiding a lien is in the best interest of the estate, a trustee may pursue the avoidance. The Court finds that the Trustee has standing to object to the claim and to attempt to avoid the lien.

*In re Guiles*, 580 B.R. 466, 469-470 (Bankr. W.D. Tex. 2017).

**D. Problems Associated With Chapter 13 Trustees Obtaining Compensation For Work Done Litigating Avoidance Issues.**

Chapter 13 Trustees face statutory barriers to receiving additional compensation for work undertaken in pursuing avoidance actions. Unlike Chapter 7 Trustees, where there are structural incentives (in addition to statutory duties) to bring avoidance actions, there are limits on compensation in Chapter 13 for work done as “attorney for the trustee”.

Section 330, which deals with the expenses of a trustee, is “subject to sections 326 . . .”. Section 326(b) appears to prohibit a bankruptcy court from allowing compensation or reimbursement of expenses of a standing Chapter 13 Trustee appointed by the U.S. Trustee under 28 U.S.C. §586(b). Accordingly, the usual power of the bankruptcy court to award trustee compensation and reimbursement of expenses under §330 is not available when the U.S. trustee has appointed a standing Chapter 13 Trustee. *See* *generally*, Keith M. Lundin & William H. Brown, *Chapter 13 Bankruptcy*, 4th Edition, § 60.1, at ¶¶7 - 12, Sec. Rev. June 10, 2004, [www.Ch13online.com](http://www.Ch13online.com).

It is unclear as to whether compensation of the Chapter 13 Trustee could be dealt with through a Plan provision. *Id*. at ¶13. If the Debtor’s Plan is asking the Chapter 13 Trustee to pursue an avoidance action, providing compensation for taking that action in the Plan might be used as an incentive for the Trustee to not object to a “let’s you and him fight” provision.

**V. Where There Is No Question Re: Debtor’s Standing - Section 522.**

**A. Avoidance Under Section 522(h) & (g).**

Section 522(h) states:

(h) The debtor may avoid a transfer of property of the debtor or recover a setoff to the extent that the debtor could have exempted such property under subsection (g)(1) of this section if the trustee had avoided such transfer, if--

(1) such transfer is avoidable by the trustee under section 544, 545, 547, 548, 549, or 724(a) of this title or recoverable by the trustee under section 553 of this title; and

(2) the trustee does not attempt to avoid such transfer.

In turn, Section 522(g) provides:

(g) Notwithstanding sections 550 and 551 of this title, the debtor may exempt under subsection (b) of this section property that the trustee recovers under section 510(c)(2), 542, 543, 550, 551, or 553 of this title, to the extent that the debtor could have exempted such property under subsection (b) of this section if such property had not been transferred, if—

(1)(A) such transfer was not a voluntary transfer of such property by the debtor; and

(B) the debtor did not conceal such property; ....

If a Debtor can meet the requirements of Section 522(h), which references Section 522(g), then there is no question about the Debtor’s ability to avoid qualifying transfers. *In re Dickson*, 655 F.3d 585, 592 (6th Cir. 2011); *Matter of Hamilton*, 125 F.3d 292, 297 (5th Cir. 1997)(“In section 522(h), Congress granted debtors the authority to exercise section 544 avoidance powers under specific and limited circumstances.”); *In re DeMarah*, 62 F.3d 1248, 1250 (9th Cir. 1995)(“Section 522(h) allows the debtor to avoid certain transfers of exempt property.”); *In re McCarthy*, 501 B.R. 89, 91 (8th Cir. 2013)(“Bankruptcy Code §522(h) allows debtors to avoid certain transfers of exempt property. A debtor may have standing under §522(h), to bring certain avoidance actions, such as those under §545.”); *In re Giachchetti*, 584 B.R. 441, 447 (Bankr. D. Mass. 2918)(avoiding the more difficult issue of derivative standing because §522(h) clearly applied); *In re Ryker*, 315 B.R. 664, 672 (Bankr. D.N.J. 2004)(“Section 522(h) permits a debtor to avoid a transfer of property to the extent the debtor could have exempted the property under §522(g)(1).”).

**1. The Elements Of Section 522(h).**

“Some courts have described §522(h) as being composed of five (5) elements: (1) the transfer was not a voluntary transfer of property by the debtor; (2) the debtor did not conceal the property; (3) the trustee did not attempt to avoid the transfer; (4) the transferred property is of a kind that the debtor would have been able to exempt from the estate if the trustee had avoided the transfer under §522(g); and (5) the debtor seeks to exercise one of the trustee's avoidance powers enumerated in §522(h). *See,* *Matter of Hamilton*, 125 F.3d 292, 297 (5th Cir.1997); *In re DeMarah*, 62 F.3d 1248, 1250 (9th Cir.1995); *In re Steck*, 298 B.R. 244, 248–249 (Bankr.D.N.J.2003).” *In re Funches*, 381 B.R. 471, 492 n.32 (Bankr. E.D. Pa. 2008).

Stated with slightly different wording:

“[A] Chapter 13 debtor has standing to avoid a transfer under § 522(h) if five conditions are met: (1) the transfer was not voluntary; (2) the transfer was not concealed; (3) the trustee did not attempt to avoid the transfer; (4) the debtor seeks the avoidance pursuant to §§544, 545, 547, 548, 549, or 724(a) of the Bankruptcy Code; and (5) the transferred property is of a kind that the debtor would have been able to exempt from the estate if the trustee had avoided the transfer under one of the provisions in §522(g). *Kildow v. EMC Mortg. Corp. (In re Kildow)*, 232 B.R. 686, 692–93 (Bankr.S.D.Ohio 1999).” *In re Dickson*, 655 F.3d 585, 592 (6th Cir. 2011).

*See also*, *In re McCarthy*, 501 B.R. 89, 91-92 (8th Cir. BAP 2013)*; LaBarge v. Benda (In re Merrifield )*, 214 B.R. 362, 365 (8th Cir. BAP 1997); *Matter of Varquez*, 502 B.R. 186, 190 (Bankr. D.N.J. 2013)(“Under sections 522(g) and (h) of the Bankruptcy Code, Chapter 13 debtors have the authority to avoid a transfer in place of the Chapter 13 trustee, in the event that the debtors could have exempted the property if the trustee had successfully prosecuted the avoidance action.”).

**2. Does the Debtor have a right to claim an exemption in the property?**

Whether or not a debtor has the right to claim an exemption will generally turn on two factors: 1) is there an exemption applicable to the property in issue; and, 2) was the transfer of the property “voluntary”?

Under §103(a), Section 522(g) is applicable to cases under Chapters 7, 11, 12, and 13 of the Bankruptcy Code. Thus, in evaluating any avoidance action, it is critical to make the distinction between an involuntary transfer (where a Debtor may have exemption rights) and a voluntary transfer (which deprives the Debtor of exemption rights under §522(g)(1)(A)). (This distinction is also important in evaluating what a Chapter 7 Trustee would do in a hypothetical liquidation - pursuing an involuntary transfer, like a garnishment, would not be undertaken if the Debtor could exempt any monies that were recovered. In contrast, a Chapter 7 Trustee would not be worried about a Debtor claiming an exemption in evaluating whether or not to take action to avoid the voluntary transfer of a car to mom for $1 because no exemption could be taken under §522(g).)

*See generally, In re McCarthy*, 501 B.R. 89 (8th Cir. BAP 2014).  Chapter 13 Debtor had standing to pursue avoidance claim in aid of exemption rights.

**B. Avoidance Under Section 522(f).**

Section 522(f) specifically gives ***debtors*** the power avoid the fixing of certain liens.

**1. Judicial liens that impair an exemption [§522(f)(1)(a)].**  The lien avoidance power provided by Section 522(f)(1) “enables the debtor to extinguish or partially avoid the judicial lien of a creditor in property that would otherwise be exempt but for the creditor's lien.” *In re Steck*, 298 B.R. 244, 248-249 (Bankr. D.N.J. 2003).

Section 522(f) lien avoidance applies in Chapter 13 cases. *In re Hall*, 752 F.2d 582, 589-90 (11th Cir.1985); *In re Steck*, 298 B.R. 244, 249-250 (Bankr. D.N.J. 2003)(“Section 103(a) provides that § 522(f) applies to all bankruptcy cases, and it is settled law that a Chapter 13 debtor can utilize § 522(f) to avoid a judicial lien that impairs an exemption, or a nonpossessory, non-purchase money security interest in household goods that would be exempt property under applicable law.”).

Other circuits addressing lien avoidance in Chapter 13 have simply assumed that a chapter 13 debtor may avoid liens under §522(f). *See*, *In re McKay*, 732 F.2d 44, 48 (3rd Cir.1984); *Mead v. Mead*, 974 F.2d 990, 991-92 (8th Cir.1992); *In re Billings*, 838 F.2d 405, 406 (10th Cir.1988).

When a debtor seeks to avoid a lien to the extent that it impairs his permitted exemptions, he does not utilize any avoidance powers derived from the trustee. *In re Tash*, 80 B.R. 304, 306 (Bankr.D .N.J.1987).

**2. Nonpossessory, nonpurchase money security interests in household goods, “tools of the trade” and professionally prescribed health aids [§522(f)(1)(B)].**

*See*, *In re Bland*, 793 F.2d 1172 (11th Cir. 1986)(en banc); *Matter of Ambrose*, 179 B.R. 982 (Bankr. S.D. Ga. 1995).

**3. Does a Chapter 13 Trustee also have standing to avoid liens under §522(f)?**

Yes. *Matter of Maddox*, 15 F.3d 1347, 1355-56 (5th Cir. 1994); *In re Kennedy*, 139 B.R. 389, 390-392 (Bkrtcy. N.D. Miss. 1992). However, a Chapter 13 Trustee does not generally take actions that will only benefit the Debtor - and, in most cases, Section 522(f) avoidance does not benefit the unsecured creditors in a Chapter 13 case.

**VI. The Statutory Basis For, And Against, Chapter 13 Debtors Exercising**

**Avoidance Powers.**

1. **Debtors Have Standing To Litigate Avoidance Actions Under §§544-549 – The “Holistic Approach” Of *In Re Cohen*.**

At present, the leading case for expanding Debtor standing, beyond that provided by Section 522(h), is *In re Cohen*, 305 B.R. 886 (9th Cir. BAP 2004).

In holding that Chapter 13 Debtors generally have standing to pursue avoidance actions, the *Cohen* decision found the following factors to be persuasive:

(1) The chapter 13 debtor remains in possession of all property of the estate during the case. §1306(b).

(2) The one chapter 7 trustee duty that is omitted from the duties of the chapter 13 trustee or debtor is the §704(1) duty to “collect and reduce to money the property of the estate.” This is the duty that obliges chapter 7 trustees to pursue avoiding actions.

(3) Chapter 13 debtors have, exclusive of the trustee, the rights and powers of a trustee to deal with “property of the estate” (after notice and a hearing) not in the ordinary course of business. §1303.

(4) The chapter 13 “property of the estate” that, as noted, remains in the debtor's possession, includes all of the property designated by §541 that existed when the petition was filed and that is acquired postpetition before the case is closed, dismissed, or converted and includes postpetition personal service income. §1306(a). It follows that chapter 13 “property of the estate” includes interests in property that the trustee recovers under the trustee avoiding powers. §541(a)(3).

(5) Under the so-called “best interest” test for chapter 13 plan confirmation, the plan must provide for distributions under it on account of allowed unsecured claims that are of a value of at least what would be paid on unsecured claims in a hypothetical chapter 7 liquidation on the effective date of the plan. §1325(a)(4). It would be an odd system that would require a chapter 13 debtor to depend upon the recovery of an avoidable transfer in order to have a confirmable plan but not permit the debtor to avoid the transfer.

“If we regard §1303 as ambiguous and look at legislative history for guidance, a strong case for debtor standing to assert trustee avoiding powers becomes a compelling case.” *Cohen*, 305 B.R. at 899.

There is legislative history that the designation in §1303 of rights and powers that chapter 13 debtors have exclusive of the trustee “does not imply that the debtor does not also possess other powers concurrently with the trustee” and that “[f]or example although [§323] is not specified in section 1303, certainly it is intended that the debtor has the power to sue and be sued.” 124 CONG. REC. H11106; *id*. S. 17423.

**B. The Majority Of Courts Reject The *Cohen* Analysis.**

**1.** There is a limited provision for Debtor avoidance under Section 522(h). Why would Congress create that limited right if a larger general right to use avoidance powers was intended?

**2.** The plain language of the avoidance provisions apply to Trustees, not Debtors. And, unlike in Chapter 11 and 12, there is no similar clear provision (other than Section 522(h)) that gives Debtors the power to use those avoidance provisions.

**3.** *Hartford Underwriters Ins. Co. v. Union Planters Bank* held that, in the context of the bankruptcy code, where a statute “names the parties granted the right to invoke its provisions, ... such parties only may act.” 530 U.S. 1, 6, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000). One of the most powerful criticisms of *Cohen* is its failure to address the *Hartford Underwriters* holding in the context of Sections 544 to 549 only providing avoidance rights to “trustees”.

One court summarized the statutory argument against *Cohen* as follows: “[I]n §522(h), Congress specifically authorized a chapter 13 debtor to exercise the trustee's avoidance powers in limited circumstances. Given this narrow exception, contrasted with the general grant of authority to chapter 11 and 12 debtors, it is clear that Congress knew how to grant a chapter 13 debtor the general duties and powers of a trustee but chose not to.” *In re Salaymeh*, 361 B.R. 822, 826 (Bankr. S.D. Tex. 2007)(citing *In re Hamilton*, 125 F.3d 292, 297 n.5 (5th Cir. 1997)).

**VII. A Deeper Dive Into The Case Law On The Avoidance Powers of the Chapter 13 Debtors.**

**A. The Majority Rule: Debtors do not have standing to use avoidance powers under Sections 544 - 549:**

“The better reasoned decisions hold that, in contrast to the provisions authorizing a chapter 13 debtor to pursue causes of action that are property of the estate, none of the provisions of chapter 13 authorize a chapter 13 debtor to sue on a trustee's avoidance powers (under, for example, 11 U.S.C. §§544 (unperfected liens), 547 (preferences), or 548 (fraudulent conveyances)) other than pursuant to 11 U.S.C. §522(h).” *Dawson v. Thomas (In re Dawson)*, 411 B.R. 1, 24 (Bankr. D.D.C. 2008); *see* *also*, *Knapper v. Bankers Trust Co. (In re Knapper)*, 407 F.3d 573, 583 (3d Cir. 2005)(right to proceed under §544 not conferred on Chapter 13 Debtors); *Estate Constr. Co. v. Miller & Smith Holding Co.*, 14 F.3d 213, 220 (4th Cir. 1994)(§548 “cannot be enforced by a debtor”); *Stangel v. United States (In re Stangel)*, 219 F.3d 498, 501 (5th Cir. 2000), *cert. denied*, *Stangel v. United States*, 532 U.S. 910, 121 S.Ct. 1240, 149 L.Ed.2d 147 (2001)(case law strongly suggests that Debtor “does not have standing under a plain reading of §545); *Hansen v. Green Tree Servicing, LLC (In re Hansen)*, 332 B.R. 8 (10th Cir. BAP 2005); *In re Lee*, 432 B.R. 212 (D.S.C. 2010)(Chapter 13 Debtor did not have standing to exercise trustee’s strong-arm avoidance powers under §544), *aff’d on other grounds*, 461 Fed. Appx. 227 (4th Cir. Jan. 6, 2012); *In re Dobbs*, 597 B.R. 74 (Bankr. E.D.N.Y. 2019); *In re Kalesnik*, 571 B.R. 491, 496 (Bankr. D. Mass. 2017); *In re Cole*, 563 B.R. 526, 529 (Bankr. W.D.N.C. 2017); *In re Atkins*, 525 B.R. 594, 603 (Bankr. E.D. Pa. 2015); *In re Thompson*, 499 B.R. 908, 912 (Bankr. S.D. Ga. 2013); *In re Turner*, 490 B.R. 1 (Bankr. D.D.C. 2013)(Chapter 13 debtor could not exercise trustee’s strong-arm powers under §544 to avoid unperfected deed of trust); *In re Ryker*, 315 B.R. 664, 668 (Bankr. D.N.J. 2004); *In re Binghi*, 299 B.R. 300, 302-303 (Bankr. S.D.N.Y. 2003); *Montoya v. Boyd (In re Montoya)*, 285 B.R. 490, 493 (Bankr. D.N.M. 2002)(Chapter 13 debtors lacked standing to bring §548 avoidance proceeding.); *In re Bell*, 279 B.R. 890, 898 (Bankr. N.D. Ga. 2002); *Miller v. Brotherhood Credit Union (In re Miller)*, 251 B.R. 770, 772 (Bankr. D. Mass. 2000)(“I find persuasive those cases which do not permit a Chapter 13 debtor to bring an independent avoidance action. I agree that, absent a specific grant of authority in the Bankruptcy Code, a Chapter 13 debtor cannot bring an avoidance action independent of section 522(h).”); *Hacker v. Hodges (In re Hacker)*, 252 B.R. 221, 223 (Bankr. M.D. Fla. 2000); *In re Hill*, 152 B.R. 204, 206 (Bankr. S.D. Ohio 1993)(“Congress did not intend for debtors to have authority to avoid preferences under § 547"); *Matravers v. United States (In re Matravers)*, 149 B.R. 204, 207 (Bankr. D. Utah 1993)(Chapter 13 debtor had standing to avoid unauthorized postpetition transfer of property under §549.); *In re Redditt*, 146 B.R. 693, 696 (Bankr. S.D. Miss. 1992)(there is no specific statutory grant of power giving a chapter 13 debtor avoidance powers); *In re Driver*, 133 B.R. 476, 478 (Bankr. S.D. Ind. 1991); *In re Tillery*, 124 B.R. 127, 128 (Bankr. M.D. Fla. 1991) (§1303 does not include the power of avoidance granted by §544); *In re Bruce*, 96 B.R. 717 (Bankr. W.D. Tex. 1989); *In re Mast*, 79 B.R. 981 (Bankr. W.D. Mich. 1987).

**B. The Minority Rule: Debtors Do Have Standing To Use Avoidance Powers Under Sections 544 - 549:**

*In re Cohen*, 305 B.R. 886 (9th Cir. BAP 2004); *In re Barbee*, 461 B.R. 711, 714-716 (6th Cir. BAP 2011); *Countrywide Home Loans v. Dickson (In re Dickson)*, 427 B.R. 399, 403-406 (6th Cir. BAP 2010)(derivative standing properly allowed), *aff'd on other grounds*, 655 F.3d 585 (6th Cir. 2011); *In re Zubenko*, 528 B.R. 784, 787 n.3 (Bankr. E.D. Cal. 2015)(following *Cohen*); *Thacker v. United Companies Lending Corp.*, 256 B.R. 724, 728–29 (W.D. Ky. 2000); *In re Bonner*, 206 B.R. 387, 387-389 (Bankr. E.D. Va. 1997)(Chapter 13 debtor or trustee may exercise the avoidance powers); *In re Tillery*, 124 B.R. 127 (Bankr. M.D. Fla. 1991); *Freeman v. Eli Lilly Fed. Credit Union*, 72 B.R. 850, 853–55 (Bankr. E.D. Va. 1987); *In re Weaver*, 69 B.R. 554 (Bankr. W.D. Ky. 1987); *In re Ottaviano*, 68 B.R. 238 (Bankr. D. Conn. 1986); *In re Einoder*, 55 B.R. 319 (Bankr. N.D. Ill. 1985); *In re Boyette*, 33 B.R. 10 (Bankr. N.D. Tex. 1983); *In re Colandrea*, 17 B.R. 568 (Bankr. D. Md. 1982).

**C. The Supreme Court’s Decision In *Hartford Underwriters*  - Has The Old Majority/Minority “Split” Changed To A Modern Trend For The Majority View?**

“In *Hartford Underwriters Ins. Co. v. Union Planters Bank*, the United States Supreme Court held that, in the context of the bankruptcy code, where a statute ‘names the parties granted the right to invoke its provisions, ... such parties only may act.’ 530 U.S. 1, 6, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000). Decisions since *Hartford* have trended toward a different result, finding that a debtor lacks a trustee's avoidance powers under Chapter 5.” *In re Lee*, 432 B.R. 212, 215 (D.S.C. 2010); *see also*, *In re Hansen*, 332 B.R. 8, 11 n.13 (10th Cir. BAP 2005)(citing *Ryker*); *Ryker v. Current (In re Ryker)*, 315 B.R. 664, 667 (Bankr. D.N.J. 2004)(characterizing as “growing majority” the view that Chapter 13 debtors lack authority to utilize the trustee avoidance powers.); *but* *see*, *In re Simmons*, 560 B.R. 308, 311 (Bankr. S.D. Ohio 2016)(“It is not controversial that chapter 13 debtors may be granted derivative standing to pursue avoidance actions, using a trustee's powers under Code Section 544. This concept is so well settled that it has been enshrined within the Court's [Mandatory Form Plan].”).

**D. If The Chapter 13 Trustee “Unjustifiably Refuses” – Does That Give The Debtor The Right To Request “Derivative Standing” And Proceed Under “Derivative Rights”?**

**Yes:**

*“*[T]he bankruptcy court properly granted the Debtor derivative standing to pursue lien avoidance under 11 U.S.C. §§ 544 and 547.” *Countrywide Home Loans v. Dickson (In re Dickson)*, 427 B.R. 399 (B.A.P. 6th Cir.2010)*, aff'd on other grounds*, 655 F.3d 585, 593(6th Cir.2011); *see* *also*, *Isaacs v. DBI-ASG Coinvestor Fund, III, LLC* (*In re Isaacs*), 895 F.3d 904, 916 (6th Cir. 2018)(“the ability to confer derivative standing ... is a straightforward application of bankruptcy courts’ equitable powers,” among which is the power “to craft flexible remedies in situations where the [Bankruptcy] Code’s causes of action fail to achieve their intended purpose.”); *In re Barbee*, 461 B.R. 711, 714-715 (6th Cir. BAP 2011); *In re Rothenbush*, 2017 WL 933019 at \*2, 2017 Bankr. LEXIS 622 at \*3 (Bankr. M.D. Fla. Feb. 28, 2017)(“*Hartford Underwriters* does not rule out derivative standing”); *In re Simmons*, 560 B.R. 308 (Bankr. S.D. Ohio 2016); *In re Smith*, 2014 WL 1404722 at \*\*2-3, 2014 Bankr. LEXIS 1538 at \*\*4-9 (Bankr. W.D. Ky. April 10, 2014)(no standing if derivative standing is not requested).

**No:**

*In re Stewart*, 473 B.R. 612 (Bankr. W.D. Pa. 2012)(rejecting argument for derivative standing).

*In re Hannah*, 316 B.R. 57, 61 (Bankr. D.N.J. 2004)(holding that Chapter 13 Debtor did not have standing to bring an avoidance action under §544(a) in the context of a discussion of derivative standing).

**Maybe, if there is a benefit to the estate, but “no” if there is not:**

*Geiger v. Federal Home Loan Mortgage Corp. (In re Weyandt)*, 544 Fed. Appx. 107 (3d Cir. 2013). Even assuming that there are situations in which it may be appropriate to grant Chapter 13 Debtor derivative standing to pursue trustee's avoidance powers, it was inappropriate to grant Debtor derivative standing to avoid prepetition foreclosure sale in order to bring into bankruptcy estate real property in which she lacked any equity that could be administered for the benefit of creditors.

**Maybe, but only if a timely request is made to the court:**

*In re Smith*, 2014 WL 1404722, at \*3, 2014 Bankr. LEXIS 1538, at \*8 (Bankr. W.D. Ky. April 10, 2014)(“In this case, the Plaintiffs did not request derivative standing prior to filing this suit. As such, they do not have standing to pursue this action. Consequently, the Court must dismiss this adversary proceeding without prejudice.”)

**Discussion of possible ‘work arounds’:**

“To avoid the need for derivative standing, clever chapter 13 trustees and debtors' counsel have adopted workarounds. For example, debtors may offer a retainer to chapter 13 trustees to pursue the avoidance claims. Or trustees may hire a debtor's counsel to serve as special counsel for purposes of pursuing the claims.” *In re Rothenbush*, 2017 WL 933019, 2017 Bankr. LEXIS 622 (Bankr. M.D. Fla. Feb. 28, 2017)(footnotes citing cases omitted).

**Leading non-Chapter 13 cases - *Cybergenics* and company:**

*Official Comm. of Unsecured Creditors of Cybergenics Corp. ex rel. Cybergenics Corp. v. Chinery*, 330 F.3d 548, 559 (3d Cir. 2003)(Chapter 11 case permitting “derivative standing”). *Cybergenics* points out that, in footnote number 5, *Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000) explicitly stated that the decision did not address the issue of derivative standing. In addressing derivative standing in the context of a creditor seeking to exercise avoidance rights in a Chapter 11 case, the Sixth Circuit Court of Appeals stated: “perhaps the most important prerequisite to derivative standing is that [the party with authority to act under the Bankruptcy Code] has abused its discretion in failing to avoid a preferential or fraudulent transfer.” *In re Gibson Grp., Inc*., 66 F.3d 1436, 1442 (6th Cir. 1995).

Notably, there is stronger statutory support for derivative standing in Chapter 11 cases, particularly when the party seeking to bring the action is the unsecured creditors committee. *See* *generally*, *In re Cooper*, 405 B.R. 801, 809 (Bankr. N.D. Tex. 2009)(discussing the interplay of Sections 1103(c)(5), 1109(b), and 1123(b)(3)(B).)

The courts are split as to whether or not a non-Trustee (debtor or creditor) can be granted derivative standing in a Chapter 7 case. *Compare*, *In re Cooper*, 405 B.R. 801, 809 (Bankr. N.D. Tex. 2009)(no derivative standing in Chapter 7 cases); *with*, *Hyundai Translead, Inc. v. Jackson Truck & Trailer Repair, Inc. (In re Trailer Source, Inc.)*, 555 F.3d 231, 242 (6th Cir. 2009)(allowing creditor derivative standing in Chapter 7, noting that the language of §503(b(3)(B) strongly supports the decision, but actually holding that: “we believe this authority derives from ‘bankruptcy courts' equitable power to craft flexible remedies in situations where the Code's causes of action fail to achieve their intended purpose.’”).

**There is also the issue of creditor derivative standing in Chapter 13 cases....**

“Because § 544(a) speaks only of *the trustee’s* right to avoid certain transfers and obligations, a debtor like Isaacs must obtain derivative standing to exercise this right.” *In re Isaacs*, 895 F.3d 904, 915 (6th Cir. 2018)(note that the *Isaacs* court specifically did not decide “whether derivative standing is generally available to a Chapter 13 debtor bringing a § 544(a) avoidance action…”. *Isaacs*, 895 F.3d at 917 n. 4.

A Pennsylvania bankruptcy court recently held that derivative standing to utilize the trustee's avoiding powers may be granted in a Chapter 13 case if several conditions were met. Creditor-Movant was required to show that: 1) the movant has alleged a colorable claim that would benefit the estate, 2) the trustee has unjustifiably refused to pursue the claim itself, and 3) the movant has obtained permission from the bankruptcy court to initiate the action on behalf of the estate. *See*, *In re Demeza*, 582 B.R. 868, 876-877 (Bankr. M.D. Pa. 2018).

However, in the recent decision in *Isaacs*, the court appeared to focus on the fact that the Chapter 13 Trustee did not object to the Motion for derivative standing, rather than “unjustifiable refusal”. *In re Isaacs*, 895 F.3d 904, 916 n. 3 (6th Cir. 2018). If the Chapter 13 Trustee’s failure to object to derivative standing was sufficient, that would appear to align with Chapter 11 cases which have held that consent of the Debtor-In-Possession is sufficient for derivative standing to be granted. See, *Smart World Techs., LLC v. Juno Online Servs., Inc. (In re Smart World Techs., LLC)*, 423 F.3d 166, 176 (2d Cir.2005); *Avalanche Mar., Ltd., v. Parekh (In re Parmetex, Inc.)*, 199 F.3d 1029, 1031 (9th Cir.1999)).

In *Demeza*, although the creditor had pled a colorable avoidance claim under the Pennsylvania Uniform Fraudulent Transfer Act with respect to the Chapter 13 debtor's transfer of a half interest in real property to the debtor's daughter, the cost-benefit analysis conducted by the court showed that the proposed fraudulent-transfer action would not benefit the estate. Accordingly, the creditor was denied derivative standing to use the Chapter 13 trustee's fraudulent-transfer avoiding powers. *See also*, *In re Rosenblum*, 545 B.R. 846 (Bankr. E.D. Pa. 2016).

**E. Can The Debtor Create Standing Through A Plan Provision And The Binding Effect Of Confirmation?**

Some courts thinks so: “In this case, the Plaintiffs' modified plan expressly addressed the Plaintiffs' standing to bring this adversary proceeding. Fifth Third was noticed with the motion and had the opportunity to object to the language contained in Section 8 of the Plaintiffs' modified plan. By electing not to object to this language within the time provided, Fifth Third may not now object to the provisions of the modified plan.” *In re Hazelwood*, 513 B.R. 323, 329 (Bankr. W.D. Ky. 2014); *see* *also*, *In re Simmons*, 560 B.R. 308, 311-312 (Bankr. S.D. Ohio 2016)(binding effect of standard provision in Mandatory Form Plan conferred standing on Debtors).

In terms of specific plan language that purports to outline Debtor and Trustee standing, the Eastern District of Michigan’s Model Chapter 13 Plan provides:

Debtor and the Chapter 13 Trustee shall haven concurrent standing to prosecute all Pre-and Post-Petition causes of action, including but not limited to actions arising under Title 11, United States Code. Any compromise or settlement of any litigation or cause of action shall be subject to the provisions of Federal Rule of Bankruptcy Procedure 9019. Any proceeds or damages recovered by or on behalf of the debtor shall be retained pending Order of the Bankruptcy Court.

There are two issues that should be considered: 1) can a Chapter 13 Plan confer standing to avoid a lien or transfer where the Defendant was not listed as a creditor, and would not have had standing to object to the Plan, even if the Defendant had been given notice; and, 2) What if the Trustee and the Debtor have a different view of a proposed settlement? If the Trustee wants to settle (say for an amount that would pay 100% to unsecured creditors) and the Debtor wants to roll the dice and litigate because the amount in excess of allowed claims would go to the Debtor – who wins? Whether this kind of provision actually provides a workable solution to providing Debtors standing remains to be seen.

**F. Why Not Both? What About The Chapter 13 Trustee And The Debtor Bringing Avoidance Actions Jointly?** **And Does That Help?**

1. **Voluntary Joinder**

*Lucero v. Green Tree Fin. Servicing Corp. (In re Lucero)*, 199 B.R. 742, 745 (Bankr.D.N.M.1996) (Chapter 13 debtors had no standing to bring avoidance action but were allowed to substitute Chapter 13 trustee as party plaintiff.), *rev'd on other grounds*, 203 B.R. 322 (10th Cir. BAP 1996).

*In re Geraci*, 507 B.R. 224 (Bankr. S.D. Ohio 2014)(Chapter 13 debtor and Chapter 13 Trustee were joint plaintiffs seeking to avoid a mortgage with a defective legal description under §544(a)(3). “Knowledge” was not attributed to the Trustee.)

1. **Involuntary Joinder**

*In re Funches*, 381 B.R. 471, 488-489 (Bankr. E.D. Pa. 2008). Trustee who had never been asked by Chapter 13 Debtor to avoid prepetition mortgage as improperly notarized, or to avoid verdict entered in state court mortgage foreclosure action as alleged preference, and who had never consented to Debtor's prosecution of such strong-arm and preference claims in his name, could not be joined as involuntary plaintiff for purpose of alleviating any concerns about Debtor's standing. Even aside from fact that the Trustee had never been asked to join in the proceeding, the Trustee was under no duty to permit the Debtor to exercise his avoidance powers, as required for him to be joined as involuntary plaintiff.

*In re Cole*, 563 B.R. 526, 530 (Bankr. W.D.N.C. 2017). Federal Rule of Bankruptcy Procedure 7019, making Federal Rule of Civil Procedure 19 applicable, does not allow the Debtor to make the Chapter 13 Trustee an “involuntary plaintiff”. Moreover, it would not cure the standing problem, because: “allowing the Plaintiffs to use Rule 19 as a post hoc mechanism to gain standing when they have none would be repugnant to foundational principles of federal jurisdiction, especially since the standing inquiry is made at the commencement of an action...”. *Id*. “Indeed, courts have declined to allow an existing plaintiff to join an involuntary plaintiff when the existing plaintiff did not have standing to commence the action.” *Id*. (Citing cases).

Contrary to the statements in *In re Cole*, the Sixth Circuit’s decision in *Isaacs* took a more flexible view of the standing “inquiry,” and the timing of a request for derivative standing. “DBI urges this court to adopt a rigid rule that a plaintiff must obtain derivative standing before filing an adversary complaint, and that Isaacs therefore lacks derivative standing because she did not seek it until after filing her adversary complaint. This argument fails, however, because such a bright-line rule would be inconsistent with the equitable nature of derivative standing.” *In re Isaacs*, 895 F.3d 904, 916 (6th Cir. 2018)(dealing with derivative standing of the Debtor, not involuntary joinder of the Trustee).

1. **Is The Trustee Really A Party?**

The Third Circuit Court of Appeals was not impressed by the Debtor’s apparent tactic of putting the Chapter 13 Trustee in the caption, where the Chapter 13 Trustee did not actually participate in the litgation. *See*, *In re Knapper*, 407 F.3d 573, 577 n.3 & 583 (3rd Cir. 2005)(“although the caption of Knapper's complaint lists the standing Chapter 13 trustee as a plaintiff, he did not participate in her adversary proceeding in any way.”). The *Knapper* court held that the Chapter 13 Debtor did not have standing to pursue the avoidance claim. *See also*, *In re Funches*, 381 B.R. 471, 487-489 (Bankr. E.D. Pa. 2008).

1. **Timing – If The Debtor Wants The Chapter 13 Trustee To Join In**

**Litigation: Ask Early:**

*See*, *In re Merritt*, 529 B.R. 845 (Bankr. E.D. Pa. 2015)(Chapter 13 Trustee objected to joining with the Debtor, in part, because the Debtor approached the Trustee so close to the two year bar date that the Trustee could not get comfortable with timely filing an action that would comply with Rule 9011).

1. **Can The Chapter 13 Trustee Intervene Or Be “Substituted In”?**

*Wood v. Mize (In re Wood)*, 301 B.R. 558, 562 (Bankr. W.D. Mo. 2003)(“the trustee is an indispensable party within the context of this proceeding because he is the only person with standing to bring the action and full relief cannot be accorded the creditors of the estate without his joinder.” The decision then states: “Therefore, the Court will order that Wood's Complaint be amended to reflect the entry of Richard V. Fink, the Chapter 13 trustee, as a party plaintiff to prosecute this action in tandem with Wood, and as the party plaintiff who filed the Motion for Judgment on the Pleadings.”).

*In re Huntzinger*, 268 B.R. 263, 265-266 (Bankr. D. Kan. 2000)(“the court ruled that the Huntzingers had no standing to prosecute the action; only the trustee

could file the complaint under § 544. Since that ruling, the trustee has moved for and has been granted permission to intervene as the party plaintiff.”).

*In re Ryker*, 315 B.R. 664, 674 (Bankr. D.N.J. 2004)(“At present, nothing in the record indicates whether the Chapter 13 Trustee intends to ratify, join or be substituted in the adversary proceeding. Ryker and his counsel are directed to immediately confer with the Chapter 13 Trustee, who shall thereafter advise the parties and the Court whether she will ratify, join, or be substituted in this adversary proceeding.”).

1. **Or, Perhaps, Even “Strongly Encouraged To Substitute In”?**

*In re Keenan*, 364 B.R. 786, 807 (Bankr. D.N.M. 2007)(“For the purposes of this Memorandum, the Court has also assumed that the judicial lien is a preferential transfer. In general, Chapter 13 debtors lack standing to pursue preferential transfer actions. See *Wood v. Mize (In re Wood)*, 301 B.R. 558, 561, 562 (Bankr.W.D.Mo.2003). Therefore, the Trustee should consider whether she has a duty to pursue a preferential transfer in this case to allow maximum relief to unsecured creditors. See id. at 562.” Footnote 33 continues: “The effect on the Debtors and the unsecured creditors would be considerable. If Mallon's lien is avoided only in part pursuant to §522(f), Mallon will continue to have a lien on the property for $60,639, but the unsecured creditors (other than Mallon) would receive less. On the other hand, if the Trustee entirely voids the lien pursuant to § 547(b), the Debtors will own their home free and clear of Mallon's lien, and the unsecured creditors other than Mallon will receive a larger dividend.”).

**G. A Trap For The Unwary Chapter 13 Trustee/Debtor/Creditor – Failing To Object To Confirmation.**

*Hope v. Acorn Financial Inc.*, 731 F.3d 1189 (11th Cir. 2014).  Trustee's post-confirmation adversary action to avoid perfection of creditor's security interest was barred by Trustee’s failure to object to the Chapter 13 Plan.  Confirmation of the Chapter 13 Plan, in which Creditor was given a secured position, can bind a Trustee who was aware of defect, failed to object, and affirmatively recommended confirmation.

*But* *see*, *In re Hazelwood*, 513 B.R. 323 (Bankr. W.D. Ky. 2014). Confirmation of the original confirmed Plan, listing a mortgage as “secured”, was superseded by the unobjected to Amended Plan, which gave Debtors standing to pursue avoidance of Creditor’s mortgage under §544.

**H. In Jurisdictions Where The Debtor Lacks Standing, The Action May Be Terminated Under Rule 12(b)(6).**

“A motion to dismiss for lack of standing is “properly brought under Rule 12(b)(1), because standing is a jurisdictional matter.” *Hunters United for Sunday Hunting v. Pennsylvania Game Commission*, 28 F.Supp.3d 340, 343 (M.D. Pa. June 18, 2014) *(*citing *Ballentine v. United States*, 486 F.3d 806, 810 (3d Cir. 2007)); s*ee also, Smith v. One West Bank, FSB (In re Smith)*, 459 B.R. 571, 572 (Bankr. M.D. Pa. 2011)(noting that the standing of a Chapter 13 debtor to utilize the strong arm powers of the trustee implicates subject matter jurisdiction because, if the debtor lacks standing, then the bankruptcy court lacks subject matter jurisdiction to address the merits of the case). “When a defendant moves to dismiss under both Rules 12(b)(1) and 12(b)(6), the court must first consider the defendant's motion under Rule 12(b)(1) because ‘[w]hether the complaint states a cause of action on which relief could be granted is a question of law ... [that] must be decided after and not before the court has assumed jurisdiction over the controversy.’ *Bell v. Hood*, 327 U.S. 678, 682, 66 S. Ct. 773, 90 L.Ed. 939 (1946). *See also Mielo v. Aurora Huts, LLC*, 2015 WL 106631, at \* 2 (W.D. Pa. January 7, 2015) (*citing Int'l Ass'n of Machinists & Aerospace Workers v. Northwest Airlines,* 673 F.2d 700, 711 (3d Cir.1982))(“Absent standing, and by extension subject matter jurisdiction, the court does not possess the power to decide the case, and any disposition it renders is a nullity.”).” *Merritt v. MidAtlantic Farm Credit, ACA (In re Merritt)*, 529 B.R. 845, 858 (Bankr. E.D. Pa. March 25, 2015).

**I. The Use Of Avoidance Powers Is Different Than A Chapter 13 Debtor Simply Pursuing Litigation On Behalf Of The Bankruptcy Estate.**

“Debtor argues that she has the ability to pursue litigation on behalf of the bankruptcy estate. That proposition is not particularly controversial. Though the Fourth Circuit has not yet considered the issue, each circuit to have considered it has found that Chapter 13 debtors have standing to bring claims in their own name on behalf of the bankruptcy estate. *See*, *e.g.*, *Smith v. Rockett*, 522 F.3d 1080, 1081 (10th Cir.2008); *Crosby v. Monroe County*, 394 F.3d 1328, 1331 n. 2 (11th Cir.2004); *Cable v. Ivy Tech State College*, 200 F.3d 467, 474 (7th Cir.1999)(ADA claim); *Olick v. Parker & Parsley Petroleum Co.*, 145 F.3d 513 (2d Cir.1998)(class action fee application). If the pursuit of litigation in the name of the estate was all that Debtor sought, there would be little issue with her chosen course. However, by the face of her complaint and argument at the May 5, 2010 hearing, she seeks to exercise the strong-arm powers of the Chapter 13 trustee pursuant to §544(a), which is an altogether different animal.”

*In re Lee*, 432 B.R. 212, 214 (D.S.C. 2010).

Despite 11 U.S.C. §323(a) stating that: “The trustee is a case under this title is the representative of the estate”, courts have balanced that language against the specific rights of Debtors, “exclusive of the trustee” under Section 1303. The Chapter 13 debtor is explicitly given the authority, exclusive of the trustee, to use, sell, or lease property of the estate in certain circumstances. *See*, *Wilson v. Dollar Gen. Corp.*, 717 F.3d 337, 344 (4th Cir. 2013). Moreover, Section 1306 broadly defines the term “property of the estate”, the term used in Section 1303. Thus, courts have held that causes of action belonging to the Debtor are included in the definition of “property of the estate”. *See* *e.g.*, *Rodriguez v. Ocwen Financial Corporation*, 2017 WL 3593972, 2017 U.S. Dist. LEXIS 132893 (S.D. Fla. Aug. 21, 2017)(citing *Wilson*). Accordingly in the context of a Chapter 13 bankruptcy, the “debtor ‘steps into the role of the trustee and exercises concurrent authority to sue and be sued on behalf of the estate.’ ” *Id*. at 344 (quoting *Cable v. Ivy Tech State College*, 200 F.3d 467, 473 (7th Cir. 1999)).

“Most courts that have considered this issue agree that a Chapter 13 debtor may pursue a non-bankruptcy suit on behalf of the estate. *See*, *Wilson v. Dollar Gen. Corp.*, 717 F.3d 337, 343 (4th Cir. 2013)("All of the five circuit courts to have considered the question have concluded that Chapter 13 debtors have standing to bring causes of action in their own name on behalf of the estate."); *Olick v. Parker & Parsley Petroleum Co.*, 145 F.3d 513, 515 (2d Cir.1998)(“Although this Court has not previously ruled on the issue, we conclude that a Chapter 13 debtor, unlike a Chapter 7 debtor, has standing to litigate causes of action that are not part of a case under title 11.”); *In re Griner*, 240 B.R. 432, 436 (Bankr. S.D. Ala. 1999)(“The Court concludes that the trustee and debtor concurrently hold the power to sue as to nonbankruptcy federal and state law claims such as Mr. Griner's suit.”); *Dufrene v. ConAgra Foods, Inc.*, 196 F.Supp.3d 979, 982-983 (Bankr. D. Minn. 2016); *but see*, *Rugiero v. Nationstar Mortg., LLC*, 580 Fed.Appx. 376 (6th Cir. 2014)(Chapter 13 case where court cites Chapter 7 cases stating that trustee is the only one who can act as representative of the estate).

“Because a Chapter 13 debtor retains possession of his property, the debtor ordinarily will have the right to sue in his or her own name. *See* Fed. R. Civ. P. 17(a)(1)(G); *Wilson*, 717 F.3d at 344.” *Lee v. AT&T Servs*., 2018 U.S. Dist. LEXIS 163465 at \*14 (C.D. Cal. Sept. 24, 2018). Even though the Debtor may pursue the litigation in his or her “own name”, some decisions have emphasized that Chapter 13 Debtors do so “*on behalf of the bankruptcy estate*”. *Bowling v. Ryder Integrated Logistics, Inc.*, 2018 WL 1157549, 2018 U.S. Dist. LEXIS 35358 (E.D. Ky. March 5, 2018)(emphasis in original).

**J. Lack Of Standing’s Potential Bleed Over Into The Claims Objection Process.**

“Even if the bank's lien is avoidable under §544, §502(d) does not alter the outcome, for the debtor lacks standing to invoke §502(d).

Although a debtor is entitled to object to a claim under 11 U.S.C. §502(a) (permitting a party in interest to object to a claim), §502(d) does not use the term “party in interest” and depends upon a showing that the lien is avoidable pursuant to a power vested only in a trustee. A debtor cannot circumvent the restriction against her exercising a trustee's avoidance powers by objecting to the claim under §502(d) and invoking defensively a power reserved to a trustee. *Holloway v. IRS (In re Odom Antennas, Inc.)*, 340 F.3d 705, 709 (8th Cir. 2003); *Energy Income Fund, L.P. v. Compression Solutions Co. (In re Magnolia Gas Co.)*, 255 B.R. 900, 914–15 (Bankr. W.D. Okla. 2000); *United Jersey Bank v. Morgan Guar. Trust Co. (In re Prime Motor Inns, Inc.)*, 135 B.R. 917, 920–21 (Bankr. S.D. Fla. 1992).” *In re Turner*, 490 B.R. 1, 4 (Bankr. D.D.C. 2013).

**VIII. Does The Trustee Having Avoidance Powers Create A Corresponding Duty To Use Them?**

**A. Some Courts Say: “Generally, No”.**

*In re Engle*, 496 B.R. 456, 464 (Bankr. S.D. Ohio 2013)(“By conditioning the distribution of the net proceeds of the Preference Action on the Trustee's election to commence litigation that he has no obligation to bring—and almost certainly will not prosecute—the Debtors have not provided for the actual avoidance of the Transfer. Quite simply, the Debtor cannot satisfy §1325(a)(4) by conditioning the required distribution of property on an event that almost certainly will not happen.”).

*In re Cecil*, 488 B.R. 200, 202-204 (Bankr. M.D. Fla. 2013)(“[I]t is left to the Chapter 13 trustee's judgment to determine when it is feasible and efficient to exercise the avoidance powers.”)

*In re Hansen*, 332 B.R. 8, 14 (10th Cir. BAP 2005)(“Section 1302, which governs the trustee's duties, does not list avoidance powers among them. In fact, §1302, which incorporates Chapter 7 trustee duties under §704 by reference, does not refer to §704(1)—the Chapter 7 trustee duty to “collect and reduce to money the property of the estate.”).

*In re Cohen*, 305 B.R. 886, 896 (9th Cir. BAP 2004)(“The one chapter 7 trustee duty that is omitted from the duties of the chapter 13 trustee or debtor is the §704(1) duty to ‘collect and reduce to money the property of the estate.’ This is the duty that obliges chapter 7 trustees to pursue avoiding actions.”).

*In re Straight*, 200 B.R. 923, 928 (Bankr. D. Wyo. 1996)(“The power to avoid a lien or transfer under §§544, 545, or 547 is granted to the “trustee.” In chapter 13, the trustee's specific duties do not include using the lien avoiding powers of chapter 5.”).

*Gilliam v. Bank of Am. Mortgage, L.L.C. (In re Gilliam)*, 2004 WL 3622646 at \*7, 2004 Bankr. LEXIS 1653 at \*25 (Bankr. D. Kan. Oct. 28, 2004)(“The Court believes the difference in Chapter 7 and Chapter 13 trustee duties simply gives Chapter 13 trustees more discretion not to use the avoiding powers; it does not eliminate their standing to use them.”).

**B. Some Courts Say “Yes”, There Is A Duty.**

*In re Johnson*, 279 B.R. 218, 225 (Bankr. M.D. Tenn. 2002)(“Chapter 13 trustees have a fiduciary obligation to object to claims, to examine the validity of security interests and to prosecute avoidance actions during the Chapter 13 case. See 11 U.S.C. § 1302(b).”).

*In re Driver*, 133 B.R. 476, 480 (Bankr. S.D. Ind. 1991)(“it would then be in the Chapter 13 trustee's interest (and is arguably among the trustee's duties, *see* 11 U.S.C. section 1302(b)(4)) to use the transfer avoidance powers to enable the debtor to propose and perform a feasible plan.”).

*In re Redditt*, 146 B.R. 693, 696-697 (Bankr. S.D. Miss. 1992)(“Where use of the avoiding powers will achieve a more equitable distribution among creditors or where it will aid in a more appropriate classification of claims, the trustee should proceed with such action pursuant to the trustee's duty to advise and assist the debtor in performance under the plan.”).

**C. Maybe It Isn’t A “Yes” Or “No” Question....**

“Equally clear is the ability of the Chapter 13 trustee to employ the avoidance powers. Under § 103(a) the provisions of Chapters 1, 3 and 5 apply to cases commenced under Chapters 7, 11, 12 or 13. 11 U.S.C. §103(a). Accordingly, a Chapter 13 trustee, is empowered to use all of the avoidance powers found in Chapter 5. This authority is not diminished because a Chapter 13 trustee is not required to perform the duty of a Chapter 7 trustee under §701(1) to collect and reduce to money the property of the estate. That duty does not provide the authority for the exercise of the avoidance powers. Rather, the authority resides in §§544, 545, 547 and 548. The avoidance powers are a means by which a Chapter 7 trustee may meet his duty under §701(1). Similarly, the exercise of avoidance powers by a Chapter 13 trustee can be a means to fulfill the duty to ‘... assist the debtor in performance under the plan,’ set forth in §1302(b)(4).

Nor is it necessarily contrary to the purpose or functioning of Chapter 13 for the Chapter 13 trustee to be the sole party to exercise the avoidance powers. It would certainly be less cumbersome if the Chapter 13 debtor enjoyed the independent authority to proceed with an avoidance action. However, there is no reason to expect that a Chapter 13 trustee will refuse to act on an avoidance claim that has merit. Further, the Chapter 13 trustee need not personally prosecute each avoidance action. For example, the trustee can retain debtor's counsel as special counsel pursuant to §327(e) in order to prosecute the matter. Limiting Chapter 13 debtors to the trustee powers identified in §1303 is consistent with both the statutory language and the structure of the Code.” *In re Ryker*, 315 B.R. 664, 670 (Bankr. D.N.J. 2004).

**D. At Least One Court Says The Chapter 13 Trustee Has No Duty To Let A Debtor Exercise Trustee’s Avoidance Rights.**

*In re Funches*, 381 B.R. 471, 489 (Bankr. E.D. Pa. 2008)(“Because the Trustee has no duty to permit the Debtor to exercise his avoidance powers in his name, the Debtor may not maintain this action in the name of the Trustee by invoking Rule 19.”).

**E. “Let’s You And Him Fight!” Plans (Nope. Nope. Nope.)**

In *In re Engle*, 496 B.R. 456 (Bankr. S.D. Ohio 2013), the Chapter 13 Debtors' proposed Plan sought to meet the “Best Interest/Liquidation Test”, by simply requiring Debtors to pay to general unsecured creditors the actual net recovery from any preference proceedings, in event that Chapter 13 trustee elected to pursue such proceedings and was successful. The *Engle* court held that this did not satisfy the “best interest test” obligation under §1325(a)(4), given that Chapter 13 trustee did not have same incentive as Chapter 7 trustee to pursue avoidance claims, and that Debtors' payment was conditioned on an event that was unlikely to occur.

The argument in *Engle* did not come out of nowhere - it was suggested by the holding in *Loeffler*:

“The Court cannot apply the best interests test under §1325(a)(4) in such a way as to require the Debtor to personally fund the distribution of assets that she does not possess and cannot personally recover. Avoidance actions are typically causes of action concerning money paid to a creditor that constitutes a preference; an avoidable lien granted to a creditor within 90 days of the petition date; or real or personal property transferred prior to the petition date in a transaction that is either constructively or actually fraudulent. In this case the allegation concerns a right to payment of money that the Debtor relinquished prior to the petition date. As is typical of many avoidance actions, it involves property the Debtor does not possess. The Court cannot require the Debtor to personally fund payment of the hypothetical value of an asset that the Debtor does not possess and that the Code gives her no authority to recover. By its very nature, an avoidance action to recover money from a third party is unlike property that vests in the debtor upon plan confirmation, the value of which the debtor pays to creditors under his plan. Except for actions to avoid the transfer of exempt property under §522(h), avoidance actions are not under the control of the debtor. It is the trustee who chooses to pursue an avoidance action.

That does not mean that a creditor in a chapter 13 proceeding should not expect to receive a distribution on account of assets that may be subject to recovery under §§544, 547 or 548. But, because a chapter 13 debtor has no control over such recovery actions, the creditor must look to the chapter 13 trustee to recover and distribute those assets exactly as it must look to the trustee to pursue those recovery actions in a chapter 7 case. So long as the Debtor's plan provides for that eventuality and provides that any such recovery must be distributed to creditors under a the Plan, it passes muster under §1325(a)(4). *See*, *e.g.*, *In re Johnson*, 26 B.R. 381, 383 (Bankr.D.Colo.1982) (“Since the Chapter 13 trustee has the power to avoid the transfer ... under 11 U.S.C. § 548, a plan providing for such event would satisfy the best interests test of Section 1325(a)(4).”).”

*In re Leoffler*, 2011 WL 6736066 at \*3, 2011 Bankr. LEXIS 5038 at \*9-11 (Bankr. D. Colo. Dec. 21, 2011)(footnotes omitted).

**F. But What About Potential Trustee Liability?**

One reason that a Chapter 13 Trustee might be motivated to pursue an avoidance action is because if, after the statute of limitations passes, the Chapter 13 case converts to a Chapter 7 - the Chapter 13 Trustee could be sued by the Chapter 7 Trustee (or creditors) for failing to avoid the transfer before the statute of limitations expired.

Not a happy thought for the Chapter 13 Trustee.

While one method of protecting creditors without having to institute avoidance litigation is an objection to confirmation of the Plan based on the Best Interest of Creditors Test – meeting the “best interest” test through monthly payments that are not actually made does not protect creditors if the case is converted to a Chapter 7.

Is there another method that preserves the ability to pursue litigation, if necessary, without the Chapter 13 Trustee actually having to actually file an avoidance action?

**1. Obtaining a waiver - the alternative to litigation.**

If the main concern is protecting creditors from the possibility of conversion after the bar date for bringing an avoidance action, one of the most common ways to address that concern is by obtaining a waiver.

A waiver saves the Chapter 13 trusteeship the time and expense of litigation, while still preserving the cause of action if it should need to be brought at a later date, after conversion.

The most important consideration in obtaining a waiver is making sure that it is effective in waiving the statute of limitations defense. That means: NOT getting a waiver from the Debtor - getting it, instead, from the potential preference/fraudulent transfer DEFENDANT. The Debtor is generally not going to be able to provide an effective waiver on behalf of a future defendant in an adversary proceeding.

Generally, this type of waiver will not protect creditors from a situation where the case is dismissed. But, because a Chapter 13 Debtor always has (arguably) a right to dismiss their Chapter 13 case, that risk is often viewed differently than a situation where a Debtor converts after expiration of the statutory time period for preference/fraudulent conveyance recovery, and still obtains the benefit of a Chapter 7 discharge.

**G. Other Potential Negative Consequences To Chapter 13 Trustees Not Pursuing Avoidance Claims:**

**1. Use Of Avoidance Powers As A Factor In Conversion To Chapter 7:**

*In re Killian*, 529 B.R. 257, 264 (C.D. Ill. 2013)(“The bankruptcy court stated that unlike a Chapter 13 trustee, a Chapter 7 trustee could avoid and recover preferential transfers, thus making conversion the better option in this case.”).

**IIX. Avoidance You Can’t Avoid - The Hypothetical Liquidation For The**

**Best Interest Test.**

The “Best Interest of Creditors Test” is set forth in Section 1325(a)(4), which states:

(4) the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under Chapter 7 of this title on such date.

**A. Under The “Best Interest” Test, The Chapter 13 Trustee Has To Look At A “Hypothetical Liquidation”**

“To determine compliance with the test, a hypothetical liquidation of the debtor’s estate under Chapter 7 on the “effective date of the plan” must be compared to the value on “the effective date of the plan” of what the debtor proposes to distribute to the holders of allowed unsecured claims. Two mathematical calculations are required: (1) an estimate must be made of what would be available for distribution to unsecured claim holders in a Chapter 7 case; and (2) the distributions to unsecured claim holders under the proposed plan must be “present valued” (discounted) as of the effective date of the plan.”

Keith M. Lundin & William H. Brown, *Chapter 13 Bankruptcy*, 4th Edition, §160.1, at ¶2, Sec. Rev. June 7, 2004, [www.Ch13online.com.](http://www.Ch13online.com.)

“The determination regarding what property creditors would receive in a liquidation should also take into account the administrative expenses that would be incurred in a chapter 7 case. These expenses may include, in addition to costs of sale, costs such as capital gains taxes incurred by the trustee who disposes of property. This determination may present issues of valuation when the debtor proposes to retain nonexempt property. When the property is sold pursuant to the plan, the amount of the actual net proceeds, less applicable exemptions, normally determines the amount that must be distributed to creditors.”

8-1325 *Collier on Bankruptcy*, ¶1325.05 (16th ed.).

**B. Avoidance Actions Are “Litigation Assets” For Purposes Of The Best Interest Of Creditors Test.**

Avoidance actions can have a monetary value from the recovery of actual transferred funds, or the avoidance action can create value for unsecured creditors through the avoidance of liens on non-exempt property, or the recovery of non-exempt property that would, in a Chapter 7 case, be liquidated through a sale.

Avoidance actions are assets that are part of the liquidation analysis. *See*, *In re Bradley*, 567 B.R. 231, 237 (Bankr. D. Me. 2017)(“the liquidation analysis must also account for any chapter 5 recoveries that would increase the assets in the estate and the distributions to creditors.”); *Cox v. Cox (In re Cox)*, 247 B.R. 556, 565 n.13 (Bankr. D. Mass 2000). While there is a question regarding the extent to which a Chapter 13 Trustee would be required to pursue avoidance actions, there is no question about the obligation of a Chapter 7 Trustee to do so under §704(a)(1). However, that obligation to pursue avoidance actions is contingent on whether or not the litigation would result in significant monies being available to pay unsecured creditors.

The Best Interest of Creditors Test depends on a number of variables that could affect the “hypothetical liquidation”. As one court has stated:

“In deciding whether to pursue litigation such as a preference action, Chapter 7 trustees must undertake a cost/benefit analysis considering not only the potential recovery but also the potential loss if the litigation is unsuccessful. *See* *In re Wildman*, 72 B.R. 700, 707 (Bankr. N.D. Ill. 1987). Neither Chapter 7 trustees nor their attorneys have a duty to collect assets when the costs of collection exceed the value to the estate of the collection. *See* *In re Taxman Clothing Co.*, 49 F.3d 310, 315 (7th Cir.1995). To the contrary, Chapter 7 trustees and their lawyers have a duty to abandon burdensome assets and burdensome litigation. *Id*.; *see also* 11 U.S.C. §554. Chapter 7 trustees should not pursue preference claims where the amount in controversy does not justify the costs. *See* *In re Minich*, 386 B.R. 723, 728–29 (Bankr. C.D. Ill. 2008). The hypothetical liquidation analysis undertaken in Chapter 13 cases must follow these same principles. If a Chapter 7 trustee would abandon an asset, then there is no amount required to be paid to unsecured creditors through a Chapter 13 plan for that asset. *See* *In re Sharp*, 394 B.R. 207, 212–13 (Bankr. C.D. Ill. 2008).”

*In re Cowger*, 2014 WL 318241, at \*2, 2014 Bankr. LEXIS 379, at \*\*5-6 (Bankr. C.D. Ill. Jan. 29, 2014); *see* *also*, *In re Hopkins*, 494 B.R. 306, 319 (Bankr. E.D. Tenn. 2013)(“In this case, the court is requiring her to include an additional amount in her plan in order to meet the best interest of creditors test. That amount is an estimate of the value of the adversary proceeding to the estate less the expenses of the litigation and costs of sale.”).

Similarly, the court in *LaLonde* stated:

“There is little doubt that this court must consider what the chapter 7 trustee could have achieved by his avoidance and sale powers. On its face, the language of §1325(a)(4) seems to demand that a court conduct just this hypothetical inquiry, and the few courts confronting the issue have agreed with this reading. *See*, *In re Carter*, 4 B.R. 692 (Bankr.D.Colo.1980); *In re Future Energy Corp.*, 83 B.R. 470 (Bankr.S.D.Ohio 1988); *In re Larson*, 245 B.R. 609 (Bankr.D.Minn.2000). In *Future Energy*, for example, the court examined whether a chapter 11 plan met the best interests test of §1129(a)(7). To make that judgment, the court considered the distribution that would have resulted had the chapter 7 trustee avoided an allegedly preferential transfer. 83 B.R. at 489–90.

Courts have generally held that a plan proponent must show that a trustee was not reasonably likely to have succeeded in an avoidance or sale action. *See*, *In re Larson*, 245 B.R. at 615 (best interests test required the court to determine whether a chapter 7 trustee “could be reasonably expected to succeed in setting aside the transfer”).”

*In re LaLonde*, 431 B.R. 199, 205 (Bankr. W.D. Wis. 2010).

In short, the practical problem appears to be: How do litigants provide proof to the bankruptcy court regarding the likelihood that a Chapter 7 Trustee would pursue litigation (or liquidation), how much it would cost, the chances of legal success, and then the probability of any judgment obtained being collectable?

**C. The Best Interest Of Creditors Test - Deductions.**

The court in *Trombetta* stated the “formula” for the Best Interest Test as follows:

“To arrive at a liquidation value to be paid the general unsecured creditors, the Court is to calculate the value of all nonexempt property of the estate, reduced by the administrative expenses that would be incurred in a chapter 7 case, by the amount of all lien claims that would be enforceable against the property under chapter 7, and by the amount attributable to priority unsecured claims allowed under chapter 7.”

*In re Trombetta*, 383 B.R. 918, 924 (Bankr. S.D. Ill. 2008); *see* *also*, *In re Sharp*, 394 B.R. 207, 212 (Bankr. C.D. Ill. 2008).

Courts generally allow certain expenses that would be incurred in a Chapter 7 liquidation to reduce the amount of the Chapter 13 payments required to meet Section 1325(a)(4)’s Best Interest of Creditors Test. *See*, *In re Steele*, 403 B.R. 882, 888 (Bankr. D. Kan. 2009)(“In performing a hypothetical liquidation analysis, the starting point is obviously the value of the property the Chapter 7 Trustee would be entitled to liquidate. . . . That is only the starting point, however. From that amount, one must deduct the costs the Chapter 7 trustee will likely incur in completing the liquidation, as well as the trustee fees and any other expenses that would be incurred in an actual Chapter 7 liquidation of the property.”).

**1. The “cost of sale” is one expense that is often allowed.**

*See*, *In re Locklear*, 386 B.R. 911 (Bankr. S.D. Ga. 2007)(deducting the costs of realtor commission); *In re Trombetta*, 383 B.R. 918, 924 n.15 (Bankr. S.D. Ill. 2008)(“These expenses would include costs of sale by the chapter 7 trustee”); *In re Delbrugge*, 347 B.R. 536 (Bankr. N.D. W.Va. 2006)(test must take into account costs of sale); *In re Dixon*, 140 B.R. 945 (Bankr. W.D.N.Y. 1992) (permitting 10% deduction from estimated sale price to account for costs of sale in chapter 7 based on court's experience).

**2. The Chapter 7 Trustee fee may also be included in the calculation.**

*In re Trombetta*, 383 B.R. 918, 924 n. 15 (Bankr. S.D. Ill. 2008)(“These expenses would include . . . trustee's fees”); *In re Delbrugge*, 347 B.R. 536, 539 (Bankr. N.D. W.Va. 2006)(“Appropriate deductions used in making the calculation required by §1325(a)(4) include: Chapter 7 trustee's fees”); *In re Gatton*, 197 B.R. 331, 332 (Bankr. D. Colo. 1996); *In re Barth*, 83 B.R. 204, 206 (Bankr. D. Conn. 1988)(allowing Chapter 7 trustee compensation as a deduction without presenting evidence).

**3. Taxes, such as capital gains taxes, that would have to be paid in the Chapter 7, are also deducted.**

*In re Cole*, 548 B.R. 132, 148 (Bankr. E.D. Va. 2016); *In re Delbrugge*, 347 B.R. 536, 539 (Bankr. N.D. W.Va. 2006) (“Appropriate deductions used in making the calculation required by §1325(a)(4) include: . . . capital gain taxes”); *In re Gatton*, 197 B.R. 331, 332 (Bankr. D. Colo. 1996)(“In addition, we must now take into consideration a hypothetical capital gains tax that would be payable by a chapter 7 trustee.”); *Matter of Young*, 153 B.R. 886, 887 (Bankr. D. Neb. 1993)(“Before the court is the limited issue whether capital gains taxes should be deducted in completing a hypothetical Chapter 7 liquidation analysis for purposes of confirming a Chapter 13 plan. I conclude that capital gains taxes should be deducted”); *In re Card*, 114 B.R. 226, 228 (Bankr. N.D. Cal. 1990)(“Since one of those expenses would be the capital gains tax, the debtor here is justified in including the hypothetical tax in his calculation.”).

**4. Debtor’s Attorney Fees For Filing The Chapter 13 Case Are Not**

**Included.**

“The comparison required by the best interests of creditors test attempts to assure that the decision to file a Chapter 13 case instead of a Chapter 7 case is not detrimental to unsecured creditors. If this case had been filed under Chapter 7, there would have been no allowed claim for Chapter 13 attorney fees. ‘[T]he Debtors' suggestion that the hypothetical liquidation should incorporate the assumption that the Chapter 7 liquidation occurs after conversion from Chapter 13 and thereby includes the payment of Chapter 13 fees as an administrative expense is not supported by any authority.’” *In re Goudreau*, 530 B.R. 783, 787-788 (Bankr. D. Kan. 2015).

**5. As With Many Things In The Law - Sometimes The Problem Is Evidence.**

*In re Cole*, 548 B.R. 132, 148-149 (Bankr. E.D. Va. 2016)(“ In the instant case, the record enables the Court to determine the amount of the Debtor's exemptions, and § 326(a) sets forth the means by which the Court may calculate the maximum commission available to a chapter 7 trustee. However, there is nothing to guide the Court in determining other potential liquidation costs, such as sales expenses, attorney's fees, and tax obligations that may be incurred, and the Court will not engage in speculation.”).

*In re Dick*, 2008 WL 294583 at \*3, 2008 Bankr. LEXIS 264 at \*8 (Bankr. D. Kan. Jan. 30, 2008)(“For chapter 13 liquidation test purposes, the Court values the parts inventory at $4,500 and accepts Palmer's appraisal of the Connex container at $1,000. The trustee would be entitled to § 326 compensation on $5,500, or $1,300. The Court has no evidence of what the auctioneer's commission would be and makes no deduction therefor.This would leave $4,200 for distribution to the creditors.”).

*In re Barth*, 83 B.R. 204, 206 (Bankr. D. Conn. 1988)(“It is the debtor's burden to establish all the conditions necessary for plan confirmation under §1325(a). . . . If a debtor claims liquidation expense in addition to trustee compensation, the burden will be on the debtor to establish such amount. The court will not accept blanket assertions that six percent, or any other percentage of estate assets, automatically should be allowed to establish liquidation cost.”).

**D. Going The Other Way - Additions: Discount Rates/Interest If Liquidation Would Provide A Dividend In Chapter 7.**

In contrast to the expense associated with liquidating assets in Chapter 7 that reduce the amount to paid to meet the Best Interest Test, some courts require an increase in the amount to be paid in a Chapter 13 Plan based upon the fact that payments will not be paid in a lump sum - but rather, will be paid over a three to five year period.

Without going into some of the complexities of timing associated with a determination of whether a Plan complies with Section 1325(a)(4), it is easy to see that payments to be received 60 months from now are not worth as much as the immediate payment of the same amount of money. For a stream of payments over time to have the same “present value” as an immediate payment, the payments over time have to be enhanced through something akin to an interest component. This type of calculation will only come into play when the amount that would be received in a Chapter 7 liquidation exceeds the present value of the amount that is to be distributed through the Chapter 13 Plan.

When the assets that need to be liquidated are litigation assets, courts may look at the reality of how long the litigation would take in a Chapter 7 (down the road several years), versus when payments would begin in Chapter 13 (after confirmation). *See*, *In re Lapin*, 302 B.R. 184, 192 (Bankr. S.D. Tex. 2003).

Of course, one of the major factors in determining “present value” is the underlying interest rates. When interest rates are high, the enhancement can be significant. *See*, *In re Hieb*, 88 B.R. 1019 (Bankr. D.S.D. 1988)(discount rate of 12% per annum). Today, because interest rates are lower, less “value” is being lost in payments over time, and it appears that this aspect of the Best Interest Test has been litigated less frequently as a result. Should we again see the days of savings accounts paying 5% interest, this issue may raised more frequently.

**E. Arriving At A Precise Number For Purposes Of Section 1325(a)(4) Is Hard - So, Many Courts Use A Standard Discount.**

Some courts simply adopt a “flat rate” to simplify the process of arriving at a “net” figure. *See*, *In re Craver*, 2012 WL 290366 at \*3, 2012 Bankr. LEXIS 446 at \*8-9 (Bankr. N.D. Ohio Jan. 31, 2012)(“In this case, both parties have adjusted for any exemptions in the property and allowed a flat ten percent for the cost of sale/administrative cost. The court recognizes the utility of a flat rate and accepts this rate. The ten percent flat rate will generally favor unsecured creditors. When chapter 7 assets total $50,000 or less, the trustee's statutory compensation alone is at least ten percent, not including any expenses related to liquidation.”); *In re Boyd*, 410 B.R. 95, 100 (Bankr. N.D. Cal. 2009)(“The Court estimates that the sale proceeds would be further reduced by costs of sale which are normally calculated as eight percent of the sale”); *In re Trombetta*, 383 B.R. 918, 924 n. 15 (Bankr. S.D. Ill. 2008)(“The chapter 13 trustees in this District subtract 12 percent of an asset's value to account for the hypothetical chapter 7 trustee's costs in selling the item and for the chapter 7 trustee's statutory fees. The debtor has not contested using this methodology.”).