JUDGES' PANEL
CONSUMER BANKRUPTCY ISSUES

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United States Bankruptcy Court
Southern District of Mississippi, Northern Division

Nunc Pro Tunc Applications to Employ Special Counsel in Chapter 13s

Rule 2014 of the Federal Rules of Bankruptcy Procedure provides that an order approving the employment of professionals pursuant to §§ 327, 1103, and 1114 of the Code shall be made only on application of the trustee or committee. Most courts have held that approval of the retention of a professional must generally be made before the professional has been employed, but that bankruptcy courts have general equitable powers to consider applications after the professional has been employed. Other courts have recognized a "per se" rule against retroactive approval of a professional's employment.

The Supreme Court's ruling in *Acevedo* has brought into question bankruptcy courts' authority to issue *nunc pro tunc* orders. The Supreme Court used strong language to caution against issuing orders *nunc pro tunc*. Neither the Fifth Circuit nor the Eleventh Circuit has addressed *Acevedo* in the context of *nunc pro tunc* applications to employ.

The bankruptcy courts in the Eleventh Circuit take a strict approach to *nunc pro tunc* applications to employ. Generally, *nunc pro tunc* applications to employ are only granted where the movant can show that (1) the professional seeking employment would have been qualified for employment at the onset and throughout the period of time for which the services are to be compensated, and (2) that the movant's failure to obtain prior approval is excusable. To find excusable neglect, courts consider other circumstances surrounding the omission or negligence, including (1) prejudice to the debtor, (2) the length of the delay and the potential impact on the judicial proceedings, (3) the reason for the delay, including whether it was within the reasonable control of the movant, and (4) whether the movant acted in good faith.

The excusable neglect standard requires a showing beyond simple neglect or inadvertence. For instance, in *McLemore*, Judge Sawyer found that special counsel's excuse that he did not know his client was in bankruptcy did not qualify as excusable neglect to justify the untimely application. Accordingly, the

application for approval of attorneys' fees and expenses was denied, and the fees and expenses paid to special counsel's firm were ordered to be paid to the chapter 13 trustee to pay unsecured creditors. This is not uncommon. In *Fisher*, Judge Callaway similarly found that a law firm's reliance on a client's statement without further checking PACER was wholly inadequate. Both judges emphasized that attorneys have access to PACER and should check it upon initial retention as well as immediately before distributing settlement proceeds. Again, in *Smith*, Judge Coleman from the Southern District of Georgia disgorged special counsel's fees and expenses where special counsel correctly and timely sought approval of his employment by one debtor but failed to do the same for his co-debtor. Judge Coleman declined to make a finding of bad faith, but still found that special counsel's mistake in forgetting that the case was a joint bankruptcy case was not excusable.

As an additional caution, by failing to check PACER, attorneys run the risk of being held liable for settlement funds that would have otherwise gone into the bankruptcy estate but were instead disbursed to the debtor. These funds may be then set aside or avoided pursuant to Section 549. For instance, Judge Sawyer in *McLemore* found that property of the estate was converted when the settlement proceeds were disbursed to the debtor, rather than to the chapter 13 trustee after special counsel failed to check PACER.

The majority of courts within the Fifth Circuit, such as the Western District of Texas in *Ramirez*, have read *Acevedo* as only a prohibition on creating facts that were never before the court, not a prohibition on the retroactive employment of professionals. The Fifth Circuit's holding in *Triangle Chemicals* remains the standard the majority of bankruptcy courts within the circuit use for applications to employ. The standard is "extraordinary circumstances," and courts balance the equities to determine the appropriate result. The "extraordinary circumstances" test is rooted in the equitable powers of the bankruptcy court. It is meant to be flexible but still discourage professionals from general non-observance of Section 327. Courts are instructed to balance the equities to determine what exactly constitutes "extraordinary circumstances" sufficient to warrant *nunc pro tunc* approval. The *Ramirez* court reasoned that the Bankruptcy Code anticipates and authorizes retroactive employment of professionals, in declining to determine that *Acevedo* has changed the standard for *nunc pro tunc* applications to employ.

Treatment of a Late-Filed POC in Chapter 13 Where Filing Creditor Did Not Receive Notice

Section 502(b)(9) of the Bankruptcy Code provides for disallowance of a claim if proof of such claim is not timely filed. Bankruptcy Rule 3002(c) provides, with certain objections, that a proof of claim in a chapter 13 case is timely filed if it is filed not later than 70 days after the order for relief. Read together, the Code and Rules leave little to no discretion for a bankruptcy court to allow a late-filed claim in a chapter 13 case, absent the exceptions in Rule 3002(c). Under Rule 3002(c)(6)(A), a court may extend the time to file a proof of claim if it finds that the notice was insufficient under the circumstances to give the creditor a reasonable time to file a proof of claim because the debtor failed to timely file the list of creditors' names and addresses as required by Rule 1007(a). Under this rule, a creditor may file a motion to extend the bar date prior to filing the claim. In *Mullane*, the Supreme Court provided the standard for adequate notice. This standard requires courts to analyze the particular facts of each case and determine whether the method used to notify an individual was reasonably certain to inform the individual of a proceeding that could affect his rights and afford him an opportunity to present his objections.

The Eleventh Circuit held in *Alton* that when the debtor is an individual debtor, mere knowledge of a pending bankruptcy proceeding is sufficient to bar the claim of a creditor who took no action, whether or not that creditor received official notice from the court of the pertinent dates. In *Alton*, notice of a bankruptcy filing sent to the creditor's attorney was sufficient notice because the creditor was found to have actual knowledge of the bankruptcy case.

In *Tice*, issued by Judge Creswell this past February, the debtor scheduled a creditor "in care of" the law firm representing the creditor in a state court action. The debtor only included the law firm's address, did not identify a specific attorney at the law firm, and used the incorrect zip code. In addition, the debtor filed a Notice of Bankruptcy in the state court case, the same day as he filed his bankruptcy petition, and the next day, an order was entered in the state court case staying the proceedings pending the bankruptcy case. Judge Creswell found that because the creditor's attorney received notice of the bankruptcy in the state court action, that attorney's knowledge of the bankruptcy was imputed to the creditor, who, accordingly, had an affirmative obligation to timely file a proof of claim. However, Judge Creswell noted

that not every attorney for a creditor is capable of imputing knowledge of a bankruptcy. She reasoned that when counsel is retained to represent a creditor for the purpose of obtaining or collecting a debt outside bankruptcy, like in this case, counsel's notice of the bankruptcy petition can be imputed to the creditor.

Similarly, pursuant to section 523(a) of the Code, if a creditor in a chapter 13 case is not provided any notice of a bankruptcy proceeding, the debt owed is not discharged. In *Barnes*, issued by Judge Sawyer, the creditor argued that he was not aware of the debtor's bankruptcy filing, and accordingly, that the debt to owed to him should not be discharged. The Court considered whether notice of a bankruptcy filing provided to a creditor's layer but not to the creditor himself qualified as sufficient notice. Judge Sawyer stated that this inquiry turns upon the facts and circumstances of each particular case. Here, the creditor was in hot pursuit of the debtor, attempting to collect a money judgement, but collection efforts stopped immediately upon the filing of the petition. Then, upon discharge, his collection efforts resumed. Judge Sawyer held that these circumstances, combined with testimony that the creditor's attorney made the creditor aware of the bankruptcy, proved that the creditor had adequate notice, and therefore disallowed the POC.

The Fifth Circuit treats notice issues with late-filed POCs similarly. The Fifth Circuit, in *Sam*, held that an attorney's actual notice of the pendency of a bankruptcy may be imputed to his client if the notice occurs within the scope of the attorney-client relationship. In *Sam*, the Court held that a Notice of Automatic Stay provided to the creditor's attorney eighteen (18) days before the bar date, though it did not indicate the actual bar date, qualified as providing actual knowledge of the case to the creditor. The Court disallowed the POC. To contrast, in *Hutchison* from the Southern District of Texas, a debtor scheduled a creditor with its name "in care of" its attorney in a state court lawsuit and did not otherwise notify the creditor of the pending bankruptcy. The attorney who was scheduled testified that he did not receive the Notice of Commencement of Case, no mention of the debtor's bankruptcy was made in the state court lawsuit, and both parties proceeded to prepare the case for trial as though no bankruptcy were pending. Accordingly, the Court found that the attorney and, therefore, the creditor had no actual notice or knowledge of the debtor's bankruptcy and allowed the POC.

In practice, this issue may not come up very often. If the late-filed POC relates to a debt that the debtor does not want to discharge anyway, such as a home or vehicle, the trustee may not object to the POC in the first place. However, if the claim involves a state court action, for instance, like the above cases, the POC may draw an objection. In this event, courts within both the Eleventh and Fifth Circuits will look to the specific facts of the case to determine whether a creditor, or her attorney, had actual notice or knowledge.

When is an extension in a chapter 13 plan beyond 3 years appropriate?

Section 1322(d) of the Bankruptcy Code states that chapter 13 plans may not provide for payments over a period longer than three years unless the court approves a longer period "for cause." Under no circumstances, however, may the court approve a chapter 13 plan with a payment period longer than five years. An extension of a chapter 13 plan is permitted upon a showing of cause—not just any cause or excuse, but good cause. This requirement is only applicable to debtors with below-median income. The "cause" standard has not been addressed by the Supreme Court, Eleventh Circuit, or Fifth Circuit, but as a general rule, courts have found "cause" for extension of the payment period beyond 36 months when the additional time will permit the debtor to substantially increase dividends to creditors, especially when the extension will permit a 100% payment of unsecured claims. Extension beyond three years has been rejected when it appears the extension of time will only advantage the debtor in acquiring an asset or delaying payment to creditors.

An important note – plan extensions under the CARES ACT officially sunset as of March 27, 2022. So, from March 27, 2020 to March 27, 2022, Debtors could have potentially extended their plans from five to seven years. This relief has expired, though.

The District Court for the Northern District of Alabama in *Davis v. Gore* explained that "cause" for an extension is decided by the bankruptcy court on a case-by-case basis. Courts may find cause when a debtor cannot cure a default or pay priority claims during a shorter term. The Debtor must meet the burden of establishing cause **and** must show that both his case and plan are filed in good faith pursuant to § 1325(a)(3). The District Court explained further that although a bankruptcy court likely would not find cause when a

debtor does not pay all disposable income into the plan, cause requires a separate inquiry and does not rest solely upon disposable income. In *Davis*, the Court ultimately found that the debtor's purchase of a car he could not afford when purchased was not sufficient cause. However, the Court pointed to the substantial lack of evidence or explanation by the debtor as a factor in its decision.

Similarly, in *Threatt*, Judge Robinson held that the Court would not find good cause for an extension beyond the **statutorily preferred** three-year term just to ameliorate the amortization of a secured automobile loan that the debtor could not afford when the vehicle was purchased, and in which there was little or no equity. Judge Robinson pointed to the absence of an unforeseeable adverse event beyond her control that occurred between the vehicle purchase and the bankruptcy. He reasoned that perpetuating a bad credit decision that would significantly reduce what was paid to unsecured creditors demonstrated a lack of cause for an extension and fell short of the good faith standard. He stated that the debtor needed to "conclude her case with a discharge and financial fresh start within the shortest time possible – the ultimate goal for individual bankruptcies."

Although the standard for cause has not been addressed by the Fifth Circuit, the Southern District of Texas in *Samadi* held that it does not find cause to extend a plan beyond three years when the purpose of the extension is simply to pay a small amount to unsecured creditors in the final months of the plan. Unsecured creditors were only getting paid 60%, and payments to the unsecureds did not begin until month 28. The Court found that the primary reason for extending payments over three years was to maintain a comfortable lifestyle while discharging substantial unsecured debt and denied the extension.

Consumer Bankruptcy Panel, June 4, 2022
Judge Tamara O. Mitchell
Career law clerk Donna McGee
United States Bankruptcy Court
Northern District of Alabama, Southern Division

FEES, MORE FEES, AND TAXES
THREE STUMBLING BLOCKS IN CONSUMER BANKRUPTCY CASES[1]

A. Chapter 7 trustee compensation in a Chapter 13 case.

Bankruptcy professionals know that in a Chapter 7 case there is a trade-off – typically most of the debtor's obligations will be discharged but, in exchange, the Chapter 7 trustee will recover estate assets and liquidate property that has equity exceeding the debtor's exemptions; in turn, the Chapter 7 trustee will distribute collected funds to the debtor's unsecured creditors. For various reasons a debtor may not realize until the trustee comes calling that her house or car may be liquidated or that she may have to, in effect, buy back the assets if she wants to keep them. Faced with the prospect of losing her assets, a debtor may decide that conversion to Chapter 13 could be a better option. By that time, the Chapter 7 trustee, and perhaps his special counsel or other professional employed on behalf of the estate, has likely worked toward collecting assets. What happens regarding payment of the fees and expenses incurred by the Chapter 7 trustee and any employed professional after the case has been converted?

1. ***In re Weldy*, Case No. 21-10325 (Bankr. S.D. Ala. Nov. 1, 2021) (Callaway, C.J.)**
The debtor filed her case under Chapter 7 and a trustee was appointed. Upon the Chapter 7 trustee's marketing of the debtor's homestead for sale, the debtor moved the court to value her home. When the court declined to do so the debtor converted her case to Chapter 13. Subsequently the Chapter 7 trustee filed an administrative expense claim for herself as well as for a realtor who worked toward preparing a market analysis for the property. The debtor opposed the claim, in part arguing that the Chapter 7 trustee's claim should not be determined until an appraisal of the real property was concluded; however, the court opined "that a trustee's compensation in a converted case should not be based on the existence or nonexistence of any equity in property." *Weldy*, Case No. 21-10325, at 2. The court noted that on one hand it may seem unfair for a Chapter 7 trustee to be compensated when she did not collect or administer any assets, but on the other hand it may seem unfair for her to receive nothing when the case converted before she could market the property. Explaining that there is no guidance in the Bankruptcy Code for determining compensation for the Chapter 7 trustee when a case is converted, the court concluded that the Chapter 7 trustee should be awarded "a quantum meruit administrative expense based on a lodestar time and hourly rate analysis." *Weldy* at 3 (citing *In re Washington*, 232 B.R. 814, 817 (Bankr. S.D. Fla. 1999)). The court awarded the Chapter 7 trustee administrative expenses, including the charges of a

[1] Unless otherwise specified or is made clear by context, any reference to a code section refers to the Bankruptcy Code, 11 U.S.C. § 101 et seq.

realtor who worked on valuing the property, but subtracted from the requested amount the fees attributable to "normal chapter 7 trustee work" as opposed to "specific work toward liquidation of potential assets." *Weldy* at 3.

B. Compensation to special counsel who failed to obtain court approval.

Another scenario in which fees become problematic involves court approval of the employment of special counsel or, more specifically, the lack thereof. The failure to obtain a court order approving the employment of special counsel tends to go hand-in-hand with the failure to obtain court approval of a settlement or of fees and expenses charged by special counsel. The lack of adherence to proper procedures can lead to disastrous consequences for special counsel's pocketbook; however, as many courts have noted, disaster may be avoided with a quick, simple step.

1. ***In re Fisher*, Case No. 16-1911, 2019 WL 1875366 (Bankr. S.D. Ala. Mar. 27, 2019) (Callaway, C.J.)**

The debtor scheduled a pending lawsuit in her Chapter 13 case. A few months later the attorney representing her in the lawsuit settled the case and retained fees and expenses although he never sought court approval of his employment or of the payment of his fees and expenses. The Chapter 13 trustee moved for turnover of the fees and expenses. The court granted the motion, ordered that the funds be remitted to the Chapter 13 trustee and, when the attorney failed to timely do so, ordered that a show cause hearing be held. In a filed response the attorney asserted, among other things, that he relied on the debtor's written representation that she was not in a bankruptcy case. Applications to employ and for compensation were filed, and the attorney turned over to the trustee the funds he had retained. In considering the application to employ the court looked to a recent case before Judge Oldshue who concluded:

> "[A] movant seeking retroactive approval of a professional's employment must demonstrate that the professional would have been qualified for employment at the onset, and throughout the period of time for which the services are to be compensated; and, that the movant's failure to obtain prior approval at an earlier time is excusable. This inquiry requires a movant to demonstrate both the professional person's suitability for an appointment and the existence of excusable neglect sufficient to justify the failure to file a timely application. To determine whether excusable neglect is present, the analysis is twofold. First, whether there is neglect, be it either actual negligence or a mere omission to act. Second, whether the neglect is excusable. To answer this question, a court necessarily considers all of the circumstances surrounding the parties' omission or negligence. Those circumstances include the danger of prejudice to the debtor, the length of the delay and the potential impact on the judicial proceedings, the reason for the delay, including whether it was within the reasonable control of the movant, and whether the movant acted in good faith."

Fisher, 2019 WL 1875366, at *2 (quoting *In re Osprey Utah, LLC*, Case No. 16-2270 (Bankr. S.D. Ala. Mar. 27, 2018) (internal citations and quotations omitted) (alteration added). The court noted that a quick PACER check should have been done before settlement proceeds were distributed, explaining that it is not enough to rely on a client's representation as to her bankruptcy status because "[t]he client may not notice or understand the 'not in bankruptcy language; the client may be confused as to whether he or she is in bankruptcy; and (not surprisingly) sometimes clients will lie, particularly if they think that answering correctly may cause them to get less money." *Fisher*, 2019 WL 1875366, at *2. Because it found that the attorney's late employment application was not due to sufficiently excusable neglect, the court denied the applications to employ and for compensation. The court ordered that the funds be applied to the debtor's case.

2. ***In re McLemore*, Case No. 202-32131-WRS, 2022 WL 362915 (Bankr. M.D. Ala. Feb. 7, 2022) (Sawyer, J.)**
The debtor filed an amended plan providing that any unexempt proceeds from a pending personal injury claim would be turned over to the Chapter 13 trustee. Thereafter, the trustee requested that the debtor's counsel provide her with contact information for the personal injury attorney. A few days later, in December 2020, the debtor's amended "pot" plan was confirmed. The following June the trustee again contacted debtor's bankruptcy counsel asking for the contact information of the personal injury attorney. In July, the debtor provided the information to his bankruptcy counsel, who then forwarded it to the trustee. The same month the debtor's Schedule A/B was amended to reflect that the debtor was pursuing a personal injury claim and "understands any non-exempt proceeds shall be turned over to the Trustee for payment to unsecured creditors." *McLemore*, 2022 WL 362915, at *1. Thereafter, the trustee discovered that the debtor had actually settled the personal injury case in June and received net proceeds of $16,788.26; no motions to approve the settlement, employ the personal injury attorney or firm, or approve attorneys' fees had been filed. The trustee sought to have the debtor's case dismissed with prejudice and the debtor barred from refiling, as well as to examine the personal injury firm's attorney fees. After the trustee's motions were filed the debtor moved to modify his plan to pay the non-exempt proceeds to the trustee, and filed applications to employ special counsel *nunc pro tunc*, and for the court to approve the settlement. The personal injury attorney admitted that he never verified the debtor's bankruptcy status with a PACER search; the court noted that the "[f]irm has continuously entered into settlements on behalf of debtors and disbursed funds in bankruptcy cases without court approval." *Id.* at 2. According to the court, paying settlement funds to the debtor without the trustee's knowledge equaled conversion of estate property that could have been avoided with a PACER check. The court noted:

> Because of [the personal injury attorney's] failure to check PACER and Debtor's failure to properly disclose the bankruptcy case to the [personal injury firm], the personal injury claim, an asset of the bankruptcy estate, was settled without court approval as required under 11 U.S.C. § 363(b) and

> Rule 9019. Not only did the [personal injury] Firm fail to obtain court approval of the settlement, but also [the personal injury attorney and the firm] failed to seek court approval of his employment as special counsel for debtor as required by 11 U.S.C. § 327 or to have any attorney fees and expenses approved as required by 11 U.S.C. § 330. Only now, after the case has settled, funds have been converted, and the Trustee has moved for dismissal and to examine transactions has the appropriate documentation been filed with the Court.

McLemore, 2022 WL 362915, at *5. Citing Judge Callaway's *Fisher* opinion as to what constitutes excusable neglect for not filing a timely application to be employed, the court noted that, with an early PACER search, the need to file an application *nunc pro tunc* could have been avoided and counsel would have known the process for getting the settlement approved and for disbursing settlement proceeds; however, by the time the employment application had been filed estate funds had already been converted. The court found no excusable neglect and thus denied the application to employ *nunc pro tunc*. Further, since the employment had not been approved, the court ordered that the personal injury firm must remit the attorney fees and expenses it had retained to the Chapter 13 trustee. Recognizing that "[o]ne school of thought is that a loss should be borne by the one that could have most easily avoided it" and noting that the personal injury firm had acted similarly in multiple other cases (as well as accused the trustee of benefitting at the expense of attorneys who did the work), the court determined that the personal injury attorney should bear the loss suffered by the estate. The court ordered that the firm pay to the trustee a sum equal to the entire settlement amount.

3. ***In re Jones*, Case No. 16-03399 (Bankr. N.D. Ala. Jul. 7, 2020) (Mitchell, J.)** The debtor filed her bankruptcy case in August 2016. Sometime thereafter she sustained an injury and, in May 2018, hired counsel to represent her. In February 2020 the debtor filed an application to employ special counsel *nunc pro tunc*; although the court approved the employment of special counsel it did not approve the employment *nunc pro tunc*. Thereafter, a motion to approve compromise and an application for compensation were filed. According to the motion to approve compromise the debtor's personal injury claim had been partially settled in February 2020, resulting in payment of $25,000; from that amount, the personal injury attorney received a $10,000 fee, the debtor received $7,574.54, and miscellaneous expenses and medical bills were paid, leaving almost $2,500 in the attorney's trust account. Furthermore, according to the motion, a final settlement was subsequently reached resulting in an additional $15,000 payment. The personal injury attorney explained in the motion that when the partial settlement was reached, he did not know the debtor was in bankruptcy. The court granted the motion to approve compromise, directing the attorney to remit to the trustee the remaining proceeds from the initial settlement as well as the entire final settlement proceeds of $15,000. In the application for compensation the personal injury attorney requested an additional fee of $6,000 from the final settlement amount of $15,000. The attorney argued he should be awarded all of his fees and expenses

because the settlement was not intentionally made without court approval and he intended no harm. In its order on the application for compensation, the court noted that if a case involves a debtor in bankruptcy then proper procedures must be followed, such as obtaining court approval of the attorney's employment and approval of the settlement itself prior to any settlement proceeds being disbursed. Court approval of attorney fees is also required prior before the attorney may receive or retain his fees. The court noted that although counsel has a duty to ask a client about bankruptcy, "given most individual debtors' lack of sophistication or understanding of legal matters, an attorney handling these types of cases should also have a PACER account" to check for a pending bankruptcy when undertaking representation (and periodically during lengthy litigation), before entering into a settlement agreement, and before distributing funds. *Jones*, Case No. 16-03399, Doc. 45, at 4-5. Quoting Judge Callaway's *Fisher* case, the court made clear that an attorney who does not check PACER to determine if the client is in bankruptcy risks liability for funds that should have gone to the estate. The court recognized that the debtor had already paid a significant sum into the case which, combined with the undistributed settlement proceeds, would result in full payment or close to full payment on the creditors' claims; thus, the creditors suffered no significant harm from the attorney's failure to check PACER. Because the creditors did not suffer significant harm the court declined to deny all fees to the personal injury attorney; however, the court recognized that if the personal injury attorney was allowed to receive full payment of his requested fees then he would escape consequences for not following the proper procedure. The court allowed the attorney to keep the $10,000 fee he retained prior to obtaining court approval but denied his request for the additional $6,000 fee.

C. What constitutes proof that tax returns were filed in order for a court to confirm a Chapter 13 plan?

Bankruptcy Code § 1325 sets forth conditions under which, if all are complied with, the court must confirm the debtor's plan. 11 U.S.C. § 1325(a). One specific obligation is that the debtor must have "filed all applicable Federal, State, and local tax returns as required by section 1308." 11 U.S.C. § 1325(a)(9). What happens when the debtor asserts that all returns have been filed but a taxing authority's proof of claim reflects otherwise? Is it enough for the debtor to testify that the return was placed in the mail? Perhaps surprisingly, there is not an abundance of case law answering these questions. However, some courts have addressed proof of filing returns in the context of dischargeability actions, and these court decisions may provide guidance for confirmation issues.

1. ***Word v. I.R.S. (In re Word)*, Case No. 6:15-bk-04736-CCJ, Adversary No. 6:15-ap-00120-CCJ, 2018 WL 1616837 (Bankr. M.D. Fla. Mar. 29, 2018)**
In an action to determine whether a debtor's tax liability was dischargeable, the parties stipulated that the only issue for the court to decide was whether the debtor's 2010 income tax return had been filed. The debtor explained that it had been routine for twenty years for her CPA husband to prepare their tax returns, discuss and sign

them with her, then he would file them. The debtor stated that her husband, who had since passed away, had filed the 2010 returns although she did not know when they were mailed. The debtor produced letters regarding a filing extension, an application for extension, and a signed copy of the 2010 return. The IRS presented testimony of a bankruptcy specialist who explained how the IRS records returns it receives in a data retrieval system; the specialist searched the system but did not find that the 2010 return was filed prior to the bankruptcy. The court explained that, when filing is disputed, a debtor has to prove by a preponderance of the evidence that a return was filed. According to the court:

> For purposes of Section 523(a)(1)(B)(i), a tax return is filed when the IRS receives actual delivery of the return. "The case law is clear that filing means delivery." Congress, however, created some exceptions to the actual delivery rule for federal income tax returns. The exceptions are found in Section 7502 of the Internal Revenue Code. A tax return sent by U.S. mail is deemed delivered to the IRS by the postmark date stamped on the envelope containing the tax return. If a tax return is sent to the IRS by registered mail, a registration receipt is prima facie evidence that the return was delivered to the IRS. By regulation authorized in Section 7502, a postmarked certified mail receipt of a tax return sent by certified mail is also prima facie evidence that a tax return was delivered to the IRS. A tax return filed electronically is deemed by regulation authorized in Section 7502 to be filed with the IRS on the date of the electronic postmark receipt. When the proof required by Section 7502 is unavailable, this Court may not consider extrinsic evidence to prove the filing of a tax return.

Word, 2018 WL 1616837, at *2 (footnotes omitted). The court remarked that the debtor did not provide the postmarked, stamped envelope containing the tax return and did not provide evidence that the return was either filed electronically or sent by registered or certified mail. The court considered the debtor to be a credible witness, but determined her testimony and evidence were insufficient to prove the return was delivered. The debtor's tax liability for 2010 was not dischargeable.

2. ***Campbell v. United States (In re Campbell)*, 186 B.R. 731 (N.D. Fla. 1995)**
The debtor failed to file income tax returns for five years. His tax attorney recommended having the taxes professionally prepared; once the debtor received the returns, he gave them to his tax attorney who in turn mailed them to the IRS. Several years later the debtor filed a Chapter 7 case to discharge the tax debt. The IRS records indicated that four out of the five returns at issue had been received, although at different times. The debtor's tax attorney testified that he mailed all five returns but the IRS had no record of receiving the fifth return. The court noted that the debtor had to prove by a preponderance of the evidence that the return was filed, and per the Supreme Court in *United States v. Lombardo*:

> Filing, it must be observed, is not complete until the document is delivered and received. "Shall file" means to deliver to the office . . . [.] A paper is

filed when it is delivered to the proper official and by him received and filed.

Campbell, 186 B.R. at 733 (quoting *U.S. v. Lombardo*, 241 U.S. 73-76-77, 36 S. Ct. 508, 509, 60 L. Ed. 897, 898 (1916). The Court went on to note that the actual delivery rule now has two exceptions as codified by Congress in in 26 U.S.C. § 7502:

> The two exceptions are:
> (1) If a tax return is postmarked with a date which would make the return timely filed, the return will be deemed timely filed even though actually received by the IRS after the due date. 26 U.S.C. § 7502(a).
> (b) If a return is not received by the IRS, a taxpayer may still claim the timely receipt if the return was mailed timely by registered or certified mail and the taxpayer has proof. 26 U.S.C. § 7502(c).

Campbell, 186 B.R. at 733-34. The court determined that since the debtor admittedly had not filed the tax return timely then the exceptions to the actual delivery rule did not apply; thus, the debtor had to prove the return was received to keep the debt from being excepted from discharge under Bankruptcy Code § 523(a)(1)(B). The IRS records included a Certificate of Lack of Filing that, according to the court, was prima facie evidence that the debtor did not file the return. The only evidence of filing provided by the debtor was that the return had been prepared, signed, and given to his tax attorney. The attorney testified he mailed the return and that he could not find the original return when he later searched his files. The court determined that, although "[t]he fact that the other returns were received is some evidence of delivery [but] there is not clear proof that the [other four] returns all were received by the IRS at one time." *Id.* at 734. The debtor did not prove by a preponderance of the evidence that the return was filed.

3. ***Woodworth v. United States (In re Woodworth)*, 202 B.R. 641 (M.D. Fla. 2015)**
The debtor brought an adversary proceeding to seeking to discharge his tax liability for five prior years. The IRS determined that the debtor had no liability for one year and his liability for two of the years was dischargeable; however, the IRS contended that the debtor did not file returns for two years and thus the corresponding liability would not be dischargeable. According to the debtor and his wife, an accountant had prepared four past due returns for them. The returns for 1982 and 1983 were "fat" while the 1984 and 1985 returns were "skinny." The returns were placed in two envelopes, each containing one "fat" and one "skinny" return. The debtor's wife testified she mailed both envelopes, and the IRS records showed the IRS received two envelopes; however, the IRS asserted that it received only the 1982 and 1983 returns. The 1982 and 1983 returns and the two envelopes, which had not been sent by certified or registered mail, were introduced into evidence. The debtor maintained that the IRS lost the 1984 and 1985 returns since those returns were in the envelopes with the other returns. The court noted that several courts have determined that the common law "mailbox rule" allowing proof of mailing to be

established by extrinsic evidence was displaced by IRC § 7502. Even though the Eleventh Circuit had not addressed establishing proof by extrinsic evidence, the Fifth Circuit has addressed the issue, determining that "to create an exception where the undisputed facts clearly fall within the literal and unambiguous language of the statute would do violence to the statutory scheme and substantially undermine the purpose of the provision." *Woodworth*, 202 B.R. at 644 (quoting *Drake v. Comm'r*, 554 F.2d 736, 738 (5th Cir. 1977)). According to the court, "[m]any of the bankruptcy courts in the Eleventh Circuit have considered the interaction between the mailbox rule and § 7502. They have generally concluded that the only legally sufficient evidence establishing the filing date is either the postmark on an envelope or a registered or certified mail receipt." *Woodworth*, 202 B.R. at 644 (citations omitted). The only proof provided of filing, or in other words, delivery to the IRS, was the testimony of the debtor and his wife which was insufficient.

Consumer Bankruptcy Panel, June 2022
Chief Judge Henry Callaway
Career law clerk Jennifer Morgan
United States Bankruptcy Court
Southern District of Alabama

Recent Consumer and Bankruptcy Opinions from the Alabama Bankruptcy and District Courts (current through April 24, 2022)

Chapter 7

In re Mitchell, Case No. 17-4324 (Bankr. S.D. Ala. Nov. 18, 2021) (Callaway, J.)

The court denied the chapter 7 trustee's motion for the debtor to turn over postpetition rent proceeds from rental property where the debtor had assigned the rents to the mortgagee prepetition. Either (1) the mortgagee had an absolute right to the rent proceeds and the bankruptcy estate had no interest in them, or (2) the mortgagee had a perfected security interest in the rent with no equity for the bankruptcy estate.

Bad faith filings

In re Bulger, 2021 WL 5991750 (Bankr. M.D. Ala. Dec. 17, 2021) and In re Bulger, 2022 WL 348627 (Bankr. M.D. Ala. Feb. 4, 2022) (Creswell, J.)

The bankruptcy case dismissed the debtor's case with a two-year refiling ban. The court found that there was no question the case should be dismissed because the debtor failed to obtain prepetition credit counseling. The court also found that the debtor's "use of the bankruptcy process as a tactic to stall his largest creditors and an attempt to leverage a settlement" in a pending state court case, combined with multiple inaccuracies and omissions in his bankruptcy schedules, warranted dismissal under Bankruptcy Code § 707(a) and imposition of a two-year bar against refiling under Code § 349(a). The court subsequently denied the debtor's motion for a stay and injunction pending appeal.

* The debtor has appealed this case on multiple grounds, including whether a bankruptcy court may impose an injunction on refiling beyond 180 days.

Administrative expenses

In re Weldy, Case No. 21-10325 (Bankr. S.D. Ala. Nov. 1, 2021) (Callaway, J.)

The debtor converted her chapter 7 case to chapter 13 before the chapter 7 trustee could market her house. The court awarded the former chapter 7 trustee a quantum meruit administrative expense based on a lodestar time and hourly rate analysis. The trustee expended time uncovering potential assets in the chapter 7 case which benefitted the estate and prompted the debtor to move to convert the case to chapter 13. But the court agreed with the debtor that some fees requested were for normal chapter 7 trustee work, rather than specific work toward

liquidation of potential assets, and reduced the fee sought. The court also allowed the trustee an expense for an informal valuation of the debtor's home.

DSO

In re Black, Case No. 17-4773 (Bankr. S.D. Ala. Jan. 20, 2022) (Callaway, J.)

A postpetition child support obligation is not "property or services necessary for the debtor's performance under the plan" under Bankruptcy Code § 1305(a). The court thus disallowed DHR's claims for postpetition child support. However, if both the debtor and the DSO creditor agreed, the court might allow payment of postpetition child support through a chapter 13 plan if the plan paid 100% to unsecured creditors.

Late-filed claims

In re Tice, 2022 WL 532741 (Bankr. M.D. Ala. Feb. 22, 2022) (Creswell, J.)

The court sustained the chapter 13 trustee's objection to a creditor's claim filed six months after the bar date. The court found that knowledge of the bankruptcy was imputed to the creditor and there was no ground to extend the time for filing a claim where notice of the bankruptcy was sent to the creditor's state court counsel and acknowledged in the state court case.

Automatic stay

In re Dellinger, 2021 WL 4465583 (Bankr. N.D. Ala. Sept. 29, 2021) (Robinson, J.)

Creditors filed a state court case against the debtor after he filed for chapter 7 bankruptcy. They moved for relief from stay in the bankruptcy court to keep prosecuting the state court case. Based on a notification from debtor's counsel and the bankruptcy trustee that they consented to the relief, the court granted the motion. A few months later, the creditors filed another motion because the debtor (now represented by new counsel) was raising the issue that the state court case – filed postpetition – would usually be considered void, not voidable. Because the debtor consented to the original motion, even if the automatic stay would have otherwise voided the state court case, the original order granting relief from stay ratified and revived the lawsuit and the debtor was estopped from challenging the validity and continuance of the state court case.

Modification of chapter 13 plans

In re Ertha, Case No. 18-551 (Bankr. S.D. Ala. Dec. 2, 2021) (Callaway, J.)

When a trustee seeks to modify a confirmed chapter 13 plan to increase the distribution to unsecured creditors because of a postconfirmation personal injury settlement, debtors are entitled to a credit against the amount owed under the liquidation test of Bankruptcy Code § 1325(a)(4) for payments that they have made or will make to unsecured creditors under the plan pursuant to the disposable income test of Code § 1325(b). Put another way, the projected disposable income test and the liquidation test are separate, not stacked. However, the credit is only for plan payments to unsecured creditors – not the total plan payments – since the liquidation test looks at what unsecured creditors are being paid.

In re Abrams, 632 B.R. 240 (Bankr. S.D. Ala. Aug. 24, 2021) (Oldshue, J.)

The court denied the chapter 13 trustee's request to increase the plan payments and the percentage to unsecured creditors. The debtor was below median income and the applicable commitment period was only 36 months, but the confirmed plan was for 42 months and included payment of a secured debt to J & J Furniture. After J & J failed to file a proof of claim and the debtor got two months behind on plan payments, the trustee moved to increase the payments and the percentage to unsecured creditors. However, the court found that the debtor could still comply with the liquidation analysis and the disposable income test without an increase in either the percentage or plan payment. Further, increasing the dividend to unsecured creditors by using the funds originally allocated for the secured claim would essentially penalize the debtor for seeking to address all his debts in his plan at the outset of the case.

Lien avoidance

In re Barbee, 2021 WL 4448550 (Bankr. S.D. Ala. Sept. 28, 2021) (Callaway, J.)

The court granted the debtor's motion to avoid judicial lien. The debtor and his wife took their homestead property as tenants in common for life with a contingent remainder in the survivor, not as joint tenants. Under Alabama law, only the debtor's life estate in the property – not his contingent remainder interest – was subject to the creditor's judicial lien. The court accepted the testimony of the debtor's expert about the value of the debtor's life estate interest in the property. Because that value was less than the debtor's homestead exemption, the court found that the lien was due to be avoided. The court also found that the motion was due to be granted under the traditional valuation approach of *In re Lehman*, 205 F.3d 1255 (11th Cir. 2000).

Debtor's retention of assets

In re Pugh, Case No. 17-4078 (Bankr. S.D. Ala. Aug. 12, 2021) (Callaway, J.)

The insurance proceeds for a wrecked vehicle were more than the scheduled value but less than the total of the scheduled value and the amount the debtor could exempt. The court credited the debtor for "pay down" of the secured claim and ordered that most of the net auto insurance funds be paid to the debtor after paying the small balance left on the secured claim. But because the debtor was behind on her plan payments, the court ordered that the amount necessary to bring the plan current be remitted to the chapter 13 trustee with the percentage to unsecured creditors to remain the same.

Exemptions

In re McCallan, 629 B.R. 491 (Bankr. M.D. Ala. May 7, 2021) (Sawyer, J.)

The bankruptcy court partially sustained the chapter 7 trustee's objections to the debtor's exemptions, and imposed an equitable lien against Florida property that the debtor and his wife owned as tenants by the entirety. Florida law allow an equitable lien to be imposed on property acquired by fraudulent means and the court found that the debtor used the proceeds for his fraudulent debt management scheme to acquire his home and its contents. The debtor could not

claim Florida's homestead exemptions because he was not domiciled there during the 730 days prior to his filing.

* The district court affirmed the bankruptcy court's ruling on March 30, 2022.

Student loans

In re Wheat, 2022 WL 243221 (Bankr. M.D. Ala. Jan. 25, 2022) (Sawyer, J.)

The court denied the defendants' motion to reconsider its 2019 order discharging the debtor's student loans. The defendants' interpretation of the "certainty of hopelessness" language in a way that debtor could not discharge their student loans unless they showed that their current circumstances would never change was "simply not the standard." Such an interpretation would "swallow the rule and make it impossible for any debtor to ever satisfy" the *Bruner* test.

In re Acosta-Conniff, 632 B.R. 322 (Bankr. M.D. Ala. Sept. 29, 2021) (Sawyer, J.)

The court found that the chapter 7 debtor, a 44-year-old single mother with two dependent children, who worked as a public school teacher, met all the prongs of the *Bruner* "undue hardship" test and thus her student loan debtor of $112,000 was dischargeable. The debtor demonstrated good faith efforts to repay her debt: she had made payments totaling $9,275, she obtained multiple forbearances and one deferment, several times the debtor sought partial forgiveness of the debt for teaching in a rural area but was denied, the debtor's reasoning for not enrolling in an income-contingent repayment plan (ICRP) was not to avoid repayment, but because of her belief that she lacked the available income to repay the debt "in any amount," the debtor had attempted, without success, to find better employment by applying for administrative positions, the debtor had worked part-time besides her full-time teaching position, and the debtor had minimally budgeted for her family's basic needs, with minimal extraneous spending.

Dischargeability

In re Raley, Case No. 20-10482 (Bankr. S.D. Ala. Nov. 2, 2021) (Oldshue, J.)

The movants sought relief from the automatic stay to proceed with pending litigation against the individual debtor in another forum related to allegations of securities fraud and also requested an extension of time to file a dischargeability complaint. The court noted that entry of the discharge order mooted the motion for relief. Further, on considering the totality of the circumstances and pertinent factors, the court determined that "cause" existed to allow a thirty day extension for movants to file a dischargeability complaint.

In re Merchant, 2021 WL 3745944 (Bankr. N.D. Ala. Aug. 23, 2021) (Robinson, J.)

Plaintiffs were not barred by issue or claim preclusion from pursuing their nondischargeability claims against a debtor because there had never been a judgment on the merits on the plaintiffs' fraud claims in state court.

The Estates of Robert Moss and Brenda Moss, et al. v. Dorand, AP No. 21-3003 (Bankr. N.D. Fla. Aug. 3, 2021) (Callaway, J.)

The court denied the plaintiffs' summary judgment motion on their nondischargeability claim under 11 U.S.C. § 523(a)(2)(A). Because the underlying state court judgment at issue was an Alabama judgment, the court applied Alabama collateral estoppel law. The state court judgment did not state that the court found for the plaintiffs on their fraud claim; the court could have accepted the plaintiffs' testimony on breach of contract only and entered its judgment on that claim. Even so, under Alabama law, not all types of fraud will support a judgment of nondischargeability, and the court could not determine from the record before it the nature of the fraud that was pleaded or proven.

Discharge injunction

Matter of Coffey, 2022 WL 243223 (Bankr. N.D. Ala. Jan. 25, 2022) (Jessup, J.)

Chapter 13 debtor sought to reopen her case to related to an alleged violation of the discharge injunction by a creditor that repossessed her vehicle. The debtor paid the value of the vehicle through her claim plus interest at the plan (not contract) rate. After the discharge, the non-filing codebtor remained liable for the unpaid contract interest. The court found no cause to reopen the case because the creditor's lien survived post-discharge as to the non-filing codebtor and there was thus no relief available to the debtor related to the creditor's post-discharge repossession of the vehicle. The codebtor stay no longer applied after the debtor was discharged.

Fraudulent transfers

Wilkins v. McCallan, 2022 WL 610308 (Bankr. M.D. Ala. Mar. 1, 2022) (Sawyer, J.)

The chapter 7 trustee could recover $5.6 million in cash transfers that the debtor (or entitled controlled by him) made to his wife. The transfers were constructively fraudulent because none of the transfers were for adequate consideration and the debtor was insolvent with the transfers were made. The court also found evidence of actual fraud.

* The case has been appealed.

Title pawns

In re Hambright, 635 B.R. 614 (Bankr. N.D. Ala. Feb. 4, 2022) (Henderson, J.)

A motor vehicle, as opposed to its certificate of title, was not a pledged good under Alabama Pawnshop Act's automatic forfeiture provision. Thus, the pawnbroker did not acquire absolute title to the vehicle and the debtor could modify the pawnbroker's rights in her chapter 13 bankruptcy.

* The pawnbroker's appeal is currently pending.

In re Arnett, 634 B.R. 1078 (Bankr. M.D. Ala. Dec. 16, 2021) (Sawyer, J.)

A title pawn contract provision stating that the borrower did not intend to file bankruptcy violated public policy and was unenforceable against a debtor who filed chapter 13 shortly thereafter. Because the contract provision was unenforceable, the pawnbroker could not use that provision to show that the debtor filed in bad faith.

* This decision involved two separate bankruptcy cases; the pawnbroker has appealed in both cases.

Extinguishment of mortgages

In re Karr, 2022 WL 677456 (Bankr. N.D. Ala. Mar. 7, 2022) (Robinson, J.) (motion to alter or amend pending as of April 25, 2022)

Chapter 7 debtor did not schedule any real estate when he filed for chapter 7 bankruptcy relief. The chapter 7 trustee discovered in the county real estate records that the debtor owned a one-half interest in property, which the trustee then proposed to sell for the benefit of the debtor's unsecured creditors. Through a series of mistakes, only the debtor's wife's one-half interest in the property had been previously sold at a foreclosure sale, but the creditor's credit bid at the sale was for the entire mortgage debt. The bank objected to the sale of the debtor's one-half interest in the property, but the court found that the mortgage was extinguished when the bank bid the entire secured debt in exchange for the conveyance of the wife's interest at the foreclosure sale. The mortgage terminated once the debt was satisfied, and the debtor's interest in the property entered the estate free and clear of any prior mortgage.

Attorney sanctions

In re McCallan, 2022 WL 804091 (M.D. Ala. Mar. 15, 2022)

The district court found that the bankruptcy court abused its discretion in sanctioning an attorney who filed an email containing offensive and insulting language into the record without redaction or asking the email to be placed under seal. Although the attorney could have used one of those methods in filing the email, no rule specifically required that and thus sanctions were unwarranted.

Employment of professionals/approval of fees

In re McLemore, 2022 WL 362915 (Bankr. M.D. Ala. Feb. 7, 2022) and In re McLemore, 2022 WL 618958 (Bankr. M.D. Ala. Mar. 2, 2022) (Sawyer, J.)

The court ordered the law firm representing the debtor in a personal injury case to turn over the entire amount of the $40,000 settlement because the firm failed to determine whether the debtor was in bankruptcy before settling the case and failed to obtain bankruptcy court approval before disbursing estate property. The firm's lawyers "could have easily avoided the quandary" by checking PACER, and the firm had "a well-established history of converting estate

property, to the benefit of its clients and to the detriment of bankruptcy estates." The court subsequently denied the motion to alter or amend filed by one of the firm's lawyers.

* This case is currently on appeal.

Upright Law

In re Deighan Law LLC, 2022 WL 630892 (Bankr. M.D. Ala. Mar. 4, 2022) (Sawyer, J.)

The court ordered a Chicago-based law firm to pay a civil penalty of $500,000 and disgorge all fees it received in over 80 cases identified by the bankruptcy administrator. The court found that the firm engaged in the unauthorized practice of law and that the quality of work in those cases ranged "from substandard to abysmal." Judge Hawkins denied the law firm's motion to reconsider.

Abusive filings

In re Haney, Case No. 21-02007 (Bankr. N.D. Ala.) (Mitchell, J.)

The pro se debtor filed voluminous documents in both the main bankruptcy and a related adversary proceeding, many of which contained malicious and vicious accusations. The bankruptcy judge issues numerous orders, including orders that the debtor was to immediately cease repetitive and duplicate filings and, after those filings continued, that the court may enter orders summarily by handwriting its ruling on the front page of the document and having it entered by the clerk's office. The court also denied the debtor's motions for recusal (which the debtor has now appealed). Most recently, citing bankruptcy's goal of giving debtors an opportunity for a fresh start, the court found that the debtor may only stay in bankruptcy if she acts in a civilized and business-like way. See In re Haney, 2022 WL 412809 (Bankr. M.D. Ala. Feb. 10, 2022). However, if the debtor violated the terms of the order or any other orders, then the court retained discretion to dismiss the case.