RECENT BANKRUPTCY CASES OF INTEREST

2022 Nevada District Court Conference
The Business of Law

Bankruptcy Breakout Session
May 17, 2022
3:15 – 4:30 p.m.

Speaker Panel:

Hon. Gregg W. Zive (Bankr. D. Nev.)
Hon. Mike K. Nakagawa (Bankr. D. Nev.)
Hon. August B. Landis (Bankr. D. Nev.)
Hon. Gary Spraker (Bankr. D. Alaska)

United States Supreme Court Cases

Buckley v. Bartenwerfer (*In re* Bartenwerfer), 860 F. App'x 544 (9th Cir. Aug. 12, 2021), *cert. granted*, 2022 WL 1295707 (May 2, 2022)

Siegel v. Fitzgerald (*In re* Circuit City Stores, Inc.), 996 F.3d 156 (4th Cir. 2021), *cert. granted*, ___ U.S. ___, 142 S. Ct. 752 (Jan. 10, 2022)

Ninth Circuit Court of Appeals Cases

Bank of New York Mellon v. Enchantment at Sunset Bay Condo. Ass'n, 2 F.4th 1229 (9th Cir. 2021)

Nichols v. Marana Stockyard & Livestock Mkt., Inc. (*In re* Nichols), 10 F.4th 956 (9th Cir. 2021)

Ninth Circuit Bankruptcy Appellate Panel Cases

Guevarra v. Whatley (*In re* Guevarra), 2022 WL 884595 (9th Cir. BAP March 25, 2022)

Massis v. Gavin (*In re* Gavin), 2022 WL 768144 (9th Cir. BAP Mar. 14, 2022)

NetJets Aviation, Inc. v. RS Air, LLC (*In re* RS Air, LLC), 2022 WL 1288608 (9th Cir. BAP April 26, 2022)

Stanley v. Mason (*In re* BCB Contracting Servs., LLC), 2022 WL 1198232 (9th Cir. BAP April 21, 2022)

Stuart v. City of Scottsdale (*In re* Stuart), 632 B.R. 531 (9th Cir. BAP 2021), *appeal docketed*, No. 21-60063 (9th Cir. Dec. 17, 2021)

Cases from Outside of the Ninth Circuit

Chicago v. Mance (*In re* Mance), 31 F.4th 1014 (7th Cir. 2022)

United States Supreme Court Cases

KeyCite Yellow Flag - Negative Treatment
Certiorari Granted by Bartenwerfer v. Buckley, U.S., May 2, 2022

860 Fed.Appx. 544
This case was not selected for publication in West's Federal Reporter.
See Fed. Rule of Appellate Procedure 32.1 generally governing citation of judicial decisions issued on or after Jan. 1, 2007. See also U.S.Ct. of App. 9th Cir. Rule 36-3.
United States Court of Appeals, Ninth Circuit.

IN RE: David William BARTENWERFER; Kate Marie Bartenwerfer, Debtors,
Kieran Buckley, Appellant,
v.
David William Bartenwerfer; Kate Marie Bartenwerfer, Appellees.
In re: David William Bartenwerfer; Kate Marie Bartenwerfer, Debtors,
Kieran Buckley, Appellant,
v.
David William Bartenwerfer; Kate Marie Bartenwerfer, Appellees.
In re: David William Bartenwerfer; Kate Marie Bartenwerfer, Debtors,
David William Bartenwerfer; Kate Marie Bartenwerfer, Appellants,
v.
Kieran Buckley, Appellee.

No. 20-60021, No. 20-60023, No. 20-60024
|
Argued and Submitted July 29, 2021 San Francisco, California
|
FILED August 12, 2021

Synopsis
Background: Judgment creditor filed adversary complaint, seeking determination that debt was excepted from discharge because Chapter 7 debtors fraudulently concealed material defects plaguing renovated house that they sold to him prepetition. Following trial, the United States Bankruptcy Court for the Northern District of California, Hannah L. Blumenstiel, J., 549 B.R. 222, ruled that debt was nondischargeable, and appeals were taken. The Bankruptcy Appellate Panel, 2017 WL 6553392, affirmed judgment as to debtor-husband, but vacated and remanded as to debtor-wife. On remand, the Bankruptcy Court, Blumenstiel, J., 596 B.R. 675, entered judgment in favor of debtor-wife. Judgment creditor appealed. The Bankruptcy Appellate Panel, 2020 WL 1970506, affirmed. Cross-appeals were taken.

Holdings: The Court of Appeals held that:

[1] collateral estoppel did not bar judgment creditor's nondischargeability claim, and

[2] in ruling that debtor-husband's fraud was not imputed to debtor-wife, the Bankruptcy Court applied the incorrect legal standard for imputed liability in a partnership relationship.

Affirmed in part, reversed in part, and remanded with instructions.

Procedural Posture(s): On Appeal; Judgment.

West Headnotes (2)

[1] **Judgment** Bankruptcy

Collateral estoppel did not bar judgment creditor's nondischargeability claim against Chapter 7 debtors; in judgment creditor's prepetition state-court action against debtors, jury's findings in favor of judgment creditor on his claim for debtors' alleged nondisclosure of material facts, but not on his claim for intentional misrepresentation, were conflicting, or at least ambiguous. 11 U.S.C.A. § 523(a)(2)(A).

[2] **Bankruptcy** Fraud committed by agent or one other than debtor

In judgment creditor's adversary proceeding against Chapter 7 debtors under the fraud discharge exception, in connection with debtors' alleged fraudulent concealment of material

defects in renovated house that they sold to him prepetition, the Bankruptcy Court applied the incorrect "knew or should have known" legal standard for imputed liability in a partnership relationship to conclude that debtor-husband's fraud was not imputed to his partner, debtor-wife; under the correct standard, debtor-wife's debt was nondischargeable regardless of her knowledge of the fraud. 11 U.S.C.A. § 523(a)(2)(A).

***545** Appeal from the Ninth Circuit Bankruptcy Appellate Panel, Brand, Jury, and Faris, Bankruptcy Judges, Presiding, Taylor, Faris, and Brand, Bankruptcy Judges, Presiding, BAP No. 16-1277, BAP No. 19-1016

Attorneys and Law Firms

Janet Marie Brayer, Attorney, Law Office of Janet Brayer, San Francisco, CA, Stephen Davis Finestone, Finestone Hayes LLP, San Francisco, CA, for Appellant.

Reno F.R. Fernandez, III, Daniel Vaknin, BKC, Macdonald Fernandez LLP, San Francisco, CA, Iain A. Macdonald, Macdonald & Associates, San Francisco, CA, for Appellees.

Before: McKEOWN and NGUYEN, Circuit Judges, and HUCK,[*] District Judge.

MEMORANDUM[**]

As partners, David and Kate Bartenwerfer renovated a house in San Francisco, California and sold it to Kieran Buckley. Shortly after the sale, Buckley alleged defects in the house and sued the Bartenwerfers in California state court for (1) breach of contract, (2) negligence, (3) nondisclosure of material facts, (4) negligent misrepresentation, and (5) intentional misrepresentation. The jury found in Buckley's favor on his breach of contract, negligence, and nondisclosure of material facts claims and against him on his remaining claims and awarded him damages. The Bartenwerfers filed for bankruptcy.

In the bankruptcy court, Buckley initiated an adversary proceeding against the Bartenwerfers, arguing that the state court judgment against the Bartenwerfers could not be discharged in bankruptcy under 11 U.S.C. § 523(a)(2)(A), which provides ***546** that a debtor cannot discharge debt that was obtained through fraud. The bankruptcy court agreed and held that the portion of the state court judgment that was traceable to Buckley's nondisclosure claim was nondischargable. The bankruptcy court found that the Bartenwerfers intended to deceive Buckley and held that Mr. Bartenwerfer had actual knowledge of the false representations made to Buckley and that Mr. Bartenwerfer's fraudulent conduct could be imputed onto Mrs. Bartenwerfer because of their partnership relationship. Additionally, the bankruptcy court declined to apply collateral estoppel in favor of the Bartenwerfers based on the jury's findings of no intentional fraud. On appeal, the Ninth Circuit Bankruptcy Appellate Panel ("BAP") affirmed the bankruptcy court's collateral estoppel ruling, but, adopting the Eight Circuit's "knew or should have known" standard from *Walker v. Citizens State Bank*, 726 F.2d 452 (8th Cir. 1984), remanded the imputed liability finding and instructed the bankruptcy court to determine whether Mrs. Bartenwerfer "knew or should have known" of Mr. Bartenwerfer's fraud. On remand, after an evidentiary hearing, the bankruptcy court held that Mr. Bartenwerfer's fraud could not be imputed onto Mrs. Bartenwerfer because she did not know of the fraud. The BAP affirmed.

Buckley appeals the BAP's decision affirming the bankruptcy court's nondischargeability judgment in favor of Mrs. Bartenwerfer. On cross-appeal, the Bartenwerfers argue that collateral estoppel should apply to bar Buckley's § 523(a)(2)(A) claim. We have jurisdiction under 28 U.S.C. § 158(d), and we affirm in part and reverse in part.

[1]We begin with the Bartenwerfers' cross-appeal. The Bartenwerfers argue that collateral estoppel applies because the state court jury found in their favor on Buckley's intentional misrepresentation claim. The jury found in favor of Buckley on his nondisclosure of material facts claim against the Bartenwerfers, but not on his intentional misrepresentation claim. These two findings are conflicting, or at least ambiguous, which weigh against applying collateral estoppel. *See* *In re Kelly*, 182 B.R. 255, 258 (9th Cir. BAP 1995) ("Any reasonable doubt as to what was decided by a prior judgment should be resolved against allowing the collateral estoppel effect."), *aff'd*, 100 F.3d 110 (9th Cir.

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1996). We affirm on this issue.

[2]In his appeal, Buckley argues that the bankruptcy court erred by failing to apply binding Supreme Court and Ninth Circuit precedent to the question of whether to impute Mr. Bartenwerfer's fraud onto his partner, Mrs. Bartenwerfer, and by holding that the fraud was not imputed. Buckley is correct. Applying basic partnership principles,

> if, in the conduct of partnership business, ... one partner makes false or fraudulent misrepresentations of fact to the injury of innocent persons, ... his partners cannot escape pecuniary responsibility therefor upon the ground that such misrepresentations were made without their knowledge. This is especially so when ... the partners, who were not themselves guilty of wrong, received and appropriated the fruits of the fraudulent conduct of their associate in business.

Strang v. Bradner, 114 U.S. 555, 561, 5 S.Ct. 1038, 29 L.Ed. 248 (1885); *see also* *In re Cecchini*, 780 F.2d 1440, 1444 (9th Cir. 1986) (holding a partner responsible for a tortfeasor/partner's fraud when the fraud was performed "on behalf of the partnership and in the ordinary course of the business of the partnership"), *overruled in other part by* *Kawaauhau v. Geiger*, 523 U.S. 57, 118 S.Ct. 974, 140 L.Ed.2d 90 (1998). Mrs. Bartenwerfer's debt is nondischargeable ***547** regardless of her knowledge of the fraud. By rejecting *Strang* and *Cecchini*, in favor of the "knew or should have known" standard, the bankruptcy court applied the incorrect legal standard for imputed liability in a partnership relationship. We reverse the bankruptcy court's judgment regarding imputed liability against Mrs. Bartenwerfer under § 523(a)(2)(A), and we remand to the bankruptcy court with instructions to enter judgment in favor of Buckley and against Mrs. Bartenwerfer.

We need not address the remaining issues raised on Buckley's direct appeal.

AFFIRMED IN PART; REVERSED IN PART AND REMANDED.

All Citations

860 Fed.Appx. 544

Footnotes

* The Honorable Paul C. Huck, United States District Judge for the U.S. District Court for Southern Florida, sitting by designation.

** This disposition is not appropriate for publication and is not precedent except as provided by Ninth Circuit Rule 36-3.

End of Document

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KeyCite Yellow Flag - Negative Treatment
Certiorari Granted by Siegel Trustee of Circuit City Stores, Inc. Liquidating Trust v. Fitzgerald, U.S., January 10, 2022

996 F.3d 156
United States Court of Appeals, Fourth Circuit.

IN RE: CIRCUIT CITY STORES, INCORPORATED; Circuit City Stores West Coast, Incorporated; InterTAN, Inc.; Ventoux International, Inc.; Circuit City Purchasing Company, LLC; CC Aviation, LLC; CC Distribution Company of Virginia, Inc.; Circuit City Properties, LLC; Kinzer Technology, LLC; Abbott Advertising Agency, Incorporated; Patapsco Designs, Inc.; Sky Venture Corp.; PRAHS, Inc. (N/A); XSStuff, LLC; Mayland MN, LLC; Courchevel, LLC; Orbyx Electronics, LLC; Circuit City Stores PR, LLC, Debtors.
Alfred H. Siegel, Trustee of the Circuit City Stores, Inc. Liquidating Trust, Plaintiff – Appellee,
v.
John P. Fitzgerald, III, Acting United States Trustee for Region 4, Defendant – Appellant.
Acadiana Management Group, LLC; Albuquerque-AMG Specialty Hospital, LLC; Central Indiana-AMG Specialty Hospital, LLC; LTAC Hospital of Edmond, LLC; Houma-AMG Specialty Hospital, LLC; LTAC of Louisiana, LLC; Las Vegas-AMG Specialty Hospital, LLC; Warren Boegel; Boegel Farms, LLC; Three Bo's, Inc., Amici Supporting Appellee.
In re: Circuit City Stores, Incorporated; Circuit City Stores West Coast, Incorporated; InterTAN, Inc.; Ventoux International, Inc.; Circuit City Purchasing Company, LLC; CC Aviation, LLC; CC Distribution Company of Virginia, Inc.; Circuit City Properties, LLC; Kinzer Technology, LLC; Abbott Advertising Agency, Incorporated; Patapsco Designs, Inc.; Sky Venture Corp.; PRAHS, Inc. (N/A); XSStuff, LLC; Mayland MN, LLC; Courchevel, LLC; Orbyx Electronics, LLC; Circuit City Stores PR, LLC, Debtors.
Alfred H. Siegel, Trustee of the Circuit City Stores, Inc. Liquidating Trust, Plaintiff – Appellant,
v.
John P. Fitzgerald, III, Acting United States Trustee for Region 4, Defendant – Appellee.
Acadiana Management Group, LLC; Albuquerque-AMG Specialty Hospital, LLC; Central Indiana-AMG Specialty Hospital, LLC; LTAC Hospital of Edmond, LLC; Houma-AMG Specialty Hospital, LLC; LTAC of Louisiana, LLC; Las Vegas-AMG Specialty Hospital, LLC; Warren Boegel; Boegel Farms, LLC; Three Bo's, Inc., Amici Supporting Appellant.

No. 19-2240, No. 19-2255
|
Argued: December 8, 2020
|
Decided: April 29, 2021

Synopsis
Background: Trustee of liquidating trust established under debtors' confirmed Chapter 11 plan filed motion to determine extent of liability for post-confirmation quarterly United States Trustee fees, asking the court to order that, notwithstanding amendment of governing statute by the Bankruptcy Judgeship Act of 2017, the amount of such fees be determined based on statutory rates in effect as of petition date in this case. United States Trustee moved for summary judgment. The United States Bankruptcy Court for the Eastern District of Virginia, No. 3:08-bk-35653, Kevin R. Huennekens, J., 606 B.R. 260, granted motion to determine and denied motion for summary judgment, and parties sought leave to appeal directly to the Court of Appeals.

Holdings: The Court of Appeals, King, Circuit Judge, held that:

[1] quarterly fees owed by certain debtors to fund the United States Trustee program were not "taxes," of kind subject to Uniformity Clause of the United States Constitution;

[2] legislation that required the payment of increased quarterly fees in large Chapter 11 cases only in judicial districts in which the United States Trustee program was in effect did not violate the uniformity requirement of the Bankruptcy Clause;

[3] application of legislation in pending Chapter 11 cases to the quarterly fees that accrued thereafter would not have impermissible retroactive effect.

Affirmed in part, reversed in part, and remanded.

Quattlebaum, Circuit Judge, filed opinion concurring in part and dissenting in part.

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Procedural Posture(s): On Appeal; Motion for Summary Judgment; Other.

West Headnotes (15)

[1] **Bankruptcy** Conclusions of law; de novo review
Bankruptcy Clear error

Court of Appeals generally reviews a bankruptcy court's factual findings for clear error and its legal rulings de novo.

1 Cases that cite this headnote

[2] **Internal Revenue** Equality and uniformity of taxes

Uniformity Clause of the United States Constitution applies only to taxes. U.S. Const. art. 1, § 8, cl. 1.

[3] **Bankruptcy** Trustees
Internal Revenue Equality and uniformity of taxes

Quarterly fees owed by certain debtors to fund the United States Trustee program were not "taxes," of kind subject to Uniformity Clause of the United States Constitution. U.S. Const. art. 1, § 8, cl. 1; 28 U.S.C.A. § 1930(a)(6).

1 Cases that cite this headnote

[4] **Bankruptcy** Uniformity requirement
Bankruptcy Trustees

Legislation that required the payment of increased quarterly fees in large Chapter 11 cases only in judicial districts in which the United States Trustee program was in effect, in order to fund shortfall in this program, and not in judicial districts that had a Bankruptcy Administrator, permissibly differentiated between geographic areas to solve a funding shortfall that existed only in judicial districts in which the United States Trustee program was in effect, and thus did not violate the uniformity requirement of the Bankruptcy Clause. U.S. Const. art. 1, § 8, cl. 4.; 28 U.S.C.A. § 1930(a)(6).

3 Cases that cite this headnote

[5] **Bankruptcy** Uniformity requirement

To be constitutionally uniform, a law enacted pursuant to the Bankruptcy Clause must apply uniformly to a defined class of debtors and must also be geographically uniform. U.S. Const. art. 1, § 8, cl. 4.

[6] **Bankruptcy** Uniformity requirement

Uniformity requirement of the Bankruptcy Clause is not straitjacket that forbids Congress from distinguishing among classes of debtors. U.S. Const. art. 1, § 8, cl. 4.

1 Cases that cite this headnote

[7] **Bankruptcy** Uniformity requirement

Bankruptcy law may be constitutionally uniform, as required by the Bankruptcy Clause, and yet may recognize state laws in certain particulars, though such recognition may lead to different results in different states. U.S. Const. art. 1, § 8, cl. 4.

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[8] **Bankruptcy** Uniformity requirement

In proper circumstances, Congress, without violating the uniformity requirement of the Bankruptcy Clause, may take into account differences that exist between different parts of the country and fashion bankruptcy legislation to resolve geographically isolated problems. U.S. Const. art. 1, § 8, cl. 4.

3 Cases that cite this headnote

[9] **Bankruptcy** Uniformity requirement

Uniformity requirement of the Bankruptcy Clause forbids only arbitrary geographic differences. U.S. Const. art. 1, § 8, cl. 4.

2 Cases that cite this headnote

[10] **Constitutional Law** Retrospective laws and decisions; change in law

Applying a statute to events occurring before it was enacted gives rise to Fifth Amendment due process concerns by potentially depriving a party of adequate notice and undermining settled expectations. U.S. Const. Amend. 5.

[11] **Statutes** Language and Intent; Express Provisions

Courts utilize a two-step analysis on retroactivity challenge to legislation, under which they first apply ordinary tools of statutory construction and ask whether Congress has expressly prescribed the statute's proper reach.

[12] **Statutes** Prospective or Retroactive Construction
Statutes Language and Intent; Express Provisions

If Congress has expressly prescribed the proper temporal reach of statute, then that is the end of the matter, and court does not proceed to second step of retroactivity analysis; only if there is no express Congressional command does court proceed to second step of analysis and decide whether applying the new provision results in an impermissible retroactive consequence by affecting substantive rights, liabilities, or duties on the basis of conduct arising before its enactment.

[13] **Bankruptcy** Retrospective operation
Bankruptcy Trustees

Legislation that required payment of increased quarterly fees in large Chapter 11 cases in attempt to make up funding deficiency in the United States Trustee program, by its clear and unambiguous terms, applied in Chapter 11 cases that were pending when the legislation went into effect to require payment of increased quarterly fees going forward by debtors that met the requirements for payment of increased fees; language in statute, providing that increased fees would be paid "in each case" and "for each quarter," with no limitation based on when the case was filed, sufficiently manifested an intent that the legislation should apply in pending cases. 28 U.S.C.A. § 1930(a)(6).

2 Cases that cite this headnote

[14] **Bankruptcy** Retrospective operation
Bankruptcy Trustees

Even assuming that legislation that required

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payment of increased quarterly fees in large Chapter 11 cases was ambiguous as to whether these increased fees applied in Chapter 11 cases that were pending when the legislation went into effect, application of legislation in pending Chapter 11 cases to the quarterly fees that accrued thereafter would not have retroactive effect, as not impairing rights that a party possessed when legislation went into effect, increasing a party's liability for past conduct, or imposing new duties with respect to transactions already completed. 28 U.S.C.A. § 1930(a)(6).

[15] **Statutes**—Presumptions and inferences

While there is a presumption against the retroactive application of statutes, that presumption only applies if there is a possibility that a statute attaches new legal consequences to events completed before its enactment.

***159** Appeals from the United States Bankruptcy Court for the Eastern District of Virginia, at Richmond. Kevin R. Huennekens, Bankruptcy Judge. (3:08-bk-35653)

Attorneys and Law Firms

ARGUED: Jeffrey E. Sandberg, UNITED STATES DEPARTMENT OF JUSTICE, Washington, D.C., for Appellant/Cross-Appellee. Andrew William Caine, PACHULSKI STANG ZIEHL & JONES LLP, Los Angeles, California, for Appellee/Cross-Appellant. ON BRIEF: Joseph H. Hunt, Assistant Attorney General, Mark B. Stern, Civil Division, Ramona D. Elliott, Deputy Director/General Counsel, P. Matthew Sutko, Associate General Counsel, Beth Levene, Executive Office for United States Trustees, UNITED STATES DEPARTMENT OF JUSTICE, Washington, D.C., for Appellant/Cross-Appellee. Lynn L. Tavenner, Paula S. Beran, David N. Tabakin, TAVENNER & BERAN, PLC, Richmond, Virginia, for Appellee/Cross-Appellant. Bradley L. Drell, Heather M. Mathews, GOLD, WEEMS, BRUSER, SUES & RUNDELL, Alexandria, Lousiana, for Amici Acadiana Management Group, LLC, Albuquerque-AMG Specialty Hospital, LLC, Central Indiana-AMG Specialty Hospital, LLC, LTAC Hospital of Edmond, LLC, Houma-AMG Specialty Hospital, LLC, LTAC of Louisiana, LLC, Las Vegas-AMG Specialty Hospital, LLC, Warren Boegel, Boegel Farms, LLC, and Three Bo's, Inc.

Before KING and QUATTLEBAUM, Circuit Judges, and TRAXLER, Senior Circuit Judge.

Opinion

Affirmed in part, reversed in part, and remanded by published opinion. Judge King wrote the majority opinion, in which Senior Judge Traxler joined. Judge Quattlebaum wrote a separate opinion concurring in part and dissenting in part.

KING, Circuit Judge:

These consolidated appeals present two constitutional issues concerning changes made to the bankruptcy laws nearly four years ago. Alfred H. Siegel, Trustee of the Circuit City Stores, Inc., Liquidating Trust (the "Circuit City Trustee"), sought a ruling in 2019 on his liability for quarterly fees assessed under a 2017 Amendment to the bankruptcy fees provisions of the United States Code (the "2017 Amendment"). In response, the Bankruptcy Court for the ***160** Eastern District of Virginia ruled that the fees aspect of the 2017 Amendment is unconstitutional. *See* *In re Circuit City Stores, Inc.*, 606 B.R. 260 (Bankr. E.D. Va. 2019), ECF No. 2 (the "Bankruptcy Opinion"). That ruling was based on a perceived lack of uniformity between quarterly fees in the two types of bankruptcy court districts, that is, U.S. Trustee districts and Bankruptcy Administrator districts.

John P. Fitzgerald, III, the Acting U.S. Trustee for Region 4 (the "U.S. Trustee"), maintains that the Bankruptcy Opinion erred in its uniformity ruling and has appealed. The Circuit City Trustee, on the other hand, has cross-appealed a separate aspect of the Opinion that rejected his claim concerning retroactive application of the 2017 Amendment. In November 2019, the Circuit City Trustee and the U.S. Trustee jointly certified these appeals to this Court.[1] We granted their joint petition for permission to appeal and consolidated the appeals. The U.S. Trustee's appeal is designated as No. 19-2240, and the Circuit City Trustee's cross-appeal is designated as No. 19-2255.

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As explained below, we rule in favor of the U.S. Trustee in each appeal. That is, we reverse the Bankruptcy Opinion's uniformity decision challenged by the U.S. Trustee, and we affirm the Opinion's retroactivity decision challenged by the Circuit City Trustee. As a result, we remand to the bankruptcy court for such other and further proceedings as may be appropriate.

I.

A review of the pertinent background and operations of the bankruptcy courts is essential to an understanding of these proceedings. Before addressing the legal issues presented, we will discuss some historical context of those courts, as well as the factual background of these proceedings.

A.

The bankruptcy courts operate under two distinct programs for the handling of their proceedings — the Trustee program and the Bankruptcy Administrator program. Congress initiated this two-program system in 1978 when it launched the Trustee pilot program within the Department of Justice. The Trustee pilot program was successful and became a permanent fixture in 1986. Eighty-eight of the 94 judicial districts operate with U.S. Trustees. The other districts — in Alabama and North Carolina — utilize the Bankruptcy Administrator program, which is overseen by the Judicial Conference of the United States.[2]

These bankruptcy court programs utilize distinct funding sources. The judiciary's general budget, overseen by the Judicial Conference, funds the Bankruptcy Administrator program. On the other hand, the bankruptcy debtors in Trustee districts primarily fund the Trustee program. Although annual congressional appropriations provide support for the Trustee program, ***161** Congress anticipated that debtor-paid fees would completely offset the program's cost. Debtor fees include Chapter 11 quarterly fees, which are based on quarterly "disbursements" that debtors make to their creditors until the cases are "converted or dismissed." *See* 28 U.S.C. § 1930(a)(6)(A).

At their inception, the Bankruptcy Administrator districts were not required to pay quarterly fees. In 1994, however, the Ninth Circuit ruled this distinction unconstitutional, explaining that the statutory imposition of such quarterly fees in certain districts but not in others was without justification and thus contravened the Bankruptcy Clause of the Constitution. *See* *St. Angelo v. Victoria Farms, Inc.*, 38 F.3d 1525, 1529, 1531-32 (9th Cir. 1994), *amended by* 46 F.3d 969 (9th Cir. 1995). In reaction to that decision, Congress empowered the Judicial Conference to fix and assess quarterly fees in the Bankruptcy Administrator districts that were "equal to those imposed" in the Trustee districts. *See* 28 U.S.C. § 1930(a)(7) ("In districts that are not part of a United States trustee region ..., the Judicial Conference may require the debtor in a case under chapter 11 of title 11 to pay fees equal to those imposed by paragraph (6) of this subsection.").[3] In 2002, the Judicial Conference began to impose quarterly fees in the Administrator districts that were consistent with the fees specified for the Trustee districts. The Administrator districts' quarterly fees are then deposited into a fund that offsets the general judicial branch appropriations rather than Trustee operations. *Id.* Until January 1, 2018, all Chapter 11 debtors, regardless of district, paid quarterly fees consistent with the same disbursement formula. At that point in time, a funding deficit in the Trustee program disrupted the status quo.

For several decades, Congress's annual appropriations to the Trustee program were entirely offset by the quarterly fees. The mid-2010s witnessed a decline in bankruptcy filings, however, and the Trustee program was no longer self-sustaining. Fueled by concerns that the financial burden might shift to taxpayers, Congress enacted the 2017 Amendment.[4] That Amendment altered the quarterly fees formula and increased the fees due in large Chapter 11 bankruptcy cases, on a temporary basis, during fiscal years 2018 through 2022. This fee increase is conditional, and it is only applicable if the Trustee Fund contains a balance of less than $200 million as of September 30 of the most recent fiscal year. The quarterly fee increase only applies to those bankruptcy debtors with disbursements of $1,000,000 or more in any quarter. If those criteria are satisfied, the quarterly fee is then the lesser of 1 percent of such disbursements, or $250,000. This potential fee is a substantial ***162** increase from the previous maximum fee of $30,000.

Initially, only those bankruptcy debtors in the Trustee districts incurred fee increases as a result of the 2017 Amendment. Several Trustee district bankruptcy courts applied the increased fees to quarterly disbursements that postdated the Amendment. As a result, large Chapter 11 debtors with bankruptcy cases pending on January 1, 2018, incurred increased fees for disbursements beginning in the first quarter of 2018. The bankruptcy debtors in the

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Administrator districts, however, were not subjected to increased quarterly fees. The Judicial Conference adopted an amended fee schedule in September 2018 and applied the increased fees to those bankruptcy cases filed in the six Bankruptcy Administrator districts on or after October 1, 2018. Consequently, any debtor in an Administrator district that filed for bankruptcy prior to October 1, 2018, does not owe increased quarterly fees, regardless of how long the bankruptcy case remains pending.

B.

1.

Circuit City Stores, Inc., and its affiliates (collectively "Circuit City") operated a chain of consumer electronic retail stores throughout the United States. In 2008, Circuit City filed for Chapter 11 bankruptcy protection in the Eastern District of Virginia, which is a Trustee district. In 2010, the bankruptcy court in eastern Virginia confirmed Circuit City's Chapter 11 liquidation plan. That plan provides, with respect to "fees that become due and payable" under 28 U.S.C. § 1930, that the Circuit City Trustee "shall pay [those] fees to the U.S. Trustee until the Chapter 11 Cases are closed or converted and/or the entry of the final decrees." *See* J.A. 110.[5] Circuit City's bankruptcy proceedings remained pending on January 2018, after the 2017 Amendment went into effect.

The Circuit City Trustee initially paid the increased quarterly fees. His willingness to pay those fees diminished, however, when the bankruptcy court in the Western District of Texas ruled in February 2019 that the 2017 Amendment is unconstitutional because it creates nonuniform bankruptcy laws in contravention of the Bankruptcy Clause, and also because it is unconstitutionally retroactive. *See* *In re Buffets, LLC*, 597 B.R. 588 (Bankr. W.D. Tex. 2019).[6] On March 28, 2019, the Circuit City Trustee filed for similar relief in the Eastern District of Virginia, seeking to limit his liability for quarterly fees assessed under 28 U.S.C. § 1930(a)(6). *See generally* J.A. 348-63. The Circuit City Trustee maintained that he was excused from complying with the revised quarterly fee schedule for the reasons adopted by the *Buffets* bankruptcy court decision in Texas — that is, the 2017 Amendment impermissibly created nonuniform bankruptcy laws that are unconstitutionally retroactive.[7] The U.S. Trustee opposed Circuit City's requests, maintaining that Congress's temporary, prospective increase ***163** in quarterly fees for a subset of Chapter 11 cases is not retroactive and does not implicate any constitutional uniformity issues.

2.

a.

By its Bankruptcy Opinion of July 15, 2019, the bankruptcy court in eastern Virginia granted Circuit City's request for relief. The court ruled that the quarterly fees imposed could be classified either as a tax or as a user fee under the Bankruptcy Code and, under either designation, the 2017 Amendment contravenes both the Bankruptcy Clause and the Uniformity Clause of the Constitution. *See* Bankruptcy Opinion 14.[8] If the quarterly fees are a tax, according to the Opinion, the 2017 Amendment contravenes the Uniformity Clause because such fees are not applied in a geographically uniform manner. *Id.* Alternatively, if the quarterly fees are Chapter 11 user fees, the Opinion ruled that the 2017 Amendment is yet unconstitutional because it violates the Bankruptcy Clause, which empowers Congress to establish uniform laws for bankruptcy in the United States. *Id.* For support, the Opinion relied on the fact that, for the first three quarters of 2018, the Judicial Conference did not increase quarterly fees in the Bankruptcy Administrator districts. *Id.* at 12. As the Opinion explained, the Bankruptcy Administrator districts imposed the amended quarterly fee schedule for bankruptcy cases filed after on or October 1, 2018. With these underpinnings, the Opinion ruled that the quarterly fees owed by the Circuit City Trustee under the 2017 Amendment "since January 1, 2018, [are unconstitutional and] must be determined based on the prior version of the statute." *Id.* at 14.

b.

The Bankruptcy Opinion also addressed Circuit City's retroactivity contention. As the Opinion explained, Congress had not explicitly defined the 2017 Amendment's temporal reach. *See* Bankruptcy Opinion 10. It was thus for the courts to decide whether the 2017 Amendment applied to bankruptcy cases pending when the Amendment became effective. The Opinion then ruled that the increased quarterly fees in Trustee districts do not contravene any anti-retroactivity principles of the Constitution because, despite the variance in expectations,

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the 2017 Amendment is "substantively prospective" rather than retroactive. *Id.* at 11 (citing *Landgraf v. USI Film Prods.*, 511 U.S. 244, 269 n.24, 114 S.Ct. 1483, 128 L.Ed.2d 229 (1994) ("Even uncontroversially prospective statutes may unsettle expectations and impose burdens on past conduct: a new property tax or zoning regulation may upset the reasonable expectations that prompted those affected to acquire property.")).

c.

In August 2019, the U.S. Trustee appealed to the district court, challenging the Bankruptcy Opinion's ruling that the 2017 Amendment is unconstitutional due to a lack of uniformity. The Circuit City Trustee then cross-appealed the Opinion's ruling on retroactivity. The parties jointly sought permission for direct appeals, bypassing the district court and urging that the constitutional issues relating to the ***164** 2017 Amendment present questions of law "as to which there [are] no controlling decision[s] of [this Court] or of the Supreme Court" and involve matters of "public importance." *See* J.A. 413-16 (citing 28 U.S.C. § 158(d)(2)(A)(i) (authorizing certification to court of appeals by "all the appellants and appellees ... acting jointly")). By Order of November 6, 2019, we granted the joint petition for these appeals, and we possess jurisdiction pursuant to that Order.

II.

[1]We generally review a bankruptcy court's factual findings for clear error and its legal rulings de novo. *See* *In re Birmingham*, 846 F.3d 88, 92 (4th Cir. 2017). Because the relevant facts underlying these appeals are undisputed, the applicable standard of review is de novo.

III.

In his appeal, the U.S. Trustee maintains that the 2017 Amendment is constitutional and lawful in all respects. He thus challenges the Bankruptcy Opinion's ruling that the 2017 Amendment is unconstitutionally nonuniform and contravenes the Bankruptcy Clause and the Uniformity Clause. The Circuit City Trustee, on the other hand, maintains that the bankruptcy court ruled correctly on the uniformity issue being challenged by the U.S. Trustee. The Circuit City Trustee urges in his cross-appeal, however, that the 2017 Amendment's increased fee schedule constitutes an unconstitutional retroactive imposition of quarterly fees. We will assess these appeals in turn.

A.

[2] [3]The U.S. Trustee maintains that the bankruptcy court in eastern Virginia erroneously ruled that that 2017 Amendment's fee increase is unconstitutional. In making that ruling, the Bankruptcy Opinion relied on both the Bankruptcy Clause and the Uniformity Clause. With respect to his Uniformity Clause challenge, the U.S. Trustee finds support in the Fifth Circuit's ruling last year — reversing the decision of the Texas bankruptcy court relied on in the Bankruptcy Opinion — that Chapter 11 quarterly fees are user fees. *See* *Matter of Buffets, L.L.C.*, 979 F.3d 366, 376 n.7 (5th Cir. 2020). Put succinctly, because the Uniformity Clause only applies to taxes, as the U.S. Trustee maintains and as the Fifth Circuit correctly ruled, that Clause is inapplicable here. *Id.* (citing U.S. Const. art. I, § 8, cl. 1 ("Congress may 'lay and collect [t]axes ...; but all Duties, Imposts, and Excises shall be uniform throughout the United States.' ")).

[4]Because the Bankruptcy Opinion incorrectly relied on the Uniformity Clause, the uniformity ruling is left with only one other basis — that the 2017 Amendment violates the Bankruptcy Clause. The Bankruptcy Clause relates to the uniformity issue because Congress is empowered therein to establish uniform bankruptcy laws throughout the United States. The Bankruptcy Opinion, relying on that Clause and the Uniformity Clause, and drawing support from the now reversed decision of the Texas bankruptcy court, ruled that the 2017 Amendment is constitutionally flawed.

The U.S. Trustee contends that the quarterly fees being challenged here fail to implicate either the Uniformity Clause or the Bankruptcy Clause, because the 2017 Amendment is not a substantive bankruptcy law. Accordingly, he maintains that the 2017 Amendment is not subject to either of the uniformity requirements. Of importance, the Fifth Circuit has reversed the Texas bankruptcy court decision on which ***165** the Bankruptcy Opinion relied, stating that "every bankruptcy court dealing with a challenge to the 2017 Amendment" has rejected the contention that the Amendment is not a law "on the subject of Bankruptcies." *See* *Buffets*, 979

F.3d at 377. We are persuaded to the Fifth Circuit's view, in that — as explained further below — there is no constitutional uniformity problem posed by the 2017 Amendment.

[5] [6] [7] [8]To be constitutionally uniform, "[a] law enacted pursuant to the Bankruptcy Clause must: (1) apply uniformly to a defined class of debtors; and (2) be geographically uniform." *See* *In re SCI Direct, LLC*, No. 17-61735, 2020 WL 5929612, at *10 (Bankr. N.D. Ohio Sept. 22, 2020) (citing *Ry. Labor Execs.' Ass'n v. Gibbons*, 455 U.S. 457, 473, 102 S.Ct. 1169, 71 L.Ed.2d 335 (1982)). The Bankruptcy Clause, however, "is not a straitjacket that forbids Congress to distinguish among classes of debtors." *See* *Gibbons*, 455 U.S. at 469, 102 S.Ct. 1169. In fact, as the Supreme Court has emphasized, "[a] bankruptcy law may be uniform and yet may recognize the laws of the State in certain particulars, although such recognition may lead to different results in different States." *Id.* (internal quotation marks omitted). In the proper circumstances, Congress may "take into account differences that exist between different parts of the country, and ... fashion legislation to resolve geographically isolated problems." *Id.*; *see also* *Reg'l R.R. Reorganization Cases*, 419 U.S. 102, 159-61, 95 S.Ct. 335, 42 L.Ed.2d 320 (1974) (recognizing that Act of Congress applicable only to rail carriers in certain regions and to carriers reorganizing within certain time period was uniform under the Bankruptcy Clause, in that it was designed to solve specific regional problem).

Several bankruptcy courts have recently addressed similar constitutional challenges to the 2017 Amendment, and most of those courts have ruled that the Amendment does not present a constitutional uniformity problem.[9] As explained below, the Fifth Circuit's *Buffets* decision correctly resolved the uniformity issue concerning the 2017 Amendment's quarterly fee increase and its application to debtors in the Trustee and Administrator districts. *See* *Buffets*, 979 F.3d 366.

The *Buffets* debtors filed their bankruptcy proceedings in the Western District of Texas in 2016. Those proceedings were pending in 2018 when the increased quarterly ***166** fees required by the 2017 Amendment went into effect. After the *Buffets* debtors declined to pay the increased fees and challenged the constitutionality of the 2017 Amendment on uniformity grounds, the bankruptcy court agreed with the debtors and ruled that the Amendment was not uniform and thus unconstitutional. The U.S. Trustee in Texas appealed, and — as in these appeals — the uniformity issue was certified to the court of appeals.

After concluding that the uniformity requirement of the Bankruptcy Clause is likely applicable to the 2017 Amendment, the Fifth Circuit decided that there is "no uniformity problem" with the Amendment. *See* *Buffets*, 979 F.3d at 377. That decision was made after a careful assessment of the applicable authorities, and the court of appeals recognized that "the uniformity requirement forbids only arbitrary regional differences in the provisions of the Bankruptcy Code." *Id.* at 378 (internal quotation marks omitted). As the court explained, however, the uniformity requirement does not deny Congress the power to enact legislation that resolves regionally isolated problems. *Id.* According to the Fifth Circuit, when Congress determined that it needed to remedy a shortfall in funding for the Trustee districts, it was entitled to "solve the evil to be remedied with a fee increase in just the underfunded districts." *Id.* (internal quotation marks omitted). Thus, the court of appeals explained, "[i]t is reasonable for Congress to have those who benefit from the Trustee program fill the hole in its finances." *Id.* at 380.

[9]As emphasized by the Fifth Circuit, the Bankruptcy Clause forbids only "arbitrary" geographic differences. And the Supreme Court has never held that a statute contravened the Bankruptcy Clause because of arbitrary geographic distinctions. For example, in the railroad setting, the Court allowed Congress to establish a special court and enact statutes to benefit bankrupt rail carriers in the northeast and midwest, as those were the only railroads facing the problem. *See* *Reg'l R.R. Reorganization Cases*, 419 U.S. at 159-61, 95 S.Ct. 335.

Just as it had successfully addressed the failure of certain railroads, Congress was confronted here with a U.S. Trustee problem. The 2017 Amendment drew a program-specific distinction that only indirectly has a geographic impact. *See* *Buffets*, 979 F.3d at 378. Although the Amendment may render it more expensive for some debtors in Virginia — as opposed to North Carolina or Alabama — to go through Chapter 11 proceedings, the 2017 Amendment does not draw an arbitrary distinction based on the residence of the debtors or creditors. Instead, the distinction is simply a byproduct of Virginia's use of the Trustee program. By increasing quarterly fees for large Chapter 11 bankruptcies in Trustee districts, Congress solved the shortfall in the program's funding. The Administrator districts, which are funded by the judiciary's general budget, did not face a similar financial issue. Because only those debtors in

Trustee districts use the U.S. Trustees, Congress reasonably solved the shortfall problem with fee increases in the underfunded districts. *Id.*

As recognized by the Fifth Circuit, the Ninth Circuit had observed in 1995 that the establishment of separate Trustee and Administrator districts was an "irrational and arbitrary" distinction for which Congress had given "no justification." *See* *St. Angelo*, 38 F.3d at 1532. The 2017 Amendment, however, does not suffer from any such shortcoming. Congress has provided a solid fiscal justification for its challenged action: to ensure that the U.S. Trustee program is sufficiently funded by its debtors ***167** rather than by the taxpayers. Because the 2017 Amendment does not contravene the uniformity mandate of either the Uniformity Clause or the Bankruptcy Clause, we are constrained to reverse the bankruptcy court and resolve appeal No. 19-2240 in favor of the U.S. Trustee.[10]

B.

Turning to the cross-appeal pursued by the Circuit City Trustee, we must decide whether the 2017 Amendment impermissibly applies to bankruptcy cases that were pending when the Amendment took effect. As explained heretofore, the bankruptcy court in Virginia characterized the 2017 Amendment as substantively prospective, and thus not in violation of any anti-retroactivity constitutional principles. On appeal, the Circuit City Trustee contends that, regardless of the statutory language, applying the new quarterly fees to pending bankruptcy cases is unconstitutionally retroactive. The Circuit City Trustee thus contends that the "exponential statutory increase" in quarterly fees could not have been anticipated when Circuit City's bankruptcy reorganization plan was confirmed. *See* Br. of Appellee 6.

[10] [11] [12]Applying a statute to events occurring before it was enacted gives rise to Fifth Amendment due process concerns. *See* *Landgraf v. USI Film Prods.*, 511 U.S. 244, 266, 114 S.Ct. 1483, 128 L.Ed.2d 229 (1994). Indeed, such a retroactive application may deprive a party of adequate notice and undermine "settled expectations." *Id.* at 265, 114 S.Ct. 1483. In assessing the retroactive impact of legislation, the courts have utilized a two-step analysis. *Id.* at 280, 114 S.Ct. 1483. First, applying ordinary tools of statutory construction, we ask whether Congress "has expressly prescribed the statute's proper reach." *Id.*; *see also* *Fernandez-Vargas v. Gonzales*, 548 U.S. 30, 37, 126 S.Ct. 2422, 165 L.Ed.2d 323 (2006). And, if Congress did so, "this is the end of the analysis." *See* *Appiah v. INS*, 202 F.3d 704, 708 (4th Cir. 2000). Only if that effort fails do the courts proceed to the second step. At step two, a reviewing court must determine whether applying the new provision results in an impermissible retroactive consequence by "affecting substantive rights, liabilities, or duties on the basis of conduct arising before its enactment." *See* *Fernandez-Vargas*, 548 U.S. at 37, 126 S.Ct. 2422 (quoting *Landgraf*, 511 U.S. at 278, 114 S.Ct. 1483). The question for the cross-appeal is thus whether the 2017 Amendment, by its terms, applies to bankruptcy cases that were pending prior to January 1, 2018. If Congress was not clear, we must then decide whether an application of the ***168** Amendment to those pending bankruptcy cases will lead to impermissibly retroactive consequences.

[13]As the text of the 2017 Amendment indicates, Congress intended for the increased quarterly fees to apply to all Chapter 11 cases. The bankruptcy fees provision mandates that quarterly fees be paid "in each case" and "for each quarter ... until the case is converted or dismissed," without limitation based on when the case was filed. *See* 28 U.S.C. § 1930(a)(6)(A). In the 2017 Amendment, Congress directed that "[t]he amendments made by this section" — i.e., the increase in quarterly fees for the larger Chapter 11 cases — "shall apply to quarterly fees payable under section 1930(a)(6) ... for disbursements made in any calendar quarter that begins on or after the date of enactment." *See* Bankruptcy Judgeship Act of 2017, Pub. L. No. 115-72, § 1004, 131 Stat. 1224, 1232 (2017). The Amendment thus makes clear that Congress intended for the increase to apply to all Chapter 11 quarterly fees due in January 2018 or thereafter, without regard to the case's filing date.

Notwithstanding the statutory provision, the Circuit City Trustee contends that Congress never intended for the 2017 Amendment to apply to bankruptcy cases that were pending prior to January 1, 2018. The Circuit City Trustee relies on a 1996 amendment of the same statute and argues that Congress was "crystal clear" in 1996 that the amendment was intended to apply to current cases. *See* Br. of Appellee 22-23. That contention reflects a critical misunderstanding of the 1996 amendment. It was only after several courts reached divergent conclusions about whether Congress intended for the 1996 amendment to apply to ongoing bankruptcy cases that Congress enacted "clarifying legislation," making it explicit that pending cases were covered. *Cf.* *Brown v. Thompson*, 374 F.3d 253, 259 & n.2 (4th Cir. 2004). Unlike the 1996 amendment, the 2017 Amendment plainly applies to all disbursements made after its effective date.

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[14] [15]Even if its terms were somehow ambiguous, however, the 2017 Amendment would have no "retroactive effect" because — consistent with Supreme Court precedent — it does not "impair rights a party possessed when he acted, increase a party's liability for past conduct, or impose new duties with respect to transactions already completed." *See* *Landgraf*, 511 U.S. at 280, 114 S.Ct. 1483. Although there is a presumption against the retroactive application of statutes, that presumption only applies if there is a possibility that a statute "attaches new legal consequences to events completed before its enactment." *Id.* at 270, 114 S.Ct. 1483. The 2017 Amendment plainly applies only to *future* disbursements, which are triggered by a debtor's conduct occurring after the law's effective date. *See* *F.D.I.C. v. Faulkner*, 991 F.2d 262, 266 (1993) ("A statute's application is usually deemed prospective when it implicates conduct occurring on or after the statute's effective date." (citations omitted)).

Of importance here, the Fifth Circuit's *Buffets* decision correctly resolved the retroactivity challenge to the 2017 Amendment. *See* 979 F.3d at 374-76. The court of appeals applied the Amendment only to disbursements made after its effective date. *Id.* at 374. After evaluating the congressional history for applying fee increases to disbursements made after an effective date, the court concluded that Congress had always made fee increases so applicable. *Id.* Its decision compared the increased quarterly fees to property taxes that increase after the purchase of a home. And the Fifth Circuit ruled that the challenged fee increase is not impermissibly ***169** retroactive because it does not impair rights that debtors possessed when they filed for bankruptcy protection, nor does it increase liability for conduct that had already occurred. *Id.* at 375-76. Instead, this quarterly fee increase merely upsets debtors' "expectations as to amounts owed based on future distributions." *Id.* at 375.

In these circumstances, Congress clearly intended for the 2017 Amendment to apply to all disbursements made after its effective date, and it intended for the Amendment to be prospective. It does not increase a debtor's "liability for past conduct, or impose new duties with respect to transactions already completed." *See* *Landgraf*, 511 U.S. at 280, 114 S.Ct. 1483. Although the Circuit City Trustee correctly posits that the Amendment increases the quarterly fees that large Chapter 11 debtors will pay, such debtors were reasonably expected to pay fees pursuant to some formula. Accordingly, we are also constrained to reject the Circuit City Trustee's challenge to the Bankruptcy Opinion's retroactivity ruling and resolve appeal No. 19-2255 in favor of the U.S. Trustee.

IV.

Pursuant to the foregoing, we resolve appeal No. 19-2240 by reversing the bankruptcy court's ruling that the 2017 Amendment is unconstitutionally nonuniform. In appeal No. 19-2255, we affirm the bankruptcy court's decision that the 2017 Amendment is not unconstitutionally retroactive. Finally, we remand for such other and further proceedings as may be appropriate.

AFFIRMED IN PART, REVERSED IN PART, AND REMANDED

QUATTLEBAUM, Circuit Judge, concurring in part and dissenting in part:

Make no mistake about it. We have two types of bankruptcy courts in the United States. Forty-eight states operate as part of the United States Trustee Program under which Unites States Trustees aid the courts in the administration and management of bankruptcy cases. But two states—Alabama and North Carolina—operate under a different system. They use Bankruptcy Administrators rather than United States Trustees. And the differences extend beyond titles. Some Chapter 11 debtors in districts that employ the United States Trustees pay materially more in quarterly fees than similarly situated debtors in districts that employ Bankruptcy Administrators. Those fee differences, in turn, trickle down and reduce the amounts unsecured creditors receive. Therefore, many unsecured creditors in the forty-eight states operating under the United States Trustee Program are receiving less of the amounts owed to them than similarly situated unsecured creditors in Alabama and North Carolina.

The Constitution prohibits this lack of uniformity. Article I, Section 8, Clause 4 of the Constitution, known as the Bankruptcy Clause, grants Congress the power to establish "uniform Laws on the subject of Bankruptcies throughout the United States." Because I believe a faithful application of the Constitution's Bankruptcy Clause renders the statutory scheme permitting these different quarterly fees unconstitutional, I respectfully dissent from the portion of Section III-A of the majority's opinion that finds to the contrary. I concur as to the remainder of the

majority's well-reasoned opinion.

I.

To understand how we arrived at the point where we have two types of bankruptcy courts, I begin with some background. "Before 1978, bankruptcy judges ***170** were responsible for the administration of individual bankruptcy cases, including such tasks as appointing trustees to cases and monitoring individual cases." U.S. GOV'T ACCOUNTABILITY OFF., GAO-GGD-92-133, BANKRUPTCY ADMINISTRATION: JUSTIFICATION LACKING FOR CONTINUING TWO PARALLEL PROGRAMS 3 (1992) [hereinafter GAO Report]. "This responsibility placed administrative, supervisory, and clerical functions on judges in addition to their judicial duties." *Id.* at 3–4.

In an attempt to lessen these functions, in 1978, Congress "launched a trustee pilot program within the Department of Justice." *Matter of Buffets, L.L.C.*, 979 F.3d 366, 370 (5th Cir. 2020) (citing Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549, 2662–65 (1978)). The program successfully reduced the administrative duties of bankruptcy judges and increased oversight of the bankruptcy system. Thus, in 1986, Congress permanently created the United States Trustee Program. The Trustee Program is overseen by the Department of Justice's Executive Office for United States Trustees ("EOUST"), which "provide[s] legal, administrative, and management support to the individual [United States Trustee] districts." GAO Report at 4.

But the Trustee Program only operates in forty-eight states, as "[t]he six districts in Alabama and North Carolina fall under the Bankruptcy Administrator program, which the Judicial Conference oversees." *Buffets*, 979 F.3d at 370. Bankruptcy Administrator districts do not benefit from "[t]he centralized support and oversight that the EOUST and its regional offices provide ...." GAO Report at 4. Instead, "[e]ach of the six [Bankruptcy Administrator] districts is independent, operating as a separate entity." *Id.* The Bankruptcy Administrator program "in each district is headed by a Bankruptcy Administrator who is selected by the U.S. Court of Appeals for a term of 5 years." *Id.* at 4–5. "It was originally thought that the exclusion of Alabama and North Carolina would last only a few years, but a later law enshrined their special status." *Buffets*, 979 F.3d at 370 n.1 (citing Federal Courts Improvement Act of 2000, Pub. L. No. 106-518, § 501, 114 Stat. 2410, 2421–22 (2000)). As the Acting United States Trustee ("U.S. Trustee") conceded at oral argument, Alabama and North Carolina's refusal to participate in the Trustee Program is not based on any unique attributes of those states. They simply prefer to use Bankruptcy Administrators rather than Trustees. The two systems are, therefore, candidly and unapologetically nonuniform. And the quarterly fees that Chapter 11 debtors pay in the Trustee Program and the Bankruptcy Administrator system are also non-uniform.

The way in which the two systems impose quarterly fees relates to the ways the two systems are funded. The Trustee Program is funded primarily by fees from debtors. *Id.* at 371. Debtors in Chapter 11 cases pay fees based on quarterly "disbursements" that are made until their cases are "converted or dismissed."[1] 28 U.S.C. § 1930(a)(6). Initially, Chapter 11 debtors in Bankruptcy Administrator districts were not required to pay these substantial quarterly fees. *Buffets*, 979 F.3d at 371. Instead, the Bankruptcy Administrator system was funded by the judiciary's general budget. *Id.* at 371. That meant that, in Bankruptcy Administrator districts, ***171** funding from United States taxpayers was not offset by Chapter 11 quarterly fees. *See id.*

In 1994, the United States Court of Appeals for the Ninth Circuit, facing arguments much like those presented to us, ruled that the lack of quarterly fees in Bankruptcy Administrator districts violated the United States Constitution's Bankruptcy Clause, which "empowers Congress to enact 'uniform Laws on the subject of Bankruptcies throughout the United States.' " *See St. Angelo v. Victoria Farms, Inc.*, 38 F.3d 1525, 1529 (9th Cir. 1994) (quoting U.S. Const. art. I, § 8, cl. 4). The Court noted that "bankruptcy law[s] may have different effects in various states due to dissimilarities in state law as long as the federal law itself treats creditors and debtors alike." *Id.* at 1531. Because Chapter 11 debtors were only required to pay quarterly fees in districts participating in the Trustee Program, unsecured creditors in those districts received less money from debtors than they would have if the cases were filed in Alabama or North Carolina. *See id.* at 1531–32. Absent a justification for treating these debtors and creditors differently based solely on their geographic location, the Court ruled that the quarterly fee statute did "not apply uniformly to a defined class of debtors." *Id.* at 1532.

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After the *St. Angelo* decision, Congress enacted 28 U.S.C. § 1930(a)(7) which empowered "the Judicial Conference to set fees in [Bankruptcy] Administrator districts that were 'equal to those imposed' in Trustee districts." *Buffets*, 979 F.3d at 371. Critically, however, the amended quarterly fee statute was permissive as to Bankruptcy Administrator districts. It did not *require* equivalent fees. It merely allowed them. *See* 28 U.S.C. § 1930(a)(7) (2018) ("In districts that are not part of a United States trustee region ... the Judicial Conference of the United States *may require* the debtor in a [Chapter 11 case] to pay fees equal to those imposed [in Trustee Program districts] ...." (emphasis added)).[2] If the Judicial Conference elected to impose quarterly fees, those funds were required to be deposited into a fund to offset appropriations from the federal judiciary's general budget. *See* *Buffets*, 979 F.3d at 371 (citing 28 U.S.C. § 1931).

"The Judicial Conference soon exercised the authority Congress gave it, charging quarterly fees in Administrator districts in the amounts specified in 28 U.S.C. § 1930 ...." *Id.* (internal quotation marks omitted). This seemingly—at least in practice—eliminated the specific uniformity problem. That changed a few years ago, however, when bankruptcy filings declined and revenue from quarterly fees decreased. *Id.* With reduced fees, the Trustee Program was unable to make ends meet. *Id.* Thus, in response to its budgetary shortfall, Congress amended 28 U.S.C. § 1930(a)(6) to increase the quarterly fees in Chapter 11 cases. *Id.* Specifically, beginning January 1, 2018, Congress temporarily increased the quarterly fees for the largest Chapter 11 debtors, requiring debtors with quarterly disbursements "equal or exceed[ing] $1,000,000" to pay "the lesser of 1 percent of such disbursements or $250,000." 28 U.S.C. § 1930(a)(6)(B) (2018). This increase in quarterly fees applies "[d]uring each of fiscal years 2018 through 2022, if the balance in the United States Trustee System Fund as of September 30 of the most ***172** recent full fiscal year is less than $200,000,000 ...." *Id.*

Important here, "[m]any courts in Trustee districts applied the new fees to any quarterly disbursements that postdated the effective date of the 2017 Amendment, even if the bankruptcy case had been pending before the fee increase." *Buffets*, 979 F.3d at 372. This was a dramatic increase for large debtors. Prior to the amendment, debtors whose quarterly disbursements exceeded $30,000,000 were required to pay a $30,000 fee. 28 U.S.C. § 1930(a)(6) (2012). After the amendment, however, those debtors were required to pay a $250,000 fee—an increase of more than 800%. *See* 28 U.S.C. § 1930(a)(6)(B) (2018).

The Bankruptcy Administrator districts did not immediately follow suit and increase their fees. *Buffets*, 979 F.3d at 372. "The Judicial Conference waited until September 2018 to adopt the increased fee schedule." *Id.* But the nine-month delay was not the only difference under the two systems. In Bankruptcy Administrator districts, the significantly increased quarterly fees applied only in cases "filed on or after October 1, 2018." *Id.* (internal quotation marks omitted). This led to vastly disparate fees paid by similarly situated debtors in different districts.

II.

With that background in mind, I turn now to the facts here. In 2008, Circuit City Stores, Inc. and its affiliates ("Circuit City") filed for Chapter 11 bankruptcy protection in the Eastern District of Virginia, which participates in the United States Trustee Program. In September 2010, the bankruptcy court confirmed Circuit City's proposed liquidation plan (the "Liquidating Plan"). "The Liquidating Plan provided for the formation of the Liquidating Trust, overseen by the Liquidating Trustee, to collect, administer, distribute, and liquidate all of [Circuit City's] remaining assets." J.A. 365 (footnote omitted). The Liquidating Plan further required the Liquidating Trustee to "pay quarterly fees to the U.S. Trustee until the Chapter 11 Cases are closed or converted and/or the entry of final decrees." J.A. 110.

Circuit City's bankruptcy cases were pending as of January 1, 2018, when the increased quarterly fee schedule took effect. It was, therefore, required to pay the increased fees. And the increased fees were far from nominal. "In the seven years between entry of the order confirming the Liquidating Plan and the effective date of section 1930(a)(6)(B), the Liquidating Trust paid approximately $833,000 in quarterly fees." J.A. 371 (footnote omitted). "In the first three quarters of 2018 alone, the Liquidating Trust paid approximately $632,000." J.A. 371. Without the increased quarterly fees, Circuit City would have paid $56,400—a difference of

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approximately $575,600.[3]

Recognizing the potential uniformity issues, the Liquidating Trustee moved to determine the extent of its liability for post-confirmation quarterly fees. The Liquidating Trust raised three arguments: (1) the amended quarterly fee statute was impermissibly applied to cases pending prior to its enactment; (2) the amended quarterly fee statute was non-uniform in violation of the Bankruptcy Clause of the United States Constitution; and (3) the amended quarterly fee statute was non-uniform in ***173** violation of the uniformity requirement in the Taxing and Spending Clause of the United States Constitution.[4] The bankruptcy court rejected the Liquidating Trustee's retroactivity argument. However, it found that § 1930(a)(6)(B) violated both the Bankruptcy Clause and the uniformity provision of the Taxing and Spending Clause. I agree with the majority's decision on retroactivity and the uniformity provision of the Taxing and Spending Clause. But I would affirm the bankruptcy court's holding that § 1930(a)(6)(B) violates the Bankruptcy Clause.

Simply put, the imposition of quarterly fees in the two bankruptcy systems is not uniform. Many Chapter 11 debtors in Trustee Program districts pay more than similarly situated debtors in Bankruptcy Administrator districts. As a consequence, similarly situated creditors receive less in Trustee Program districts than in Bankruptcy Administrator districts. How then does the U.S. Trustee justify this obvious lack of uniformity? He offers three reasons that I address in turn.

A.

First, the U.S. Trustee argues that the Constitution's uniformity requirement only applies to substantive bankruptcy laws. To illustrate his point, the U.S. Trustee refers to 28 U.S.C. § 158(b)(1), which authorizes each circuit court to determine whether to establish a bankruptcy appellate panel, as a non-substantive bankruptcy law that is not uniformly implemented. Moreover, the U.S. Trustee argues that important aspects of bankruptcy practice—such as prescribing fees that an attorney or private trustee may charge and the waiver of certain fees for debtors or creditors—vary at the district level. He contends that those provisions are not substantive and, as a result, do not violate Article I, Section 8, Clause 4 of the Constitution. And he then argues that § 1930(a)(6)(B) likewise is not a substantive bankruptcy law and, thus, not constitutionally infirm.

However, there are several problems with this argument. Initially, the U.S. Trustee offers no precedent in support of his substantive versus non-substantive distinction. In fact, as the Fifth Circuit recognized, every bankruptcy court that has addressed this argument has rejected it. *See* *Buffets*, 979 F.3d at 377. This is hardly surprising since the Supreme Court has "defined 'bankruptcy' as the 'subject of the relations between an insolvent or nonpaying or fraudulent debtor and his creditors, extending to his and their relief.' " *Ry. Labor Execs. Ass'n v. Gibbons*, 455 U.S. 457, 466, 102 S.Ct. 1169, 71 L.Ed.2d 335 (1982) (quoting *Wright v. Union Central Life Ins. Co.*, 304 U.S. 502, 513–14, 58 S.Ct. 1025, 82 L.Ed. 1490 (1938)). The differences in § 1930(a)(6) and (a)(7) fit squarely within this definition.

What's more, there is a world of difference between the provisions cited by the U.S. Trustee and those at issue here. Of course, certain bankruptcy practices will vary at the local level. Bankruptcy courts must have the flexibility to operate in the most appropriate and efficient manner possible given their locality and staffing. But unlike various local rules or the existence of bankruptcy appellate panels, the disparate application of § 1930(a)(6)(B) regularly leads to similarly situated debtors paying *more* in fees and *less* to creditors in Trustee Program districts than they would in Bankruptcy Administrator ***174** districts. The bankruptcy court below provided a succinct example: "Had the Debtors filed their chapter 11 bankruptcy petitions a mere 140 miles south in Raleigh, North Carolina, the Debtors would be paying substantially lower quarterly fees than they are paying now." J.A. 376 (footnote omitted). Certainly, statutes that alter the amounts similarly situated creditors receive based on geography are sufficiently substantive to implicate the Bankruptcy Clause.

B.

The U.S. Trustee next argues that § 1930(a)(6)(B) is, in any event, uniform. He insists that § 1930(a)(7)

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"mandates that quarterly fees in bankruptcy-administrator districts be 'equal to those imposed by [section 1930(a)(6)].' " Appellant's Br. at 28 (quoting 28 § 1930(a)(7)). Not so. Section 1930(a)(7) states that, in Bankruptcy Administrator districts, "the Judicial Conference of the United States *may require* the debtor in a [Chapter 11 case] to pay fees equal to those imposed by [§ 1930(a)(6)]." 28 U.S.C. § 1930(a)(7) (2018) (emphasis added). If the operative version of § 1930(a)(7) used the word "shall" rather than "may," this would be an entirely different case.

Illustrating this point, on January 12, 2021, during the pendency of this appeal, President Donald J. Trump signed the Bankruptcy Administration Improvement Act of 2020, Pub. L. 116-325, 134 Stat. 5085 (2021). The Act fixed the uniformity problem by striking the word "may" from § 1930(a)(7) and inserting the word "shall." Pub. L. 116-325, 134 Stat. at 5088. The Act further noted that its purpose was to "confirm the longstanding intention of Congress that quarterly fee requirements remain consistent across all Federal judicial districts." *Id.* at 5086. The U.S. Trustee submitted a Rule 28(j) letter alerting the Court to this legislative change and arguing that the Act merely clarified, rather than changed § 1930(a)(7). I disagree. As is evident from the nine-month delay in implementing the increased quarterly fees, the unambiguous language of § 1930(a)(7) prior to the Act vested the Judicial Conference with discretion to assess increased quarterly fees. The Act constitutes a commendable congressional effort to remedy an unconstitutional statute. While that likely ameliorates the uniformity issue going forward, it does not eliminate the problem in the as-applied challenge before us.

That is so because the Act does not address the other critical difference between § 1930(a)(6) and (a)(7). Remember, in Bankruptcy Administrator districts, the increased quarterly fees only applied to cases filed after October 1, 2018. But in Trustee Program districts, the increased quarterly fees not only applied to disbursements in all cases filed after January 1, 2018, but also to all cases *pending* as of January 1, 2018. Therefore, because the increased quarterly fees in Trustee Program districts capture cases like this one—that was pending as of January 1, 2018—and the language of § 1930(a)(7) prior to enactment of the Act was discretionary as to Bankruptcy Administrator districts, the U.S. Trustee's argument that § 1930(a)(6)(B) and (a)(7) are actually uniform is at odds with reality.

C.

Finally, the U.S. Trustee claims that the differences in the Trustee Program and the Bankruptcy Administrator system are not geographically based. Instead, they are based on the unique budgetary challenges confronting Trustee Program districts. All Trustee Program districts, according to the U.S. Trustee, are treated uniformly, and, therefore, we should only inquire whether the increased fees apply with the ***175** same force and effect in the Trustee Program districts.

But this argument misses the forest for the trees. Justifying the differences here on the fact that the Trustee Program districts face the budgetary problems—the trees—ignores the fact that those districts only face the budgetary problems because Congress treated them differently in the first place—the forest. And Congress did that purely based on geography.

To be fair, statutes accounting for geographic differences are not automatically a problem. *See* *Blanchette v. Conn. Gen. Ins. Corps.*, 419 U.S. 102, 159, 95 S.Ct. 335, 42 L.Ed.2d 320 (1974) ("The uniformity provision does not deny Congress power to take into account differences that exist between different parts of the country, and to fashion legislation to resolve *geographically isolated* problems." (emphasis added)). But they are a problem if not aimed at addressing issues that are geographical in nature. Here, the quarterly fee statute does not "account [for] differences that exist between different parts of the country ...." *See* *id.* at 159, 95 S.Ct. 335. It is not a congressional attempt "to resolve geographically isolated problems." *See* *id.* Indeed, the difference in bankruptcy systems is arbitrary and financially damages unsecured creditors in every state other than Alabama and North Carolina.

In fact, a September 1992 report by the United States Government Accountability Office found no justification for having both the Bankruptcy Administrator and Trustee Programs. GAO Report at 16 ("We could not find any justification for continuing two separate programs."). Consistent with that, when faced with the question at oral argument whether there was anything geographically distinct about Alabama or North Carolina that justified a different approach in those states, the U.S. Trustee, to his credit, conceded there was not. While the uniformity

provision of the Bankruptcy Clause "was not intended to hobble Congress by forcing it into nationwide enactments to deal with conditions calling for remedy only in certain regions," *Blanchette*, 419 U.S. at 159, 95 S.Ct. 335 (internal quotation marks omitted), it is a necessary safeguard to prevent laws from arbitrarily damaging creditors and debtors as a result of regionalism. Accordingly, while the constitutionality of the two types of bankruptcy systems is not before the court, I would nonetheless hold that the amended quarterly fee statute, as applied to the Liquidating Trustee, violates the Bankruptcy Clause.

Words have meaning, and the words of the Bankruptcy Clause are clear. I do not reach my conclusion lightly, as I recognize that, "[i]n considering any constitutional attack on a federal statute, a court presumes that Congress has complied with the Constitution." *United States v. Comstock*, 627 F.3d 513, 518 (4th Cir. 2010). However, no matter how you slice it, uniform means not different. That was true when the Constitution was drafted, and it is still true today. Thus, for the reasons stated above, I would find that the amended quarterly fee statute is unconstitutionally non-uniform.

All Citations

996 F.3d 156, 70 Bankr.Ct.Dec. 38

III.

Footnotes

1 The U.S. Trustee and the Circuit City Trustee jointly sought permission to appeal from this court, pursuant to 28 U.S.C. § 158(d)(2)(A). That provision confers jurisdiction on a court of appeals to consider a direct appeal from a bankruptcy court, bypassing the district court, if the statutory conditions are satisfied.

2 The exclusion of Alabama and North Carolina from the Trustee program was intended to be temporary. More than twenty years later, however, Congress confirmed the special status of the six judicial districts in those two states as Bankruptcy Administrator districts. *See* Federal Courts Improvement Act of 2000, Pub. L. No. 106-518 § 501, 114 Stat. 2410, 2421-22 (2000).

3 As discussed further in footnote 10, in January 2021 — after this appeal was argued — Congress amended § 1930(a)(7) of Title 28, replacing the word "may" with the word "shall." *See infra* note 10.

4 The 2017 Amendment provision at issue in these appeals is codified in § 1930(a)(6)(B) of Title 28 and provides in pertinent part as follows:

> During each of fiscal years 2018 through 2022, if the balance in the United States Trustee System Fund as of September 30 of the most recent full fiscal year is less than $200,000,000, the quarterly fee payable for a quarter in which disbursements equal or exceed $1,000,000 shall be the lesser of 1 percent of such disbursements or $250,000.

See 28 U.S.C. § 1930(a)(6)(B). Congress specified that the 2017 Amendment "shall apply to quarterly fees payable under section 1930(a)(6) ... for disbursements made in any calendar quarter that begins on or after the date of enactment." *See* Bankruptcy Judgeship Act of 2017, Pub. L. No. 115-72, § 1004, 131 Stat. 1224, 1232 (2017).

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5 Citations herein to "J.A. ——" refer to the contents of the Joint Appendix filed by the parties in this appeal.

6 As explained more fully below, in November 2020, the Fifth Circuit reversed the February 2019 *Buffets* decision of the bankruptcy court. *See* *Matter of Buffets, L.L.C.*, 979 F.3d 366 (5th Cir. 2020).

7 In explaining his retroactivity contention, the Circuit City Trustee asserts, *inter alia*, that the 2017 Amendment's application to pending cases contravenes the Due Process Clause of the Fifth Amendment, in that it deprived bankruptcy debtors of fair notice.

8 The Bankruptcy Clause of the Constitution provides, in pertinent part, that Congress may "establish ... uniform Laws on the subject of Bankruptcies throughout the United States." *See* U.S. Const. art. I, § 8, cl. 4. The Uniformity Clause, on the other hand, relates only to taxation and empowers Congress to "lay and collect [t]axes ...; but all Duties, Imposts, and Excises shall be uniform throughout the United States." *See id.* at cl. 1.

9 At least ten bankruptcy courts have addressed the uniformity question that we assess today, and six of those courts have ruled in favor of constitutionality. *See* *In re John Q. Hammons Fall 2006, LLC*, 618 B.R. 519, 524-26 (Bankr. D. Kan. 2020) (reviewing uniformity question that we assess with respect to 2017 Amendment and ruling — as we do today — in favor of constitutionality); *In re MF Glob. Holdings Ltd.*, 615 B.R. 415, 446-48 (Bankr. S.D.N.Y. 2020) (same); *Point.360 v. Office of the U.S. Trustee*, No. 2:19-ap-01442 (Bankr. C.D. Cal. Mar. 31, 2021) (same); *In re Mosaic Mgmt. Grp., Inc.*, 614 B.R. 615, 623-25 (Bankr. S.D. Fla. 2020) (same); *In re Clayton Gen., Inc.*, No. 15-64266, 2020 Bankr. LEXIS 842 at *27 (Bankr. N.D. Ga. Mar. 30, 2020) (same); *In re Exide Techs.*, 611 B.R. 21, 36-38 (Bankr. D. Del. 2020) (same).

On the other hand, four bankruptcy courts have addressed the same uniformity question that we assess and ruled — as did the Bankruptcy Court in eastern Virginia — that the challenged 2017 Amendment is unconstitutional. *See* *In re Circuit City Stores, Inc.*, 606 B.R. 260, 269-70 (Bankr. E.D. Va. 2019) (addressing uniformity question and ruling that challenged 2017 Amendment is unconstitutional); *In re Life Partners Holdings, Inc.*, 606 B.R. 277, 286-88 (Bankr. N.D. Tex. 2019) (same); *In re Buffets, LLC*, 597 B.R. 588, 594-95 (Bankr. W.D. Tex. 2019) (same), *rev'd*, 979 F.3d 366 (5th Cir. 2020); *USA Sales, Inc. v. Office of the U.S. Trustee*, 2021 WL 1226369, at *17-18 (C.D. Cal. Apr. 1, 2021) (same).

10 The U.S. Trustee also contends on appeal that the combined application of § 1930(a)(6)(B) and 1930(a)(7) of Title 28 ensure that any quarterly fee increases would apply equally to all judicial districts. *See* Br. of Appellant 29-32. As such, the Trustee maintains, any discrepancy in impact would be merely a byproduct of implementation efforts, rather than unlawful congressional action. *Id.* Of possible relevance to this proposition, Congress amended § 1930(a)(7) of Title 28 and replaced the word "may" with the word "shall." Subsection (a)(7) now reads: "In districts that are not part of a United States trustee region ... the Judicial Conference of the United States shall require the debtor in a case under chapter 11 of title 11 to pay fees equal to those imposed by paragraph (6) of this

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subsection."

The U.S. Trustee promptly submitted to our panel a post-argument Local Rule 28(j) letter, pointing out this amendment but positing that it is merely a clarifying amendment that further confirms that Congress never gave the Judicial Conference discretion to charge unequal fees. The Liquidating Trustee failed to respond to the U.S. Trustee's Rule 28(j) letter and has not contested the proposition it espouses. Because we rule that the 2017 Amendment is constitutional, we need not further address this additional argument of the U.S. Trustee.

1 Logistically, the Trustee Program is funded by congressional appropriations; however, the appropriation is offset by fees paid into the United States Trustee System Fund. *See* 28 U.S.C. § 589a(b) (directing that various fees should be deposited into the United States Trustee System Fund to offset the congressional appropriation).

2 As noted below, Congress recently amended the language of 28 U.S.C. § 1930(a)(7) to require Bankruptcy Administrator districts to impose equivalent fees. Therefore, because this case involves a challenge to the imposition of quarterly fees prior to the recent amendment, all citations to § 1930(a)(7) refer to the version of the statute in effect prior to the amendment unless otherwise specified.

3 The quarterly fee figures offered by the United States Trustee appear to differ from the amounts referenced by the Liquidating Trustee and the bankruptcy court. Regardless of the specific amount, it is undisputed that the Liquidating Trustee paid exponentially higher quarterly fees in 2018 than it would have in a Bankruptcy Administrator district.

4 "The Congress shall have Power To lay and collect Taxes, Duties, Imposts, and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States." U.S. Const. art. I, § 8, cl. 1.

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Ninth Circuit Court of Appeals Cases

2 F.4th 1229
United States Court of Appeals, Ninth Circuit.

BANK OF NEW YORK MELLON, fka Bank of New York, AS TRUSTEE FOR the CERTIFICATEHOLDERS OF CWALT, INC., ALTERNATIVE LOAN TRUST 2005-54CB, MORTGAGE PASS-THROUGH CERTIFICATES SERIES 2005-54CB, Plaintiff-Appellant,
v.
ENCHANTMENT AT SUNSET BAY CONDOMINIUM ASSOCIATION; 732 Hardy Way Trust, Defendants-Appellees,
and
Harold Hill; Nevada Association Services, Inc., Defendants.

No. 19-17048
|
Argued and Submitted November 17, 2020
Pasadena, California
|
Filed June 25, 2021

Synopsis
Background: Lender's assignee, as holder of first deed of trust on borrower's condominium, filed suit in diversity against homeowners association (HOA) and purchaser of condominium at HOA's nonjudicial foreclosure of its lien, seeking to quiet title and for declaratory judgment that foreclosure while automatic stay triggered by borrower's filing of chapter 13 bankruptcy petition was in effect was void. The United States District Court for the District of Nevada, Richard F. Boulware II, J., granted purchaser's motion for summary judgment, 2019 WL 4781838, and assignee appealed.

Holdings: The Court of Appeals, VanDyke, Circuit Judge, held that:

[1] assignee had prudential standing to sue, under Nevada law, and

[2] assignee's interest in condominium was superior to that of purchaser, regardless of purchaser's purported status as bona fide purchaser.

Reversed and remanded.

VanDyke, Circuit Judge, filed concurring opinion.

Forrest, Circuit Judge, filed dissenting opinion.

Procedural Posture(s): On Appeal; Motion for Summary Judgment.

West Headnotes (7)

[1] **Federal Courts** Summary judgment

The Court of Appeals reviews de novo a district court's decision on cross-motions for summary judgment.

[2] **Federal Courts** Summary judgment

On appeal from the district court's ruling on summary judgment, when no material facts are disputed, the Court of Appeals asks only whether the district court correctly applied the relevant substantive law.

[3] **Declaratory Judgment** Subjects of relief in general
Quieting Title Persons entitled to relief

Lender's assignee, as holder of first deed of trust on condominium, had prudential standing to sue homeowners association (HOA) and purchaser of condominium at foreclosure to quiet title and for declaratory judgment that HOA's nonjudicial foreclosure of its lien while automatic stay was in effect during borrower's chapter 13 bankruptcy was void; action in diversity was brought under Nevada statute that allowed suit by "any person against another who claims an estate or interest in real property, adverse to the person bringing the action, for the purpose of determining such adverse claim," and thus

assignee's interest in condominium fell within statute's zone of interests. Nev. Rev. St. § 40.010.

[4] **Federal Civil Procedure**In general; injury or interest

Whether a plaintiff's claims are within a statute's zone of interests is not a jurisdictional question, for the purposes of determining whether a plaintiff has prudential standing; indeed, whether a plaintiff comes within the zone of interests is an issue that requires the court to determine, using traditional tools of statutory interpretation, whether a legislatively conferred cause of action encompasses a particular plaintiff's claim.

[5] **Bankruptcy**Validity of acts in violation of injunction or stay
Common Interest Communities Lien foreclosure; other remedies and proceedings for nonpayment

Under Nevada law, homeowners association's (HOA) nonjudicial foreclosure of its lien while automatic stay was in effect during borrower's chapter 13 bankruptcy was void, and thus interest of lender's assignee, as holder of first deed of trust on condominium, was superior to that of purchaser of condominium at foreclosure sale, regardless of purchaser's purported status as bona fide purchaser; borrower listed condominium in bankruptcy schedules, and HOA did not obtain relief from automatic stay before condominium was sold.

[6] **Bankruptcy**Validity of acts in violation of injunction or stay

Under Nevada law, where a property is listed in a relevant bankruptcy schedule and sold via foreclosure during the bankruptcy proceedings without the creditor having obtained relief from the automatic stay, such a sale is void, and the purchase of the property at the sale is without effect.

1 Cases that cite this headnote

[7] **Liens**Foreclosure and sale without action

Under Nevada law, a party's status as a bona fide purchaser is irrelevant when a defect in the foreclosure proceeding renders the foreclosure sale void.

***1230** Appeal from the United States District Court for the District of Nevada, Richard F. Boulware II, District Judge, Presiding, D.C. No. 2:17-cv-01916-RFB-EJY

Attorneys and Law Firms

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Before: Johnnie B. Rawlinson, Danielle J. Forrest, and Lawrence VanDyke, Circuit Judges.

Concurrence by Judge VanDyke;

Dissent by Judge Forrest

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OPINION

VANDYKE, Circuit Judge:

In this case, we are again presented with the effect of a foreclosure of a superpriority lien granted to a homeowners' association (HOA) under Nevada Revised Statute 116.3116.[1] As a consequence of the late-2000's financial crisis and its effect on Nevada homeowners, our court has seen many cases involving Nevada's HOA superpriority lien statute. But this case involves a unique wrinkle that we have not yet addressed. We must decide whether the Bank of New York Mellon (Bank), as the first deed of trust lienholder, may set aside a completed superpriority lien foreclosure sale on the grounds that the sale occurred in violation of the automatic stay in bankruptcy proceedings. *See* 11 U.S.C. § 362(a). Because the Bank has standing under Nevada's quiet title statute, Nevada Revised Statute 40.010, and established case authority confirms that any HOA foreclosure sale made in violation of the bankruptcy stay—like the foreclosure sale here—is void, not merely voidable, ***1231** *Schwartz v. United States (In re Schwartz)*, 954 F.2d 569, 571–72 (9th Cir. 1992), we conclude that the Bank may raise the HOA's violation of the automatic stay provision, and that the Bank has superior title.[2]

I. BACKGROUND

This dispute involves the property at 732 Hardy Way in Mesquite, Nevada (Property), located in the Enchantment at Sunset Bay Condominium Association (HOA), and subject to the HOA's Declaration of Covenants, Conditions, and Restrictions, recorded in 2003. In 2005, Harold Hill purchased the Property with a $185,400 loan that was assigned to the Bank in 2013. In January 2014, Hill fell behind in his HOA dues, and the HOA recorded a Notice of Delinquent Assessment Lien. The next month, the HOA recorded a Notice of Default and Election to Sell and informed Hill that he needed to pay $3,130.56 or his home would be sold. By April 2014, Hill had filed for Chapter 13 bankruptcy and stated in his bankruptcy plan that he was surrendering the Property to the Bank and the HOA. An automatic bankruptcy stay went into effect, staying "any act to ... enforce any lien against property of the estate." 11 U.S.C. § 362(a)(4).

While Hill's bankruptcy case was still pending, the HOA recorded a Notice of Foreclosure Sale on July 15, 2014, and several weeks later sold the Property to 732 Hardy Way Trust (Trust) for $6,072.29 at a nonjudicial foreclosure sale.[3] The Bank subsequently initiated this litigation, in which it (1) sued the HOA and the Trust to quiet title and for declaratory relief on the basis that the foreclosure sale was void and therefore did not extinguish the Bank's first deed of trust; (2) sought a preliminary injunction to prevent the Trust from selling or transferring the Property; and (3) requested an order declaring that the Bank could foreclose on its deed of trust. The Bank also sued the HOA for breach of Nevada Revised Statute 116.1113 and wrongful foreclosure.[4]

The Bank and the Trust each moved for summary judgment. The Trust argued it had superior title because the HOA foreclosure sale extinguished the Bank's deed of trust. Conversely, the Bank argued that the HOA foreclosure sale did not extinguish its lien because, inter alia, the sale violated the automatic bankruptcy stay and was thus void under Nevada and Ninth Circuit precedent, or alternatively, Nevada's HOA foreclosure statute violated due process. The district court granted summary judgment in favor of the Trust and dismissed the remaining claims against the HOA, holding simply "that the foreclosure sale extinguished the [Bank's] deed of trust on the [P]roperty and that [the Trust] purchased the property free and clear of the deed of trust." The Bank timely appealed, and we have jurisdiction pursuant to 28 U.S.C. § 1291.

II. DISCUSSION

[1] [2]"We review de novo 'the district court's decision on cross-motions for summary judgment.' " *BNSF Ry. Co. v. Or. Dep't of Revenue*, 965 F.3d 681, 685 (9th Cir. 2020) (citation omitted). "Here, ... no material facts are disputed, so we 'ask only ***1232** whether the district court correctly applied the relevant substantive law.' " *Id.* (citation omitted).

A. The Bank Has Standing to Raise the Violation of the Automatic Bankruptcy Stay.

[3]The district court concluded that under *Tilley v. Vucurevich (In re Pecan Groves)*, 951 F.2d 242, 245 (9th

Cir. 1991), the Bank lacked standing to challenge any violation of the automatic stay because it "was neither a party, a debtor, or a trustee in [the underlying] bankruptcy matter." The Bank argues that the district court misapplied *In re Pecan Groves* and incorrectly used that bankruptcy case to prevent the Bank from raising the voidness of the foreclosure sale in this diversity action in federal court. We agree that the district court indeed erred because the Bank had standing to make the argument that the HOA foreclosure sale occurred in violation of the bankruptcy stay and was thus void.

[4]The parties do not dispute that the Bank has Article III standing, as the alleged extinguishment of the Bank's first deed of trust can be fairly traced to the HOA's violation of the bankruptcy stay. *See* *Spokeo, Inc. v. Robins*, —— U.S. ——, 136 S. Ct. 1540, 1547, 194 L.Ed.2d 635 (2016). Instead, the Trust argues that the Bank does not have prudential standing such that the Bank's grievance "fall[s] within the zone of interests protected or regulated by the statutory provision ... invoked in the suit." *Bennett v. Spear*, 520 U.S. 154, 162, 117 S.Ct. 1154, 137 L.Ed.2d 281 (1997).[5]

We disagree. The Bank here brought its quiet title claim under Nevada Revised Statute 40.010, which allows suit "by any person against another who claims an estate or interest in real property, adverse to the person bringing the action, for the purpose of determining such adverse claim." Such a broad statement clearly "grants the [Bank] the cause of action that [it] asserts"—a declaration of its interest in the subject Property vis-à-vis the Trust's interest—such that the Bank satisfies the zone-of-interests test for prudential standing purposes. *Bank of Am. Corp. v. City of Miami*, —— U.S. ——, 137 S. Ct. 1296, 1302, 197 L.Ed.2d 678 (2017).

Although we held in *In re Pecan Groves* that "a creditor has no independent standing to appeal an adverse decision regarding a violation of the automatic stay," the Bank's quiet title action does not implicate this ruling. *In re Pecan Groves*, 951 F.2d at 245. In that case, we addressed whether a creditor had standing to appeal a bankruptcy order and reasoned that as "the trustee ha[d] not appealed the adverse ruling ... [n]o other party [could] challenge this ruling." *Id.* We did not consider whether a creditor was precluded from advancing a quiet title action premised on violation of the automatic stay, particularly in a diversity case where state law recognizes such a claim as a basis for voiding a foreclosure sale.

***1233** In contrast to the facts and procedural posture of *In re Pecan Groves*, the Bank brought this quiet title diversity action pursuant to Nevada precedent invalidating HOA foreclosure sales when the HOA has violated the automatic stay. *LN Mgmt. LLC Series 5105 Portraits Place v. Green Tree Loan Servicing, LLC (Portraits Place)*, 133 Nev. 394, 399 P.3d 359, 360–61 (2017) (recognizing that "the HOA foreclosure sale was an act in violation of the automatic stay, despite the lack of notice of the homeowners' bankruptcy," and that the sale was "invalidated"). When adjudicating various types of state law disputes, Nevada courts consistently consider the voidness of actions taken in violation of a federal bankruptcy stay. *See* *SFR Investments Pool 1, LLC v. U.S. Bank, N.A.*, 135 Nev. 346, 449 P.3d 461, 465 (2019) (en banc) (holding that "it was proper of the district court to consider the stay in balancing the equities, as the court must consider all of the circumstances surrounding the sale" because "[t]he fact that the sale was in violation of a bankruptcy stay at the time the sale was held may be relevant to U.S. Bank's failure to act and the sale price," and "it would be reasonable for a lender not to attend a foreclosure sale if it believe[d] that the sale [was] being conducted in violation of a bankruptcy stay"); *Gundala v. BAC Home Loans Servicing, LP*, 483 P.3d 1121, 2021 WL 1531154, at *1 (Nev. 2021) (unpublished) (concluding that "the HOA recorded a Notice of Delinquent Assessment in March 2011 and a Notice of Default in June 2011, both of which were recorded while the automatic stay was in effect," and "[b]ecause the abovementioned notices were both recorded while the automatic stay was in effect, the district court correctly determined that they were void and that the ensuing HOA foreclosure sale was also void"); *NV Eagles, LLC v. Nationstar Mortg., LLC*, 462 P.3d 1230, 2020 WL 2527389, at *1 (Nev. 2020) (unpublished) (opining that "[a]lthough appellant contends that the sale did not violate the automatic stay because the debtor had been personally discharged before the sale, the subject property was still part of the bankruptcy estate at the time of the sale and therefore was still subject to the automatic stay," and that "the [state] district court correctly determined that the HOA's foreclosure sale was invalid because it violated the automatic bankruptcy stay"); *CitiMortgage, Inc. v. Corte Madera Homeowners Ass'n*, 962 F.3d 1103, 1110 (9th Cir. 2020) (recognizing in a quiet title action that "generally, the filing of bankruptcy will stay all proceedings relating to a foreclosure sale," and that, under Nevada law, the filing of notices related to foreclosure may violate the automatic stay) (citation and alteration omitted).

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B. Any HOA Foreclosure Sale in Violation of the Automatic Bankruptcy Stay is Void under Nevada Law.

[5]To prevail on its claim, the Bank must prove that its interest in the Property is superior to the Trust's interest. *Chapman v. Deutsche Bank Nat'l Tr. Co.*, 129 Nev. 314, 302 P.3d 1103, 1106 (2013) (en banc). In this case, the Bank's interest is superior to the Trust's interest because under Nevada precedent, an HOA foreclosure "sale conducted during an automatic stay in bankruptcy proceedings is invalid." *Portraits Place*, 399 P.3d at 359–60.

[6] [7]Here, the Bank provided evidence showing that: (1) Hill listed the Property in his bankruptcy schedules in March 2014; (2) the automatic bankruptcy stay was active through 2017; and (3) the Property was auctioned off on September 19, 2014.[6] As the Nevada Supreme Court ***1234** concluded in *Portraits Place*, where the property is "listed ... in the[ ] relevant bankruptcy schedule" and sold "[d]uring the bankruptcy proceedings ... without seeking relief from the automatic stay," such a "sale was void." *Id.* The "purchase of the property at the [foreclosure] sale was without effect." *40235 Wash. St. Corp. v. Lusardi*, 329 F.3d 1076, 1080 (9th Cir. 2003).[7] Therefore, the Bank should receive quiet title to the Property under Nevada Revised Statute 40.010.

The dissent's assertion that our decision relies on federal bankruptcy code as the substantive rule of decision in this case misconstrues our rationale. A violation of federal law can have independent consequences under state law. And when that happens, it is not entirely accurate to characterize those consequences as "sole[ly]" a matter of federal, not state, substantive law. Instead, the substantive rule of decision depends on how *state law* treats the federal violation. A helpful analogy might be driving in Nevada with an expired Oregon driver's license. Whether the license is expired or not will be controlled by Oregon law. But the *consequences* of driving on that expired license in Nevada will be controlled by Nevada law. Similarly, here, the factual voidness of the Property's transfer is a result of federal bankruptcy law. But the consequences of such a void transaction for purposes of a Nevada quiet title action are controlled by Nevada's property laws.[8] Nevada courts may determine that violations of federal bankruptcy laws—particularly violations that result in "void" transactions—have state law consequences for Nevada property, which was exactly what the Nevada Supreme Court did in *Portraits Place*. 399 P.3d at 360 (concluding in a Nevada quiet title action that because "the HOA foreclosure sale was an act in violation of the automatic stay ... the violation of the automatic stay invalidated the HOA foreclosure sale").

III. CONCLUSION

The district court erred in holding that the Bank lacked standing to pursue its quiet title claim in federal court. Because the Bank has standing, its interest as a creditor is protected under Nevada law, and the HOA foreclosure sale in violation of the bankruptcy stay was void, applicable precedent compels us to conclude that the Bank has superior title. For these reasons, we reverse the district court's grant of summary judgment in favor of the Trust, its denial of summary judgment to the Bank, and its dismissal of the Bank's claims against the HOA, and remand for proceedings consistent with this opinion.

REVERSED AND REMANDED.

VANDYKE, Circuit Judge, concurring:

I write separately to explain further why I think Judge Forrest's thoughtful analysis in her dissent is nonetheless incorrect. Stepping back from our doctrinal differences for a moment, there is something peculiar about the dissent's conclusion that, yes, the HOA foreclosure sale at issue in this case was void as a matter of federal bankruptcy law, but Nevada property law must turn a blind eye to that fact. That approach would force Nevada to ignore a reality that our own court has recognized again and again: that violations of ***1235** a bankruptcy stay are void, not merely voidable.[1]

I think the dissent's counterintuitive conclusion is a result of trying to reconcile the irreconcilable. Underlying the dissent's analysis is the concept that the factual voidness of the foreclosure sale here may only be raised in this state-law action by certain entities—meaning, the sale is only void as to *certain* entities if they so choose. But that is what is usually meant when we say a transaction is "voidable, not void." If only the "debtor [may] affirmatively challenge creditor violations of the stay," for example, then such violations "are merely voidable," not void. *Schwartz v. United States (In re Schwartz)*, 954 F.2d 569, 571 (9th Cir. 1992). Ultimately, the dissent cannot escape its reliance on a "voidable, not void" rationale—one that is directly at odds with our circuit's clear authority recognizing that violations of a bankruptcy

stay are, in fact, "void," not voidable. *Id.* at 575.

This fundamental contradiction is not by accident. It is a necessary consequence of the dissent's commendable but nevertheless doomed attempt to apply our circuit's caselaw about prudential standing in bankruptcy proceedings to this non-bankruptcy case applying Nevada property law in a diversity action. The first problem with this attempt is addressed by the majority opinion—that prudential standing in bankruptcy proceedings and Nevada property law are just two different things, and the dissent is improperly trying to mix apples and oranges. But this problem is exacerbated by something else—the fact that our circuit's caselaw about prudential standing in bankruptcy proceedings historically grew out of a "voidable, not void" rationale, which our circuit has since repeatedly rejected. It should come as no surprise, then, that when the dissent (improperly) attempts to transpose our bankruptcy prudential standing jurisprudence onto this case, it ends up right back where that jurisprudence started—with a voidable, not void, rationale. And as a corollary to that error, the dissent is forced to mistakenly argue that a creditor such as the Bank "falls outside the zone of interests protected by the automatic stay," when both the Supreme Court and our court have said otherwise.

1. Towards the end of the dissent, it acknowledges that in our circuit's caselaw a foreclosure sale in violation of the bankruptcy stay is void, and not merely voidable. But the dissent interprets void to mean void *only as to certain entities*—those related to the debtor's estate—meaning that in the absence of an active debtor, creditors may not challenge "void" transactions. This is just redefining "void, not voidable" as "voidable, not void." It also ignores the fact that we have consistently reapplied *In re Schwartz* to affirm that any violations of the automatic stay provision are indeed void—full stop. *See Burton v. Infinity Capital Mgmt.*, 862 F.3d 740, 747 (9th Cir. 2017) (judicial interference); *In re Dyer*, 322 F.3d 1178, 1188 (9th Cir. 2003) (attempt to record deed of trust); *40235 Wash. St. Corp. v. Lusardi*, 329 F.3d 1076, 1080 (9th Cir. 2003) (tax sale). Nor are we the only court to hold this view. *See In re Myers*, 491 F.3d 120, 127 (3d Cir. 2007) ("We have indeed held that actions taken in violation of the stay are void."); *United States v. White*, 466 F.3d 1241, 1244 (11th Cir. 2006) ("It is the ***1236** law of this Circuit that '[a]ctions taken in violation of the automatic stay are void and without effect.' " (citation omitted)); *Mann v. Chase Manhattan Mortg. Corp.*, 316 F.3d 1, 3 (1st Cir. 2003) ("acts undertaken in violation of the automatic stay are ... void"); *In re Colonial Realty Co.*, 980 F.2d 125, 137 (2d Cir. 1992) ("[S]o central is the § 362 stay to an orderly bankruptcy process that actions taken in violation of the stay are void and without effect." (quotation marks and citation omitted)); *Ellis v. Consol. Diesel Elec. Corp.*, 894 F.2d 371, 372 (10th Cir. 1990) ("It is well established that any action taken in violation of the stay is void and without effect.").[2]

If a transaction is void, it is null—it is as if it never existed.[3] On the other hand, if a transaction is voidable, it may still be enforced by some entities, but not others. The dissent essentially redefines "void" to mean "void from the perspective of certain entities, but not others." But that is what everyone else means when they say a transaction is merely voidable.[4]

2. The dissent's conclusions that transactions in violation of the bankruptcy stay are only void as to certain debtors and creditors is understandable given the cases on which the dissent relies—not because "void" has ever been understood to mean "only void for some entities," but because the older bankruptcy standing cases the dissent cites were either directly or indirectly based on the now-rejected rationale that such transactions were merely *voidable*, not void. For example, the dissent applies *Magnoni v. Globe Inv. & Loan Co., Inc. (In re Globe)*, 867 F.2d 556, 560 (9th Cir. 1989), which reached its conclusion that Bankruptcy Code "section 362 ... does not confer any rights to outside parties" by citing to *In re Brooks*, 79 B.R. 479 (B.A.P. 9th Cir. 1987). The dissent also cites to *Tilley v. Vucurevich (In re Pecan Groves)*, which similarly relied on *In re Brooks* to conclude that only "the trustee ... [may] seek to enforce the protections of the automatic stay." 951 F.2d 242, 245 (9th Cir. 1991). The *In re Brooks* decision, in turn, rested on two key assertions, that (1) "a transfer made in violation of the stay *may be voidable* at the trustee's discretion," rather than simply void, *id.* at 480 (emphasis added), and (2) the automatic bankruptcy stay benefits only the debtor, and "[o]ther parties affected ... [have] no substantive or procedural rights," *id.* at 481.[5]

Both of these determinations are inconsistent with our more recent bankruptcy jurisprudence.[6] *In re Schwartz* clarified ***1237** that such transfers are actually void, not merely voidable. 954 F.2d at 571–72. And the Supreme Court has explicitly stated that, irrespective of whether claims are made against the debtor's estate, "[t]he automatic stay ... benefits creditors *as a group* by

preventing individual creditors from pursuing their own interests *to the detriment of the others*." *City of Chicago v. Fulton*, —— U.S. ——, 141 S. Ct. 585, 589, 208 L.Ed.2d 384 (2021) (emphasis added). Our court has said the same thing in the years since *In re Globe*. *See* *In re Mwangi*, 764 F.3d 1168, 1173 (9th Cir. 2014) ("The stay [thus] protects the debtor ... and also protects creditors as a class from the possibility that one creditor will obtain payment on its claims to the detriment of all others." (citation omitted)); *In re Sherman*, 491 F.3d 948, 971 (9th Cir. 2007) (citing H.R. Rep. No. 95–595, at 340 (1977) to "observ[e] that another purpose of the automatic stay is to protect creditors by providing 'an orderly liquidation procedure under which all creditors are treated equally' "); *In re Dawson*, 390 F.3d 1139, 1147 (9th Cir. 2004), *abrogated on other grounds by In re Gugliuzza*, 852 F.3d 884 (9th Cir. 2017) (citing H.R. Rep. No. 95–595, at 340 (1977) to note "[t]he automatic stay also provides creditor protection. Without it, certain creditors would be able to pursue their own remedies against the debtor's property"); *United States v. Dos Cabezas Corp.*, 995 F.2d 1486, 1491 (9th Cir. 1993) ("The purpose of the automatic stay provision is two-fold. By halting all collection efforts, '[i]t gives the debtor "a breathing spell" ' .... By preventing creditors from pursuing to the detriment of others, their own remedies against the debtors' property *the stay protects creditors*." (emphasis added) (citation omitted)); *cf.* *Matter of Ring*, 178 B.R. 570, 577–81 (Bankr. S.D. Ga. 1995) (observing that "[c]learly, creditors do benefit from the automatic stay" such that "it creates a facially anomalous result [if] ... a creditor who is adversely affected by [a stay violation] nevertheless is without standing" in bankruptcy proceedings and concluding that, contrary to Ninth Circuit precedent arising from *In re Brooks*, "a holder of a lien in property ... has standing to seek a declaratory judgment that such transfer is void *ab initio*" before the bankruptcy court).

Given this precedent, the dissent's assertion that "the automatic stay does not protect individual creditors when pursuing claims that are adverse or unrelated to the debtor's estate" is not an accurate reflection of our circuit's (or the Supreme Court's) precedent generally. It is admittedly accurate (albeit wrong) only within the narrow context of our caselaw governing *prudential standing in a bankruptcy proceeding*. It is not accurate more broadly. Because the principles underlying *In re Globe*'s and *In re Pecan Groves*'s conclusions in the bankruptcy proceeding context are clearly outdated and inconsistent with our more recent precedent, I would not extend their prudential standing rationale to control what types of arguments can be raised with respect to a Nevada state-law property claim (e.g., factual voidness). Our bankruptcy proceeding jurisprudence is internally inconsistent. I see no reason to extend the *outdated* side of that inconsistency to effectively censor a party from ***1238** presenting a factually-true argument in the context of its state-law claim outside of a bankruptcy proceeding.

The majority's decision awarding quiet title to the Bank because the foreclosure sale in violation of the bankruptcy stay was void does not, contrary to the dissent, undermine the protections of the bankruptcy stay or the trustee's role in protecting the estate. Quite the opposite, it achieves one of the objectives of the stay noted even by the dissent: by allowing other creditors to point out that a creditor's sale violated the stay and is therefore void, it reduces the incentive for creditors to "rac[e] to various courthouses to pursue independent remedies to drain the debtor's assets." *Dean v. Trans World Airlines, Inc.*, 72 F.3d 754, 755–56 (9th Cir. 1995). Contrary to the dissent, recognizing the voidness of this transaction in a Nevada quiet title action in no way "seeks to use the stay in a manner contrary to its purposes."[7]

Boiled down to their essentials, the difference between the majority and the dissent in this case reduces to whether a transaction in violation of a bankruptcy stay is void, or merely voidable. Our precedent clearly says it is void—like it never happened. Our outdated bankruptcy standing jurisprudence may, until it is corrected, improperly require us to ignore that glaring fact in some circumstances in federal bankruptcy proceedings. But there is no reason Nevada property law must duplicate that error.

FORREST, Circuit Judge, dissenting:

The majority holds that a first deed of trust lienholder—here, Bank of New York Mellon (Bank)—can set aside a completed foreclosure sale through a state-law quiet-title action on the grounds that the foreclosure violated the automatic bankruptcy stay provided for under the Bankruptcy Code. I respectfully dissent because, in seeking this relief, the Bank is not acting as a "creditor" within the meaning of the Bankruptcy Code and, therefore, is not entitled to enforce the automatic stay or seek relief based on a violation of the stay.

I. Standing

As a threshold matter, I agree with the majority that the district court erred in holding that the Bank lacked standing to bring its quiet-title claim. Standing doctrine (both constitutional and prudential) presents a threshold question of justiciability—i.e., is the plaintiff "entitled to have the court decide the merits of the dispute[?]" *Warth v. Seldin*, 422 U.S. 490, 498, 95 S.Ct. 2197, 45 L.Ed.2d 343 (1975). Constitutional standing considers whether a federal court has the power to adjudicate a case, *Lexmark Int'l, Inc. v. Static Control Components, Inc.*, 572 U.S. 118, 128 n.4, 134 S.Ct. 1377, 188 L.Ed.2d 392 (2014), and prudential standing concerns "judicially self-imposed limits on the exercise of federal jurisdiction," *Bennett v. Spear*, 520 U.S. 154, 162, 117 S.Ct. 1154, 137 L.Ed.2d 281 (1997) (citation omitted). The parties here dispute only whether the Bank has prudential standing to challenge the foreclosure sale.[1]

***1239** There is no reason to impose prudential limitations on our jurisdiction in the instant case. The Bank brings its quiet-title claim under Nevada Revised Statute 40.010, which allows suit "by any person against another who claims an estate or interest in real property, adverse to the person bringing the action, for the purpose of determining such adverse claim."[2] Thus, Nevada's quiet-title statute "grants the [Bank] the cause of action that [it] asserts," *Bank of Am. Corp. v. City of Miami*, —— U.S. ——, 137 S. Ct. 1296, 1302, 197 L.Ed.2d 678 (2017), and the Bank may pursue its claim in a federal court sitting in diversity. That is not the end of the story, however.

II. Automatic Bankruptcy Stay

To prevail on its quiet-title claim, the Bank must prove that its interest in the subject property is superior to the interests of the foreclosure purchaser, 732 Hardy Way Trust (Trust). *Chapman v. Deutsche Bank Nat'l Tr. Co.*, 129 Nev. 314, 302 P.3d 1103, 1106 (2013) (en banc). The rule of decision for determining where superior title lies does not arise from Nevada's quiet-title statute; the quiet-title statute merely provides a *procedural* mechanism for resolving competing title claims and does not confer any *substantive* rights to real property. *See* Nev. Rev. Stat. 40.010; *Chapman*, 302 P.3d at 1106 ("A plea to quiet title does not require any particular elements, but each party must plead and prove his or her own claim to the property in question ....") (internal quotation marks and citation omitted). The substantive rules of decision for a quiet-title claim must arise from another source.

Here, the sole substantive rule on which the Bank relies is Section 362(a) of the Bankruptcy Code—the automatic bankruptcy stay. But this claim is viable only if the Bank falls within the "particular class of persons [who] has a right to sue under this substantive statute." *Lexmark*, 572 U.S. at 127, 134 S.Ct. 1377 (alteration and citation omitted). To determine if the Bank can seek relief based on the automatic bankruptcy stay, we must look to the Bankruptcy Code. *See* *40235 Wash. St. Corp. v. Lusardi*, 329 F.3d 1076, 1079–80 (9th Cir. 2003).

The commencement of a bankruptcy case creates a bankruptcy estate comprised of the debtor's property interests. 11 U.S.C. § 541(a). That property is used to pay creditors' allowed claims in a process facilitated by a bankruptcy trustee who represents the estate and "acts as a fiduciary for the debtor's creditors." *Hillis Motors, Inc. v. Haw. Auto. Dealers' Ass'n*, 997 F.2d 581, 585 (9th Cir. 1993) (citing 11 U.S.C. § 323(a)). Bankruptcy is, at bottom, "a distribution system; it distributes property from the debtor to creditors so that creditors can apply such payments to the debtor's debts." 1 Collier on Bankruptcy ¶ 1.03 (16th ed. 2021). Creditors play a distinct and limited role in this system: they assert claims *for distribution from the debtor's estate*. *See* 11 U.S.C. § 101(10)(A), (B) (defining "creditor" as an "entity that has a [right to payment] ***1240** against the debtor" or "against the estate"); *id.* § 101(5) (defining "claim").

It is well-established that Section 362(a)'s automatic stay provision protects debtors by providing "breathing space" from creditor harassment, *Burton v. Infinity Cap. Mgmt.*, 862 F.3d 740, 746 (9th Cir. 2017), and an opportunity for a fresh start at the conclusion of a successful bankruptcy process, *Schwartz v. United States (In re Schwartz)*, 954 F.2d 569, 571 (9th Cir. 1992); *see also* *Burkart v. Coleman (In re Tippett)*, 542 F.3d 684, 691 (9th Cir. 2008). But that is not its only purpose. The stay also protects creditors' interests in the debtor's estate. *See, e.g.*, *Treasurer of Snohomish Cnty. v. Seattle-First Nat'l Bank (In re Glasply Marine Indus., Inc.)*, 971 F.2d 391, 394 (9th Cir. 1992) ("Congress designed the automatic stay to protect the

relative position of all creditors."). That is, the automatic stay protects a creditor's ability to collect a fair return on its debt relative to the claims of other creditors *by preserving the debtor's estate*. This makes sense because without the automatic stay, creditors could "rac[e] to various courthouses to pursue independent remedies to drain the debtor's assets." *Dean v. Trans World Airlines, Inc.*, 72 F.3d 754, 755–56 (9th Cir. 1995). By prohibiting such disorderly depletion, the automatic stay protects "creditors as a class from the possibility that one creditor will obtain payment on its claims to the detriment of all others." *Hillis*, 997 F.2d at 585; *see also* *City of Chicago v. Fulton*, —— U.S. ——, 141 S. Ct. 585, 589, 208 L.Ed.2d 384 (2021) (explaining the automatic stay protects creditors "*as a group* by preventing individual creditors from pursuing their own interests *to the detriment of the others*") (emphases added).

But, important for this case, the automatic stay does not protect litigants pursuing claims that are adverse or unrelated to the distribution of the debtor's estate. This is clear from our decision in *Magnoni v. Globe Investment & Loan Co., Inc. (In re Globe)*, 867 F.2d 556, 558–60 (9th Cir. 1989), where several parties who co-owned real property with the debtor sought to set aside the foreclosure of the debtor's interest in the co-owned property as violative of the automatic stay. The co-owners were "creditors" of the debtor because they had filed proofs of claim in the debtor's bankruptcy case. *Id.* at 558 & n.4. Nonetheless, we held that they could not invoke protection from the automatic stay because they had "not pursued [their] action as [the debtor's] creditors, but rather as owners of the ... property." *Id.* at 559. Setting aside the sale would not have benefitted the debtor's estate because the estate had received a cash payment for the value of the debtor's interest in the subject property. *Id.* at 558. In such circumstances, the co-owners were acting not as "creditors" seeking to recover from the bankruptcy estate but instead as "aggrieved property owners with interests adverse to the estate." *Id.* at 560. And we held that the automatic stay "does not confer any rights" on parties in this position. *Id.* As we explained, "[the automatic stay] is intended to protect the debtor and to assure equal distribution among creditors." *Id.* Thus, the co-owners' claim based on violation of the stay was "wholly without merit" because it was "antagonistic to the express purpose behind [the automatic stay]." *Id.*

This case is analogous. The Bank wants the foreclosure sale declared void to preserve its lien interest in the subject property.[3] *See Chapman*, 302 P.3d at 1106. But ***1241** this outcome protects the Bank's interests as an "aggrieved property owner[ ]." *In re Globe*, 867 F.2d at 560. Voiding the foreclosure sale does not advance or preserve the bankruptcy estate, and it has nothing to do with the Bank's "claim against the *debtor*" or "against the *estate*." 11 U.S.C. § 101(10)(A), (B) (emphases added). The Bank's failure to object to the debtor's pre-foreclosure surrender of the subject property as part of the debtor's bankruptcy plan only reinforces this conclusion. Whereas the Bank's quiet-title claim is unrelated to its role as a "creditor" and the purposes for which the automatic stay was enacted, I would reject the Bank's "disingenuous attempt to use the Bankruptcy Code [for its own] advantage." *In re Globe*, 867 F.2d at 560. The automatic stay "does not confer any rights" upon the Bank in the context of this case. *Id.*[4]

Tilley v. Vucurevich (In re Pecan Groves), 951 F.2d 242 (9th Cir. 1991), further supports this conclusion. There we held that creditors (and certainly aggrieved property owners) lack standing in bankruptcy proceedings to challenge a bankruptcy court's adverse decision regarding a claimed stay violation. *Id.* at 244–46. This holding respects the principle that it is the bankruptcy trustee who "is charged with the administration of the estate for the ... creditor's benefit." *Id.* at 245; *see also* *Hillis Motors*, 997 F.2d at 585 (explaining that the trustee represents the estate and "acts as a fiduciary for the debtor's creditors"). Creditors cannot "subvert the trustee's powers" by "pursu[ing] claims the trustee abandon[ed]." *In re Pecan Groves*, 951 F.2d at 245. In this case, allowing the Bank to enforce the stay outside the bankruptcy proceedings—relief that would not benefit the debtor's bankruptcy estate and that was forgone by the trustee in the bankruptcy case—would undermine the trustee's administrative role and contradict the principle expounded by *In re Pecan Groves*.[5]

The majority contends that none of the foregoing analysis matters because state law, not federal law, resolves this case. It hangs its hat on *LN Management LLC Series 5105 Portraits Place v. Green Tree Servicing LLC (Portraits Place)*, 133 Nev. 394, 399 P.3d 359, 360–61 (2017), which upheld a creditor's challenge to an HOA foreclosure sale because it violated the automatic stay and was therefore void.[6] This ***1242** reasoning would make sense if the Bank were relying on state law for its quiet-title claim. But it's not. Thus, the question before us turns not on state law, but on federal bankruptcy law—i.e., whether the party seeking to enforce the automatic stay "fall[s] within the zone of interests

protected by [11 U.S.C. § 362(a)]." *See* *Lexmark*, 572 U.S. at 129, 134 S.Ct. 1377 (citation omitted). And although the majority relies on *Portraits Place* to answer this question, the Nevada Supreme Court's view of federal bankruptcy law and application of the automatic stay is not binding on us. *See* *Budinich v. Becton Dickinson & Co.*, 486 U.S. 196, 198, 108 S.Ct. 1717, 100 L.Ed.2d 178 (1988) ("Although state law generally supplies the rules of decision in federal diversity cases, it does not control the resolution of issues governed by federal statute.") (internal citations omitted). Indeed, the Nevada Supreme Court seemingly understood this foundational principle of federalism when it applied *federal* law, including our decision in *In re Schwartz* in deciding whether a foreclosure sale conducted in violation of the automatic bankruptcy stay is void or voidable. *Portraits Place*, 399 P.3d at 360–61 (citing *In re Schwartz*, 954 F.2d at 571). In this context, the majority's assertion that state law dictates the outcome here makes no sense.

Finally, I recognize that we have held that "violations of the automatic stay are void, not voidable." *In re Schwartz*, 954 F.2d at 571.[7] But that does not necessarily mean that anyone dissatisfied with conduct it believes violated the automatic stay may claim protection under Section 362 of the Bankruptcy Code. In *In re Schwartz*, there was no question that the party seeking to enforce the automatic stay—the debtor—fell within the zone of interests protected by the automatic stay. *Id.* at 570. The Internal Revenue Service (IRS) had assessed taxes and penalties against the debtor while the automatic stay was in effect, and the debtor argued that the IRS's claim asserted in a later bankruptcy proceeding based on the IRS's prior violative assessment was void. *Id.* We agreed, noting that the automatic stay "is designed to protect debtors from all collection efforts while they attempt to regain their financial footing." *Id.* at 571. We had no occasion in *In re Schwartz* to address the question presented here—whether a party that falls outside the zone of interests protected by the automatic stay or that seeks to use the stay in a manner contrary to its purposes is nonetheless entitled to enforce the stay. Thus, the majority's reliance on *In re Schwartz* (and *Portraits Place*'s application of *In re Schwartz*) puts the cart before the horse. If the Bank fell within the "particular class of persons [who] has a right to sue under [the automatic bankruptcy stay]," *Lexmark*, 572 U.S. at 127, 134 S.Ct. 1377 (alteration and citation ***1243** omitted), as the debtor did in *In re Schwartz*, then the void-not-voidable rule applies. But the Bank is not within such class of persons. The analysis ends there. With no right to assert Section 362(a) of the Bankruptcy Code as a basis for relief, the Bank's quiet-title claim is "wholly without merit" and must be dismissed. *In re Globe*, 867 F.2d at 560.

The concurrence argues that this reasoning upends the void-not-voidable rule. Maybe if "void" were viewed in absolute terms. But our caselaw, taken as a whole, does not apply the void-not-voidable rule in this way. If conduct violating the automatic stay were truly void ab initio, prudential standing would be immaterial—the conduct would have no legal effect as to anyone, period. More than once, however, we have applied prudential standing principles to violations of the automatic stay. *In re Globe*, 867 F.2d at 556; *In re Pecan Groves*, 951 F.2d at 242. And the majority and the concurrence fail to cite any cases where we allowed a litigant with interests unrelated to the distribution of the debtor's estate to enforce the automatic stay. *Cf.* *Burton*, 862 F.3d at 743–44 (claim filed to protect debtor's estate); *Dyer v. Lindblade (In re Dyer)*, 322 F.3d 1178, 1184 (9th Cir. 2003) (adversary action initiated by the bankruptcy trustee); *Lusardi*, 329 F.3d at 1078 (quiet-title proceeding initiated by the debtor).

The concurrence seeks to reconcile the contradiction in our precedent by suggesting that *In re Globe* and *In re Pecan Groves* are no longer good law because they predate *In re Schwartz* and are based on the now rejected premise that violations of the automatic stay are voidable, not void. Concurring Op. —— – —— & n.3. As already explained, *In re Schwartz* did not, and had no reason to, consider what impact the void-not-voidable rule had on our existing precedent that limits the litigants entitled to enforce the automatic stay. And there is nothing in our precedent instructing that *In re Globe* and *In re Pecan Groves* have been disavowed. *See, e.g.*, *Duckor Spradling & Metzger v. Baum Tr. (In re P.R.T.C., Inc.)*, 177 F.3d 774, 778 (9th Cir. 1999) (citing *In re Pecan Groves* for standing rule); *see also Lei v. Demas Wai Yan (In re Demas Wai Yan)*, 703 F. App'x 582, 583 (9th Cir. 2017) (applying *In re Globe* and *In re Pecan Groves*'s limitation on those who can enforce the automatic stay); *Morgal v. Nw. Title Agency, Inc.*, 201 F. App'x 486, 487 (9th Cir. 2006) (same); *Schneider v. San Bernardino Cnty.*, 33 F.3d 59, 1994 WL 441779, at *3 (9th Cir. Aug. 15, 1994) (unpublished) (same).

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Finally, I note that the result of the majority's decision is to allow litigants asserting a state-law claim that seeks to enforce the automatic bankruptcy stay to obtain relief that they cannot get directly under the Bankruptcy Code in bankruptcy court. This is a peculiar state of affairs, and the majority and the concurrence fail to explain why we should allow such maneuvering.

For these reasons, I respectfully dissent.

All Citations

2 F.4th 1229, 21 Cal. Daily Op. Serv. 6320, 2021 Daily Journal D.A.R. 6434

Footnotes

1 We refer here only to the version of the Nevada homeowners' association foreclosure statute in effect from 2013 to 2015, prior to the 2015 amendment. *See* 2015 Nev. Stat. 1332–49.

2 We thus do not reach the issue of whether the sale should be set aside as a matter of equity or based on the Bank's due process claims.

3 The Trust does not dispute the Bank's assertion that the HOA foreclosure sale violated the bankruptcy stay when it recorded its notice of sale. *See* 11 U.S.C. § 362(a)(4), (5) (preventing "any act to create, perfect, or enforce" a lien against either the property of the estate or the property of the debtor).

4 The Bank also pursued claims against Hill and the HOA's collection agent, which it does not raise on appeal.

5 As the Supreme Court observed in the *Lexmark* case, portraying this question as one of " 'prudential standing' is [technically] a misnomer." *Lexmark Int'l, Inc. v. Static Control Components, Inc.*, 572 U.S. 118, 127, 134 S.Ct. 1377, 188 L.Ed.2d 392 (2014) (citation omitted). The Supreme Court "in *Lexmark* ... rejected the 'prudential standing' label and made clear that whether a plaintiff's claims are within a statute's zone of interests is not a *jurisdictional* question." *Pit River Tribe v. Bureau of Land Mgmt.*, 793 F.3d 1147, 1156 (9th Cir. 2015) (emphasis added) (citing *Lexmark Int'l*, 572 U.S. at 126–28, 134 S.Ct. 1377). Indeed, "[w]hether a plaintiff comes within 'the "zone of interests" ' is an issue that requires us to determine, using traditional tools of statutory interpretation, whether a legislatively conferred *cause of action* encompasses a particular plaintiff's claim." *Lexmark Int'l*, 572 U.S. at 127, 134 S.Ct. 1377 (emphasis added) (citation omitted).

6 The Trust in its answering brief does not contest this case authority or these facts, focusing its argument solely on contesting the Bank's standing.

7 The Trust's argument that it was a bona fide purchaser (BFP), is not a defense in this situation under Nevada law because "[a] party's status as a BFP is irrelevant when a defect in the foreclosure proceeding renders the sale void."

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Bank of Am., N.A. v. SFR Investments Pool 1, LLC, 134 Nev. 604, 427 P.3d 113, 121 (2018) (en banc), *as amended on denial of reh'g* (Nov. 13, 2018).

8 State law here merely recognizes and applies a fact (voidness) created by operation of federal law. A state's attempt to nullify the result of federal law might present questions not at issue in this case.

1 On the other hand, unlike the dissent I don't find it particularly peculiar that a party could assert a claim in a state-law quiet title action that it was procedurally prevented from raising in a bankruptcy proceeding. Procedural rules regularly prevent parties from asserting claims in one type of proceeding but not another. Diverse parties litigating a state-law tort claim under $75,000 could litigate their dispute in state court, for example, but would be procedurally barred from litigating in federal court.

2 There is, as the dissent notes, a circuit split on the "void-versus-voidable distinction." As demonstrated by the cases cited above, our circuit is firmly on the "void, not voidable" side of that split.

3 *Void*, BLACK'S LAW DICTIONARY (6th ed. 1990) (citing, inter alia, *In re Oliver*, 38 B.R. 245, 248 (Bankr. D. Minn. 1984)) ("Null; ineffectual; nugatory; having no legal force or binding effect; unable, in law, to support the purpose for which it was intended. An instrument or transaction which is wholly ineffective, inoperative, and incapability of ratification and which thus has no force or effect so that nothing can cure it.").

4 *Voidable*, BLACK'S LAW DICTIONARY (6th ed. 1990) ("That which may be avoided or declared void; not absolutely void, or void in itself.").

5 The dissent relies on *In re Globe* and *In re Pecan Groves* as support for its position that "void" really means just void as to certain parties. That would only work if those opinions purported to be reaching their conclusions in a "void, not voidable" framework. But quite the contrary, as explained, those opinions are squarely rooted in *In re Brooks*'s "voidable, not void" rationale, so the dissent's attempt to rely on them as demonstrating how to "apply the void-not-voidable rule" makes no sense.

6 The dissent states I am "suggesting that *In re Globe* and *In re Pecan Groves* are no longer good law." Well, that depends on what the dissent means. If it means to suggest that I am suggesting those decisions are no longer binding precedent about prudential standing in bankruptcy proceedings, that's not true. Right or wrong, their holdings remain binding precedent in that context until changed by our court. If the dissent means that I don't think they are *good* law in the sense of being *correct* law, then I might be guilty as charged. The cases are expressly based on a premise (violations of the bankruptcy stay are voidable, not void) that we have since rejected in our bankruptcy law.

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7 The dissent characterizes my argument as claiming "that the automatic stay protects the Bank because it was a 'creditor' of the debtor in the underlying bankruptcy proceedings." That misunderstands my argument. The Bank prevails in this case because the HOA foreclosure sale was void, and can be recognized as such in a Nevada quiet title action, regardless of who would be "protected"—that is, who would have prudential standing to assert such voidness—*in a bankruptcy proceeding*. Whether or not the Bank was a creditor in the underlying bankruptcy proceedings is irrelevant to my analysis. I only discuss bankruptcy creditors in response to the dissent's claim that recognizing the voidness of that transaction in this state-law case somehow undermines federal bankruptcy law.

1 The Supreme Court has historically discussed the zone-of-interests test as a category of prudential standing. *See, e.g.*, *Bennett*, 520 U.S. at 162, 117 S.Ct. 1154. Although one Supreme Court case directed that courts should not limit standing "merely because prudence dictates," *Lexmark*, 572 U.S. at 125–28 n.4, 134 S.Ct. 1377, its most recent case addressing this issue once again blended prudential concerns with standing doctrine, *Bank of America Corp. v. City of Miami*, —— U.S. ——, 137 S. Ct. 1296, 1302–03, 197 L.Ed.2d 678 (2017) (holding that the plaintiffs had satisfied "the 'cause-of-action' (or 'prudential standing') requirement"); *see also* Wright & Miller, 13A Fed. Prac. & Proc. Juris. § 3531.7 (3d ed. 202) (discussing enduring uncertainty about the prudential zone-of-interests test).

2 As the majority noted, Nevada's HOA foreclosure statute was amended in 2015. 2015 Nev. Stat. 1332–49. I also refer only to the version in effect from 2013–2015.

3 As the majority notes, it is undisputed that the automatic stay was in effect when the foreclosure proceeding was first initiated. However, the bankruptcy court record establishes that the automatic stay had been lifted as to the subject property by the time the foreclosure sale itself occurred.

4 The concurrence argues that the automatic stay protects the Bank because it was a "creditor" of the debtor in the underlying bankruptcy proceedings. But it fails to acknowledge that the Bank is not presently pursuing relief as a "creditor" as that term is defined for purposes of bankruptcy—i.e., an entity that has a [right to payment] against the debtor" or "against the estate." 11 U.S.C. § 101(10)(A), (B); *id.* § 101(5). Instead, the Bank is acting as a "creditor" in the general sense of that term—i.e., one "to whom a debt is owed." Black's Law Dictionary (11th ed. 2019). Nor does the concurrence explain why the automatic stay should protect a creditor pursuing a claim that is wholly unrelated to the distribution of the debtor's estate.

5 I agree with the majority that *In re Pecan Groves*'s holding regarding standing in bankruptcy proceedings is inapplicable to this case.

6 The majority relies on four other cases to conclude that Nevada law controls this case. Maj. Op. —— – ——. Two are unpublished Nevada Supreme Court decisions that do no more than apply *Portraits Place*. *See Gundala v. BAC Home Loans Servicing, LP*, 483 P.3d 1121, 2021 WL 1531154, at *1 (Nev. 2021) (unpublished); *NV Eagles, LLC v. Nationstar Mortg., LLC*, 462 P.3d 1230, 2020 WL 2527389, at *1 (Nev. 2020) (unpublished). The other two cases do not support the majority's conclusion. In *SFR Investments Pool 1, LLC v. U.S. Bank, N.A.*, 135 Nev. 346, 449 P.3d

461, 465 (2019), the Nevada Supreme Court considered whether a foreclosure sale should be set aside on equitable grounds and held that a violation of the bankruptcy stay might indicate unfairness in the foreclosure proceedings. But here, the majority does not grant equitable relief due to evidence of "fraud, oppression, or unfairness." *See id.* Rather, it holds that the foreclosure sale is void because it violated the automatic bankruptcy stay. Finally, in *CitiMortgage, Inc. v. Corte Madera Homeowners Association*, 962 F.3d 1103, 1110–11 (9th Cir. 2020), our court said nothing about whether a creditor pursuing a claim unrelated to the debtor's estate may seek protection under the Bankruptcy Code; instead, we remanded for the district court to consider *in the first instance* whether the property was property of the debtor or the estate and whether the foreclosure notices at issue violated the bankruptcy stay.

7 There is a longstanding circuit split over the void-versus-voidable distinction. *See, e.g.*, *Chapman v. Bituminous Ins. Co.*, 345 F.3d 338, 344 (5th Cir. 2003) (*In re Coho Res. Inc.)*; *Bronson v. United States*, 46 F.3d 1573, 1578 (Fed. Cir. 1995); *Easley v. Pettibone Mich. Corp.*, 990 F.2d 905, 909–12 (6th Cir. 1993); *see also* *In re Myers*, 491 F.3d 120, 127 (3d Cir. 2007) (holding that the void-not-voidable rule is not absolute because Section 362(d) of the Bankruptcy Code allows bankruptcy courts to retroactively annul the stay); *Soares v. Brockton Credit Union (In re Soares)*, 107 F.3d 969, 976 (1st Cir. 1997) (same).

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10 F.4th 956
United States Court of Appeals, Ninth Circuit.

IN RE Donald Hugh NICHOLS; Jane Ann Nichols, Debtors,
Donald Hugh Nichols; Jane Ann Nichols, Appellants,
v.
Marana Stockyard & Livestock Market, Inc.; The Parsons Company; Clay Parsons; Karen Parsons; Arizona Department of Revenue; Jill H. Ford, Chapter 7 Trustee, Appellees.

No. 20-60043
|
Argued and Submitted July 9, 2021 Portland, Oregon
|
Filed September 1, 2021

Synopsis
Background: Creditors moved to convert Chapter 13 case to one under Chapter 7 based on debtors' continuing delay while criminal proceedings were pending against them, and debtors filed a competing motion to voluntarily dismiss. The United States Bankruptcy Court for the District of Arizona, Brenda Moody Whinery, Chief Judge, 2020 WL 504745, denied dismissal motion and granted motion to convert, and debtors appealed. The Bankruptcy Appellate Panel (BAP), Taylor, J., 618 B.R. 1, affirmed. Debtors appealed.

Holdings: The Court of Appeals, O'Scannlain, Senior Circuit Judge, held that:

[1] the Ninth Circuit's decision in *In re Rosson*, 545 F.3d 764, holding that there was an implied exception to a Chapter 13 debtor's absolute right to dismiss where the debtor had engaged in bad faith or abuse of the bankruptcy process, was effectively overruled by *Law v. Siegel*, 134 S.Ct. 1188, and so was no longer binding precedent in the Circuit, and

[2] considering the question anew, debtors in a Chapter 13 bankruptcy have the absolute right to dismiss their case, subject to the single exception noted expressly in the Bankruptcy Code itself, regardless of the bankruptcy court's determination that they engaged in an abuse of the bankruptcy process.

Reversed and remanded.

Procedural Posture(s): On Appeal; Motion to Convert or Dismiss Case.

West Headnotes (10)

[1] **Bankruptcy**—Carrying out provisions of Code

A bankruptcy court may not use its equitable powers, under the section of the Bankruptcy Code authorizing the court to issue any order that is necessary or appropriate to carry out the provisions of title 11, to contravene express provisions of the Code. 11 U.S.C.A. § 105(a).

3 Cases that cite this headnote

[2] **Courts**—Number of judges concurring in opinion, and opinion by divided court

Although Court of Appeals is typically bound by prior decision of another three-judge panel, it may depart from such precedent if subsequent Supreme Court opinion undercuts theory or reasoning underlying prior circuit precedent in such way that cases are clearly irreconcilable.

1 Cases that cite this headnote

[3] **Courts**—Number of judges concurring in opinion, and opinion by divided court

Ninth Circuit's decision in *In re Rosson*, 545 F.3d 764, holding that there was implied exception to Chapter 13 debtor's absolute right to dismiss where debtor had engaged in bad faith or abuse of bankruptcy process, was

effectively overruled by *Law v. Siegel*, 134 S.Ct. 1188, holding that bankruptcy court may not use its equitable powers under the Bankruptcy Code to contravene express provisions of the Code, and so *Rosson* was no longer binding precedent in the Circuit; *Law* undercut the reasoning of *Rosson*, such that the cases were clearly irreconcilable, and Court of Appeals could depart from *Rosson* precedent. 11 U.S.C.A. §§ 105(a), 1307(b).

3 Cases that cite this headnote

[4] **Courts**Decisions of Same Court or Co-Ordinate Court

Court of Appeals does not hesitate to overrule its own precedents when their underlying reasoning cannot be squared with the Supreme Court's more recent pronouncements.

1 Cases that cite this headnote

[5] **Bankruptcy**Voluntary Dismissal; Request by Debtor

Chapter 13 debtors have the absolute right to dismiss previously unconverted case, regardless of the bankruptcy court's determination that they engaged in an abuse of the bankruptcy process; unambiguous text of the section of the Code governing conversion or dismissal of Chapter 13 cases plainly requires the court to dismiss a case upon the debtor's request, and there is no textual indication that the court has any discretion whatsoever. 11 U.S.C.A. § 1307(b).

3 Cases that cite this headnote

[6] **Statutes**Mandatory or directory statutes

Term "shall" in a statute normally creates obligation impervious to judicial discretion.

[7] **Bankruptcy**Voluntary Dismissal; Request by Debtor

Section of the Bankruptcy Code governing conversion or dismissal of Chapter 13 cases contains a single express exception to the debtor's right to dismiss, which bars dismissal where the debtor has already exercised his right to convert the case to Chapter 13 from Chapters 7, 11, or 12. 11 U.S.C.A. § 1307(b).

4 Cases that cite this headnote

[8] **Bankruptcy**Voluntary Cases
BankruptcyInvoluntary Cases

Section of the Bankruptcy Code providing, inter alia, that an involuntary case may be commenced only under Chapter 7 or 11 of title 11 is designed to ensure that Chapter 13 remains a wholly voluntary alternative to Chapter 7. 11 U.S.C.A. § 303(a).

1 Cases that cite this headnote

[9] **Constitutional Law**Particular Issues and Applications

Even if the Bankruptcy Code did not provides ample tools for bankruptcy courts to address debtor misconduct, it would be up to Congress, as opposed to the courts, to remedy the omission by way of appropriate legislation.

[10] **Constitutional Law**Making, Interpretation, and Application of Statutes

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Courts must adhere to statute's clear mandate, regardless of practical difficulties that may ensue.

***958** Appeal from the Ninth Circuit, Bankruptcy Appellate Panel, Taylor, Lafferty III, and Brand, Bankruptcy Judges, Presiding, BAP No. 20-1032

Attorneys and Law Firms

German Yusufov (argued), Yusufov Law Firm PLLC, Tucson, Arizona, for Appellants.

D. Alexander Winkelman (argued) and Frederick J. Petersen, Mesch Clark Rothschild, Tucson, Arizona, for Appellees.

Before: Diarmuid F. O'Scannlain, Richard A. Paez, and Mark J. Bennett, Circuit Judges.

OPINION

O'SCANNLAIN, Circuit Judge:

We must decide whether debtors in a Chapter 13 bankruptcy have the right to dismiss their case, regardless of the bankruptcy court's determination that they engaged in an abuse of the bankruptcy process.

I

A

Appellants Donald Hugh Nichols and his wife, Jane Ann Nichols (collectively, "the Nicholses"), filed a Chapter 13 bankruptcy petition seeking to restructure their debts. After filing the petition, the Nicholses were indicted on federal criminal charges for their alleged participation in a scheme to defraud Appellee Marana Stockyard and Livestock Market, Inc. ("Marana").

To avoid disclosure of information that might compromise their position in the criminal proceedings, the Nicholses declined to complete any of the steps required by the Bankruptcy Code to advance their case. They refused, *inter alia*, to hold a meeting with creditors, *cf.* 11 U.S.C. § 341; to file outstanding tax returns, *cf. id.* § 1308; or to propose an appropriate repayment plan, *cf. id.* § 1322. Their bankruptcy case thus languished for months without resolution.

Marana, which had filed a claim in the Nicholses' bankruptcy case seeking to recover losses from the alleged fraud, moved pursuant to 11 U.S.C. § 1307(c) for the case to be converted to a liquidation under Chapter 7 of the Bankruptcy Code.[1] In ***959** response, the Nicholses requested a stay of the bankruptcy case during the pendency of the criminal proceedings.

The bankruptcy court denied the motion to stay. At the same time, the bankruptcy court determined that conversion of the case to a Chapter 7 liquidation was justified "for cause" under § 1307(c) due to the Nicholses' delays, which the court deemed to be unwarranted. The bankruptcy court also determined that conversion to Chapter 7 would have been proper, in the alternative, under § 1307(e), insofar as the Nicholses had failed to file tax returns for several years.[2]

B

The Nicholses requested another opportunity to remain in Chapter 13, however. The bankruptcy court acceded to their request and postponed by 30 days the entry of an order converting the case to Chapter 7. The bankruptcy court required the Nicholses to file outstanding tax returns and to submit a confirmable repayment plan to the Chapter 13 trustee before expiration of the 30-day period.

The Nicholses did not comply with the bankruptcy court's requirements. Before the expiration of the 30-day period, the Nicholses moved to dismiss voluntarily their bankruptcy case pursuant to § 1307(b).[3]

C

Although § 1307(b) confers upon a Chapter 13 debtor the right to request dismissal of his case "at any time," the bankruptcy court denied the Nicholses' motion to dismiss. Relying upon our decision in *In re Rosson*, 545 F.3d 764 (9th Cir. 2008), the bankruptcy court understood there to be an implied exception to § 1307(b) where the debtor has engaged in bad faith or abuse of the bankruptcy process. The bankruptcy court concluded that the Nicholses had "used Chapter 13 to hide from creditors during the pendency of the criminal proceedings" and that "[s]uch conduct constitutes an abuse of the bankruptcy process, justifying denial of the ... Motion to Dismiss." The bankruptcy court thereupon converted the case to a liquidation under Chapter 7.

The Nicholses timely appealed the bankruptcy court's order to the Ninth Circuit's Bankruptcy Appellate Panel ("BAP"). The BAP affirmed the bankruptcy court's order. The Nicholses then timely appealed the BAP's decision to this court.

II

The Nicholses now argue that the bankruptcy court erred by relying upon *Rosson*'s implied "bad faith or abuse of process" exception to § 1307(b) to deny their request for voluntary dismissal. According to the Nicholses, *Rosson* has been effectively overruled by the Supreme Court's subsequent decision in *Law v. Siegel*, 571 U.S. 415, 134 S.Ct. 1188, 188 L.Ed.2d 146 (2014), which, they contend, must be understood to prohibit a bankruptcy court from invoking equitable considerations to contravene § 1307(b)'s express language conferring upon a Chapter 13 debtor an absolute right to dismiss his case. The ***960** narrow question before us is whether *Rosson* has been implicitly abrogated by *Law*.

A

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Rosson concerned a Chapter 13 debtor who was ordered by the bankruptcy court to deposit the proceeds of an expected arbitration award with the Chapter 13 trustee. 545 F.3d at 768. When the bankruptcy court was informed that the debtor had received the anticipated payment, but had not deposited it as instructed, the bankruptcy court determined *sua sponte* to convert the case to Chapter 7. *Id.* Before the conversion order could be entered, however, the debtor moved to dismiss under § 1307(b). *Id.* The bankruptcy court denied the motion to dismiss and converted the case, stating that it would be a "gross miscarriage of justice" to allow the debtor to "abscond" with assets of the estate. *Id.* at 769. The debtor appealed to the district court, which affirmed. *Id.*

2

On subsequent appeal to this court in *Rosson*, we acknowledged the existence of a circuit split regarding a debtor's right to dismiss under § 1307(b) while a motion to convert under § 1307(c) remains pending. *Id.* at 771–72 (comparing *In re Barbieri*, 199 F.3d 616 (2d Cir. 1999); with *In re Molitor*, 76 F.3d 218 (8th Cir. 1996)). We further recognized that the Ninth Circuit's BAP had previously concluded that § 1307(b) confers upon a Chapter 13 debtor an absolute right to voluntary dismissal of his case. *Id.* at 772 (discussing *In re Croston*, 313 B.R. 447 (9th Cir. BAP 2004); and *In re Beatty*, 162 B.R. 853 (9th Cir. BAP 1994)). We determined, however, that the BAP's interpretation of § 1307(b) was no longer tenable after the Supreme Court's decision in *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365, 127 S.Ct. 1105, 166 L.Ed.2d 956 (2007), which concerned the scope of a debtor's right to convert from Chapter 7 to Chapter 13 pursuant to 11 U.S.C. § 706(a).[4] *Id.* We understood *Marrama* to stand for the broad proposition that "even otherwise unqualified rights in the debtor are subject to limitation by the bankruptcy court's power under § 105(a) to police bad faith and abuse of process." *Id.* at 773 n.12.

Based on such interpretation of *Marrama*, we held that "the debtor's right of voluntary dismissal under § 1307(b) is not absolute, but is qualified by the authority of a bankruptcy court to deny dismissal on grounds of bad-faith conduct or to prevent an abuse of process." *Id.* at 774 (quotation marks and citation omitted). Accordingly, we affirmed the bankruptcy court's order denying the debtor's motion to dismiss and converting the case to Chapter 7 because of the debtor's bad faith

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conduct. *Id.* at 774–75.

B

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Law, which was decided six years later, concerned a Chapter 7 debtor who perpetrated a fraud on the bankruptcy court by falsely reporting that a lien existed on his primary residence. 571 U.S. at 418–19, 134 S.Ct. 1188. The trustee later determined that the alleged lien was a sham filed by the debtor to protect his interest in the home. *Id.* at 419, 134 S.Ct. 1188. Accordingly, the trustee initiated an adversary proceeding to have the lien removed, and, after he prevailed, he sought to have his ***961** attorney's fees paid from the debtor's exempt property. *Id.* at 419–20, 134 S.Ct. 1188.

Despite 11 U.S.C. § 522(k)'s express prohibition on the use of a debtor's exempt property to cover expenses associated with administering the estate, the bankruptcy court granted the trustee's request.[5] *Id.* at 420, 134 S.Ct. 1188. On appeal, the BAP affirmed the order as a permissible exercise of the bankruptcy court's equitable powers. *Id.* Upon subsequent appeal to this court, we also affirmed. *Id.* In an unpublished memorandum disposition, we concluded that the surcharge was proper because it was "calculated to compensate the estate for the actual monetary costs imposed by the debtor's misconduct, and was warranted to protect the integrity of the bankruptcy process." *Id.* (quoting *In re Law*, 435 F. App'x. 697, 698 (9th Cir. 2011)).

2

[1]The Supreme Court reversed. In so doing, the Court made clear that a bankruptcy court may not use its equitable powers under § 105(a) to contravene express provisions of the Bankruptcy Code. 571 U.S. at 422–23, 134 S.Ct. 1188. On behalf of a unanimous Court, Justice Scalia wrote that § 105(a) does not "allow the bankruptcy court to override explicit mandates of other sections of the Bankruptcy Code," including § 522(k)'s express prohibition on charging a debtor's exempt property to pay the trustee's administrative expenses. *Id.* at 421, 134 S.Ct. 1188 (quoting 2 Collier on Bankruptcy ¶ 105.01[2] (16th ed. 2013)).

In doing so, the Supreme Court firmly rejected the argument—advanced by the Solicitor General in an amicus brief—that *Marrama* must be understood to establish that a bankruptcy court's § 105(a) powers to punish bad faith conduct implicitly qualify language contained elsewhere in the Bankruptcy Code. *Id.* at 425–26, 134 S.Ct. 1188. On the contrary, *Law* concluded that "*Marrama* most certainly did not endorse, even in dictum, the view that equitable considerations permit a bankruptcy court to contravene express provisions of the Code." *Id.* at 426, 134 S.Ct. 1188.

C

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[2] [3]Although we are typically bound by the prior decision of another three-judge panel, we may depart from such precedent if a subsequent Supreme Court opinion "undercut[s] the theory or reasoning underlying the prior circuit precedent in such a way that the cases are clearly irreconcilable." *Miller v. Gammie*, 335 F.3d 889, 900 (9th Cir. 2003) (en banc). Here, we have no doubt that *Law* undercuts the reasoning of *Rosson*.

The holding of *Rosson* cannot stand absent the premise, ostensibly articulated in *Marrama*, that a bankruptcy court's equitable powers under § 105(a) can limit express language contained elsewhere in the Bankruptcy Code. *See* 545 F.3d at 773 n.12. *Law*, however, clearly rejected such reasoning. *See* 571 U.S. at 426, 134 S.Ct. 1188. In fact, *Law* explicitly rejected the sweeping interpretation of *Marrama* that we embraced in *Rosson*. *See id.* *Rosson* and *Law* are thus irreconcilable, such that *Rosson* has been effectively overruled.

Marana argues, however, that *Rosson* is consistent

with *Law* because *Rosson* did not limit the Chapter 13 debtor's right to dismiss based on § 105(a), but rather based on a "holistic interpretation" of § 1307. According to Marana, *Rosson* ***962** stands for the proposition that, when faced with a bad-faith debtor's motion for voluntary dismissal under § 1307(b), a bankruptcy court may nevertheless heed its competing statutory mandate under § 1307(c) to convert the case to Chapter 7 to promote the best interest of creditors.

Moreover, Marana contends that *Law*'s treatment of *Marrama* does not undermine *Rosson*. Marana argues that *Rosson* should be understood to rely on *Marrama* not for the sweeping proposition that express provisions of the Bankruptcy Code are limited by the bankruptcy court's § 105(a) powers to punish bad faith, but rather for the far narrower principle that a debtor's bad faith is a "cause" justifying conversion to Chapter 7 under § 1307(c). Because, on Marana's view, *Law* rejected only the broad reading of *Marrama*, but otherwise left that precedent intact, Marana argues that *Rosson* remains similarly undisturbed.

Marana's arguments fail to persuade, however, because they mischaracterize the reasoning that we actually employed in *Rosson*. We did not rely on § 1307(c), nor did we discern in such statutory subsection any import for interpreting the mandate of § 1307(b). Rather, we primarily relied on the premise that *Marrama* had established "the important point" that "even otherwise unqualified rights in the debtor are subject to limitation by the bankruptcy court's power under § 105(a) to police bad faith and abuse of process." 545 F.3d at 773 n.12.

Our expansive reading of *Marrama* was a defensible one at the time. Indeed, in *Law*, the Solicitor General advanced the very same reading of *Marrama* that we adopted in *Rosson*. *See, e.g.*, Brief for the United States at 25, *Law v. Siegel*, 571 U.S. 415, 134 S.Ct. 1188, 188 L.Ed.2d 146 (2014) (No. 12-5196) (citing *Marrama* for the principle that § 105(a) empowers a bankruptcy court to disregard the express language of § 522(k) in order to punish fraud, misrepresentation, or other misconduct by the debtor). We must recognize, however, that such a position was unanimously and unambiguously rejected in *Law*.

2

[4]Consequently, we now hold that *Rosson* has been effectively overruled by *Law* and is no longer binding precedent in this Circuit. Ever since our en banc opinion in *Miller v. Gammie*, 335 F.3d 889 (9th Cir. 2003), in which we clarified the standard in this Circuit for departure from a prior three-judge panel's decision based on intervening Supreme Court precedent, we have not hesitated to overrule our own precedents when their underlying reasoning could not be squared with the Supreme Court's more recent pronouncements.[6] We follow the same course here.

III

[5]Because we are no longer bound by *Rosson*, we must consider anew whether a Chapter 13 debtor's right to voluntary dismissal of his case under § 1307(b) admits of an exception in the event of the debtor's bad faith or abuse of process. If not, the Nicholses were entitled to dismiss their case, regardless of the bankruptcy court's determination that conversion to Chapter 7 was warranted.

***963** A

1

[6]On this point, section 1307(b)'s text is unambiguous. The statute provides, in relevant part: "On request of the debtor at any time ... the court shall dismiss a case under this chapter." The term "shall" "normally creates an obligation impervious to judicial discretion." *Lexecon Inc. v. Milberg Weiss Bershad Hynes & Lerach*, 523 U.S. 26, 35, 118 S.Ct. 956, 140 L.Ed.2d 62 (1998); *see also* *Barbieri*, 199 F.3d at 619 ("The term 'shall,' as the Supreme Court has reminded us, generally is mandatory and leaves no room for the exercise of discretion by the trial court."). Section 1307(b)'s text plainly requires the bankruptcy court to dismiss the case upon the debtor's request. There is no textual indication that the bankruptcy court has any discretion whatsoever.

Although our sister circuits have disagreed with respect to the existence of a "bad faith" exception to a debtor's right

to dismiss under § 1307(b), there is no dispute that the statute's text, by its own terms, confers an absolute right to dismiss. For example, the Fifth Circuit, which concluded, similarly to our holding in *Rosson*, that a debtor's right to dismiss is subject to an implied exception in the event of the debtor's bad faith conduct, nonetheless confirmed that "the plain language of ... § 1307(b) can be read to confer an absolute right to dismiss." *In re Jacobsen*, 609 F.3d 647, 649 (5th Cir. 2010).

Indeed, the Fifth and Eighth Circuits' view—that the debtor's right under § 1307(b) is subject to an implied exception—is grounded, not on an alternative reading of the statutory text, but rather on the same, now-discredited theory of equitable powers that we had previously embraced in *Rosson*. *See* *Jacobsen*, 609 F.3d at 661 ("Proceeding from the propositions in *Marrama* that an apparently unqualified right is subject to an exception for bad faith and that bad faith justifies a bankruptcy court's exercise of its powers under § 105(a), we conclude that § 1307(b) is subject to a similar exception ...."); *In re Molitor*, 76 F.3d 218, 220 (8th Cir. 1996) (relying on the "broad purpose" of the Bankruptcy Code to arrive at an interpretation that protects bankruptcy courts from "a myriad of potential abuses").

As we have already discussed, the Supreme Court's decision in *Law* clearly rejected such reasoning. And, ever since *Law* was decided, no other Circuit has taken the position that there is an implied equitable exception to § 1307(b)'s right to dismiss. *Cf. Smith v. U.S. Bank N.A.*, 999 F.3d 452, 456 (6th Cir. 2021) ("The command of 1307(b) is no mere procedural nicety, which is likely why no circuit court has accepted [the implied bad faith exception] argument since *Law* ...."). Accordingly, for the same reason that we dispensed with *Rosson*, we must also reject the approach previously adopted by the Fifth and Eighth Circuits, and instead hew to the "absolute right" approach articulated by the Second Circuit in *Barbieri* and followed, most recently, by the Sixth Circuit in *Smith*.

2

[7]Furthermore, the statutory text does not provide any support for the view that any other subsection in § 1307, such as § 1307(c), limits the debtor's right to dismiss under § 1307(b). Had it wished to provide for such an exception, Congress easily could have indicated the existence of one expressly. Indeed, § 1307(b) *does* contain a single *express* exception to the debtor's right to dismiss, which bars dismissal where the debtor has *already* exercised his right to convert the case to Chapter 13 from Chapters 7, 11, or 12. That Congress codified an express exception to § 1307(b)'s right to dismiss demonstrates that Congress ***964** considered the issue of exceptions and chose not to prescribe additional ones. *See* *United States v. Johnson*, 529 U.S. 53, 58, 120 S.Ct. 1114, 146 L.Ed.2d 39 (2000) ("The proper inference ... is that Congress considered the issue of exceptions and, in the end, limited the statute to the ones set forth.").

Marana argues that an "absolute right" reading of § 1307(b) would effectively render § 1307(c) a nullity by depriving the bankruptcy court of discretion to convert a case to Chapter 7 for cause. But "that is no more significant than the fact that an order granting a creditor's motion to convert under § 1307(c) would foreclose dismissal under § 1307(b)." *Barbieri*, 199 F.3d at 620. "In the event of competing motions filed under subsections (b) and (c), one subsection will inevitably prevail at the expense of the other." *Id.* (brackets omitted) (quoting *In re Patton*, 209 B.R. 98, 100 (Bankr. E.D. Tenn. 1997)). "Accordingly, the assertion that an absolute right under § 1307(b) would nullify § 1307(c) 'carries no weight since either party could make the same argument.' " *Id.* (quoting *Patton*, 209 B.R. at 104).

[8]Far from conflicting with other sections of the Bankruptcy Code, the "absolute right" reading of § 1307(b) is entirely consistent with the text and policy of § 303(a), which is designed to ensure that Chapter 13 remains a "wholly voluntary alternative to Chapter 7." *Smith*, 999 F.3d at 455 (quoting *Harris v. Viegelahn*, 575 U.S. 510, 514, 135 S.Ct. 1829, 191 L.Ed.2d 783 (2015)); *see also* *Barbieri*, 199 F.3d at 620 (reasoning that the reading of § 1307(b) as conferring an absolute right to dismiss best reflects "the intention of Congress to create an entirely voluntary chapter of the Bankruptcy Code").

B

We conclude that § 1307(b)'s text confers upon the debtor an absolute right to dismiss a Chapter 13 bankruptcy case, subject to the single exception noted expressly in the statute itself. Consequently, the bankruptcy court here

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erred in denying the Nicholses' motion to dismiss based solely on its finding of abuse of the bankruptcy process.

[9] [10]We are confident that the Bankruptcy Code provides ample alternative tools for bankruptcy courts to address debtor misconduct. Even if such tools were lacking, however, it would be up to Congress to remedy the omission by way of appropriate legislation. We must adhere to the statute's clear mandate, regardless of practical difficulties that may ensue.

Accordingly, we **REVERSE** the decision of the bankruptcy court, and we **REMAND** this matter to the bankruptcy court for further proceedings in accord with this opinion.[7]

REVERSED and REMANDED.

All Citations

10 F.4th 956, 70 Bankr.Ct.Dec. 165, 21 Cal. Daily Op. Serv. 9164, 2021 Daily Journal D.A.R. 9120

IV

Footnotes

1 Section 1307(c) provides, in relevant part:

> [O]n request of a party in interest or the United States trustee and after notice and a hearing, the court may convert a case under this chapter to a case under chapter 7 of this title, or may dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause, including—
>
> (1) unreasonable delay by the debtor that is prejudicial to creditors;
>
> ...

2 Section 1307(e) provides:

> Upon the failure of the debtor to file a tax return under section 1308, on request of a party in interest or the United States trustee and after notice and a hearing, the court shall dismiss a case or convert a case under this chapter to a case under chapter 7 of this title, whichever is in the best interest of the creditors and the estate.

3 Section 1307(b) provides:

> On request of the debtor at any time, if the case has not been converted under section 706, 1112, or 1208 of this title, the court shall dismiss a case under this chapter. Any waiver of the right to dismiss under this subsection is unenforceable.

4 Section 706(a) provides:

> The debtor may convert a case under this chapter to a case under chapter 11, 12, or 13 of this title at any time, if the case has not been converted under section 1112, 1208, or 1307 of this title. Any waiver of the right to convert a case under this subsection is unenforceable.

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5 Section 522(k) provides, in relevant part: "Property that the debtor exempts under this section is not liable for payment of any administrative expense ...."

6 *See, e.g.*, *Langere v. Verizon Wireless Servs., LLC*, 983 F.3d 1115, 1122 (9th Cir. 2020); *United States v. Baldon*, 956 F.3d 1115, 1121 (9th Cir. 2020); *Dorman v. Charles Schwab Corp.*, 934 F.3d 1107, 1112 (9th Cir. 2019); *Murray v. Mayo Clinic*, 934 F.3d 1101, 1105 (9th Cir. 2019); *United States v. Valencia-Mendoza*, 912 F.3d 1215, 1222 (9th Cir. 2019); *Rodriguez v. AT & T Mobility Servs. LLC*, 728 F.3d 975, 981 (9th Cir. 2013); *Phelps v. Alameida*, 569 F.3d 1120, 1133 (9th Cir. 2009).

7 Appellants' motion to strike portions of the Supplemental Excerpts of Record is denied as moot as our opinion does not rely on the contested portions of the record. Appellants' Mot. to Strike from Excerpts of Record Documents, *Nichols v. Marana Stockyard and Livestock Mkt.*, No. 20-60043 (9th Cir. Jan. 4, 2021), ECF No. 27.

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Ninth Circuit BAP Cases

2022 WL 884595
United States Bankruptcy Appellate Panel of the Ninth Circuit.

IN RE: Rizal Juco GUEVARRA, Debtors.
Rizal Juco Guevarra, Appellant,
v.
Douglas M. Whatley, Appellee.

BAP No. EC-21-1141-SFL
|
Bk. No. 2:18-bk-25306
|
Filed MARCH 25, 2022

Synopsis
Background: After initially representing that he had no interest in real property titled in his and his nephew's names as joint tenants and failing to exempt the property in his original bankruptcy schedules, and after Chapter 7 trustee, with court approval, sold the property, debtor filed pro se amended schedules in which he claimed an interest in the property valued at $32,500.00 and claimed the sale proceeds as exempt under California's "wild card" exemption. Trustee objected. The United States Bankruptcy Court for the Eastern District of California, Christopher D. Jaime, J., 2020 WL 2844384, sustained objection on basis that exemption was claimed for improper purpose and, on appeal, the Bankruptcy Appellate Panel (BAP), 2021 WL 1179619, vacated and remanded. On remand, the Bankruptcy Court, Jaime, J., 2021 WL 2350748, sustained objection based on equitable estoppel. Debtor appealed.

Holdings: The Bankruptcy Appellate Panel (BAP), Spraker, J., held that:

[1] the Bankruptcy Court clearly erred when it found that debtor knowingly concealed his ownership in the property, for purposes of establishing "representation" element of equitable estoppel under California law;

[2] the Bankruptcy Court clearly erred when it found that debtor "concealed" a present intent to exempt his interest in the property, for purposes of estoppel; and

[3] the Bankruptcy Court clearly erred in finding that trustee was actually and permissibly ignorant of the truth, for purposes of estoppel.

Reversed.

Procedural Posture(s): On Appeal; Objection to Claimed Exemptions.

West Headnotes (32)

[1] **Bankruptcy** Scope of review in general

Bankruptcy Appellate Panel (BAP) would exercise its discretion to take judicial notice of the documents filed in debtor's bankruptcy case.

[2] **Bankruptcy** Discretion

Bankruptcy Appellate Panel (BAP) reviews the bankruptcy court's decision whether to apply equitable estoppel for an abuse of discretion.

[3] **Bankruptcy** Discretion

Bankruptcy court abuses its discretion if it applies an incorrect legal standard, or its factual findings are illogical, implausible, or without support in the record.

[4] **Bankruptcy** Property of Estate in General
Bankruptcy Exemptions

When a debtor files a Chapter 7 petition, the debtor's legal and equitable interests in property as of the petition date become property of the bankruptcy estate, subject to the debtor's right to exempt certain property of the estate. 11

U.S.C.A. §§ 522, 541.

[5] **Bankruptcy** Validity and effect of opt-out legislation

Bankruptcy Code includes a list of federal bankruptcy exemptions but also permits states to "opt out" of the federal exemption scheme and offer their own list of exemptions. 11 U.S.C.A. § 522.

[6] **Bankruptcy** Validity and effect of opt-out legislation

California has "opted out" of the federal exemption scheme and permits its debtors only those exemptions allowable under state law. Cal. Civ. Proc. Code § 703.130.

[7] **Bankruptcy** Particular proceedings or issues
Bankruptcy Effect of State Law

Although the bankruptcy court has jurisdiction to decide the merits of a California debtor's exemption claims, the allowance or disallowance of such claims is governed by California law. Cal. Civ. Proc. Code § 703.130.

[8] **Exemptions** Construction of exemption laws in general

California exemptions are liberally construed in favor of debtor.

[9] **Bankruptcy** Date of determination

Court must determine a debtor's exemption rights as they existed on the date he filed his bankruptcy petition.

[10] **Bankruptcy** Amendment
Bankruptcy Amendment

Debtors in bankruptcy have general right to amend their schedules, including their exemptions, at any time before case is closed. Fed. R. Bankr. P. 1009(a).

[11] **Bankruptcy** Equitable powers and principles
Bankruptcy Amendment
Bankruptcy Amendment

Bankruptcy courts have no equitable authority under federal law to restrict debtors' right to amend their schedules, including their exemptions, at any time before case is closed, based on perception of bad faith or prejudice to creditors. Fed. R. Bankr. P. 1009(a).

[12] **Bankruptcy** Equitable powers and principles
Bankruptcy Amendment
Bankruptcy Amendment

Bankruptcy courts' equitable power to restrict debtors' general right to amend their bankruptcy schedules, including their exemptions, at any time before case is closed might be derived from state law if state law provides equitable basis for disallowing the amended exemption.

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[13] **Exemptions** Estoppel

Equitable estoppel can be invoked to sustain objections to California exemptions.

[14] **Estoppel** Presumptions and burden of proof

Under California law, when equitable estoppel is raised in an objection to an exemption, the objecting party bears the burden of proof to establish the elements of equitable estoppel.

[15] **Estoppel** Essential elements

To successfully invoke equitable estoppel under California law, the objecting party must establish: (1) a representation or concealment of material facts, (2) made with knowledge, actual or virtual, of the facts, (3) to a party ignorant, actually and permissibly, of the truth, (4) with the intention, actual or virtual, that the ignorant party act on it, and (5) that party was induced to act on it.

[16] **Bankruptcy** Validity and effect of opt-out legislation

California permits bankruptcy debtors to choose either California's bankruptcy exemptions or California's nonbankruptcy exemptions, but not both. Cal. Civ. Proc. Code §§ 703.140(a), 703.140(b), 704.010 et seq.

[17] **Estoppel** Basis of estoppel

Under California law, doctrine of equitable estoppel is based on theory that party who by his declarations or conduct misleads another to his prejudice should be estopped from obtaining benefits of his misconduct.

[18] **Estoppel** Representations

Under California law, the party asserting equitable estoppel must prove some misrepresentation or concealment of a material fact by the other party.

[19] **Exemptions** Estoppel

Where, following Chapter 7 trustee's sale of real property jointly titled in debtor's and his nephew's names, debtor amended his schedules pro se to claim an interest in the property and to claim sale proceeds as exempt under state "wild card" exemption, the Bankruptcy Court clearly erred when, in sustaining trustee's exemption objection based on equitable estoppel, it found that debtor knowingly concealed his ownership in the property, as established "representation" element of estoppel under California law; while debtor stated that he had no ownership interest of value, such statements were part of a broader, more nuanced resulting trust argument that he held bare legal title to the property and held equitable title in trust for nephew, debtor early on informed trustee, through his counsel, of facts and law supporting that argument, and so there was no misrepresentation of material fact, only a dispute about legal implications of those facts.

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[20] **Estoppel**Representations

Under California law, equitable estoppel focuses on representations to party allegedly prejudiced.

[21] **Trusts**Presumptions and burden of proof

Under California law, a transferee of real property who does not pay the purchase price for the property is presumed to hold the property in a resulting trust for the party who paid the consideration.

[22] **Bankruptcy**Legal or equitable interests in general

When a debtor holds only bare legal title to real property, the substantive equitable interest does not become property of bankruptcy estate. 11 U.S.C.A. § 541(d).

[23] **Bankruptcy**Bona fide purchasers and rights thereof

If a bankruptcy trustee has constructive notice of a resulting trust held by the debtor for the beneficial owners of the property, it cannot be avoided under the trustee's strong-arm powers. 11 U.S.C.A. § 544(a)(3).

[24] **Exemptions**Estoppel

Where, following Chapter 7 trustee's sale of real property jointly titled in debtor's and his nephew's names, debtor amended his schedules pro se to claim interest in the property and to claim sale proceeds as exempt under state "wild card" exemption, the Bankruptcy Court clearly erred when, in sustaining trustee's exemption objection based on equitable estoppel, it found that debtor "concealed" a present intent to exempt his interest in the property so as to induce trustee to sell it, as established "representation" element of estoppel under California law; debtor provided trustee with all existing facts concerning his ownership, and absence of an exemption for debtor's interest in the property in his original schedules did not constitute a representation that he would not later amend the exemption, particularly in light of changed circumstances existing after debtor lost his challenge to the estate's rights in the property.

[25] **Exemptions**Acts or omissions constituting waiver in general

Under California law, debtor's initial decision to exempt his retirement account under state's wild-card exemption did not preclude his later amendment of his exemptions to claim the account exempt under a more specific provision applicable to a debtor's right to receive a payment under a pension or similar plan or contract. Cal. Civ. Proc. Code § 703.140(b)(10)(E).

[26] **Exemptions**Estoppel

Where, following Chapter 7 trustee's sale of real property jointly titled in debtor's and his nephew's names, debtor amended his schedules pro se to claim interest in the property and to claim sale proceeds as exempt under state "wild card" exemption, the Bankruptcy Court clearly erred when, in sustaining trustee's exemption objection based on equitable estoppel, it found that trustee was actually and permissibly ignorant of debtor's ownership and of his ability to exempt his interest if court rejected his

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resulting trust argument, as established element of estoppel under California law; trustee knew of debtor's interest under grant deed as well as his resulting trust argument, he knew or should have known that there was no need for debtor to exempt an interest that was limited to bare legal title because the estate did not have any beneficial interest in such property, and he was charged with knowing that debtor could amend his exemption in light of adverse court ruling. 11 U.S.C.A. § 541(d).

[27] **Estoppel** Knowledge of facts
Estoppel Reliance on adverse party

Under California law, where the person pleading estoppel had knowledge of the facts, there is no reliance.

[28] **Bankruptcy** Waiver or Loss of Exemption

Bankruptcy court lacks authority to deny an exemption on grounds of bad faith.

[29] **Estoppel** Nature and Application of Estoppel in Pais

Equitable estoppel is not substitute for bad faith.

[30] **Bankruptcy** Waiver or Loss of Exemption

Courts must be careful not to penalize debtors for exercising statutory right to amend their exemptions or to read too much into debtor's failure to exempt asset; without more, such omission does not constitute misrepresentation or concealment for purposes of equitable estoppel.

[31] **Bankruptcy** Amendment
Bankruptcy Waiver or Loss of Exemption

Standing alone, debtor's failure to exempt asset does not impermissibly induce bankruptcy trustee to administer asset, as he or she knows that debtors may amend their exemptions as matter of right.

[32] **Bankruptcy** Waiver or Loss of Exemption

Courts are not free to ignore the necessary implications of *Law v. Siegel*, 134 S.Ct. 1188, which abrogated bankruptcy courts' authority to deny an exemption on grounds of bad faith, simply because they present a practical problem for Chapter 7 trustees in administering estate assets.

Appeal from the United States Bankruptcy Court for the Eastern District of California, Christopher D. Jaime, Bankruptcy Judge, Presiding

Attorneys and Law Firms

Mark T. O'Toole, argued for appellant;

Barry H. Spitzer, Sacramento, argued for appellee.

Before: SPRAKER, FARIS, and LAFFERTY, Bankruptcy Judges.

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OPINION

SPRAKER, Bankruptcy Judge:

INTRODUCTION

***1** [1]The bankruptcy court held that debtor Rizal Guevarra was equitably estopped from amending his exemption. Guevarra appeals this decision. The bankruptcy court found that Guevarra induced the chapter 7[1] trustee to sell his joint interest in real property by denying any interest and by failing to exempt the real property in his original schedules. The court based its decision on an unduly narrow understanding of Guevarra's position. The record demonstrates that the trustee was fully apprised of the facts concerning Guevarra's ownership and his argument that he held his interest in a resulting trust for his nephew. As such, the trustee cannot prove all the elements of equitable estoppel. Therefore, we REVERSE.

FACTS[2]

Many of the facts set forth below are drawn from this Panel's prior decision in *Guevarra v. Whatley (In re Guevarra)*, BAP No. EC-20-1165-LBT, 2021 WL 1179619 (9th Cir. BAP Mar. 29, 2021). Guevarra commenced his bankruptcy case in August 2018. Douglas M. Whatley was appointed to serve as the chapter 7 trustee. Guevarra listed in his schedules real property located in North Highlands, California (the "Property"). More specifically, in response to the question in Schedule A/B "Do you own or have any legal or equitable interest in any residence, building, land, or similar property," he answered "yes" and listed the Property by its street address. In the space provided in the schedule for describing the nature of his ownership interest, he stated: "[c]o-signed for Nephew; Debtor has no interest in property." He valued the Property at $217,612 but stated that the value of the portion he owned was "0.00." Guevarra also listed the loan secured by the deed of trust encumbering the Property as a secured debt in his Schedule D.

Consistent with his Schedule A/B, Guevarra did not exempt any interest in the Property. He did, however, claim an exemption under California Code of Civil Procedure ("CCP") § 703.140(b)(5)—also known as California's "wild card" exemption—for $310.00 in his bank accounts and $22,306.20 in a 401(k) account.

The deed for the Property listed Guevarra and his nephew Daryl Guevarra as joint tenants. Indeed, Guevarra never denied this. By the time of the § 341(a) hearing held in September 2018, or shortly thereafter, the trustee knew that Guevarra and Daryl held title to the Property as joint tenants. Almost immediately, the trustee disagreed with Guevarra's assertion that he had no interest of value in the Property. On December 13, 2018, the trustee's counsel wrote to Daryl to advise him that the bankruptcy estate asserted an interest in the Property. As counsel explained to Daryl, "[a]ccording to the documents provided by your uncle, you and he are on title to the real property ...."

***2** Guevarra's counsel responded to the trustee's counsel roughly a week later committing to provide the trustee with documents showing that Guevarra did not live at the Property and had not made any payments on the loan. Nonetheless, based on Guevarra's joint tenancy interest, the trustee continuously asserted that 50% of any equity in the Property was property of the bankruptcy estate. And Guevarra continuously countered that while the deed granted him joint title to the Property, he did not hold any interest in the Property.

The trustee sued Daryl to sell the Property under § 363(h) and obtained entry of default. Instead of seeking default judgment in the adversary proceeding, however, the trustee moved to sell Guevarra's interest in the Property.[3] The trustee proposed to sell Guevarra's interest to Global Capital Concepts, Inc. for $32,000 subject to existing liens. The motion identified Guevarra as a joint tenant together with his nephew under the Grant Deed and disclosed a deed of trust against the Property.

Despite Guevarra's titled interest, the motion to sell disclosed that "if a Court of competent jurisdiction determines the bankruptcy estate did not have an interest in the Subject Property, the bankruptcy estate will refund the money paid by the Buyers." Though the trustee did not say why the estate might not have an interest in the Property, the motion discussed the trustee's strong-arm rights under the Bankruptcy Code. Specifically, the trustee argued that his status as a bona fide purchaser for value under § 544(a)(3) entitled the estate to sell its interest "free of a prior equitable interest or constructive trust interest."[4]

Guevarra's counsel obtained leave to file a late, terse six-sentence opposition to the sale motion without a declaration or other evidence. In it, Guevarra merely restated his position that he only was a co-signer on his

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nephew's home loan and therefore had no genuine economic interest in the Property. Rather than offer any analysis, the opposition advised that Guevarra would move to convert the case to chapter 13 and asked that the sale motion be continued so that it could be heard with the to-be-filed conversion motion. Guevarra's counsel filed the motion to convert the case to chapter 13 the day before the hearing on the trustee's motion to sell. The motion acknowledged that it was filed to "save his nephew's home."

At the sale hearing, the bankruptcy court noted Guevarra's argument that he did not have any interest in the Property and was merely a co-signer on the loan. The court observed that this argument was consistent with Guevarra's schedules but was otherwise unsupported by any evidence. Based on the deed and deed of trust, the court ruled that Guevarra's joint tenancy interest was estate property.

Though the recently filed motion to convert was not on the calendar, Guevarra's counsel advised the court of it and asked that the sale motion be continued to a date when both matters could be heard. The court responded that Guevarra did not have a right to convert his case because he had acted in bad faith by knowingly misstating his interest in the Property on the schedules. Responding to the issue of bad faith, Guevarra's counsel informed the court that "I produced proof to the trustee that he never made a down payment and doesn't live in the house and that the nephew's made every payment." The court replied, "[t]hat doesn't matter, he's on the title." Guevarra's counsel then offered to cite applicable cases on the issue, stating that he had previously provided them to trustee's counsel though they were not included in the opposition. The court did not accept the offer for supplemental briefing. In its findings of fact and conclusions of law approving the sale, the court found that Guevarra believed he was on title and "yet filed the schedules incorrectly stating he was a co-signer."

***3** The bankruptcy court approved the sale of Guevarra's interest in the Property to a competing bidder for $32,500. The court entered its sale order in December 2019, and the trustee closed the sale. Guevarra did not appeal either the sale order or the order denying his motion to convert.

In March 2020, Guevarra amended his schedules. By this time, Guevarra's counsel had been suspended from the practice of law. Guevarra filed his amended schedules pro se. In his amended Schedule A/B, he continued to list the value of his 50% interest in the Property as "$0.00." However, he described the nature of his ownership interest as: "Debtor interest in said property it [sic] was sold for $32,500 by chapter 7 trustee[.]" In the space provided for additional information, Guevarra put: "Debtor claims said funds under exemption statute CCP 703." In his amended Schedule C, Guevarra claimed $27,915 of these sale proceeds as exempt under California's "wild card" exemption.[5]

The trustee objected to Guevarra's amended exemption. According to the trustee, Guevarra had acted in bad faith and was equitably estopped from asserting the exemption claim. The trustee pointed out that Guevarra had insisted since the commencement of his chapter 7 case that he had no interest of value in the Property. The trustee additionally noted that it had taken Guevarra nineteen months from the commencement of his case to amend his schedules to claim the exemption in the Property (or its proceeds). The trustee explained that had he known Guevarra would claim an interest and an exemption in the proceeds he would not have sold the Property.

In support of the objection, the trustee filed the declaration of his counsel stating that he had spoken to Guevarra's counsel to discuss the ownership issue and requested documents. The trustee submitted his counsel's December 13, 2018 letter to Daryl informing him of the estate's interest in the Property based on the deed and deed of trust. The trustee also included the response from Guevarra's counsel dated December 19, 2018, committing to provide documents to establish that Guevarra never paid any money for the Property and never lived there, whereas Daryl paid all the monies owed on the Property including the down payment and lived there.

Guevarra opposed the objection in another terse document. As he explained, he never attempted to hide the Property from the trustee, and he correctly identified it in his original schedules. Guevarra explained that he changed his wild card exemption after the court ruled that he owned 50% of the Property. For the first time, he submitted case law to support his argument, citing *Johnson v. Johnson*, 192 Cal. App. 3d 551, 555-56, 237 Cal.Rptr. 644 (1987), *Siegel v. Boston (In re Sale Guaranty Corp.)*, 220 B.R. 660, 664 (9th Cir. BAP 1998), *aff'd*, 199 F.3d 1375 (9th Cir. 2000), and *Law v. Siegel*, 571 U.S. 415, 134 S. Ct. 1188, 188 L.Ed.2d 146 (2014). The *Johnson* and *Sale Guaranty* cases address California's recognition of resulting trusts. Specifically, these cases hold that a transferee of property who does not pay the purchase price for the real property "is presumed to hold the property in a resulting trust for the party who paid the consideration." *In re Sale Guar. Corp.*, 220 B.R. at 664; *Johnson*, 192 Cal. App.

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3d at 555-56, 237 Cal.Rptr. 644.

***4** Guevarra also submitted a declaration from Daryl in support of the opposition. Daryl's declaration was consistent with Guevarra's argument: his uncle only co-signed the home loan and was placed on title so that he (Daryl) could qualify for the loan. Daryl further stated that he and his wife had always lived in the home situated on the Property, that he always made the loan payments, and that he and Guevarra never intended for Guevarra to hold any interest of value in the Property.

The bankruptcy court denied the amended exemption without a hearing. The court ruled that California law requires exemptions to be claimed in good faith and to benefit the person taking the exemption. The bankruptcy court found that Guevarra claimed his wild card exemption for the improper purpose of protecting Daryl's property. Consequently, the bankruptcy court sustained the trustee's exemption claim objection.

On appeal, we vacated and remanded. We held that California's wild card exemption does not require debtors to harbor an intent to use the exempt property for any particular purpose. Rather, debtors were free to use property in which they claimed a wild card exemption for whatever purpose they saw fit.

Pertinent to the matter currently before us, we noted that California law presumes that a joint tenant who does not pay for real property holds bare legal title subject to a resulting trust. Citing *Johnson* and *Sale Guaranty*, we observed:

> Both cases involved resulting trusts. Under California law, if a transferee of property does not pay the purchase price for the property, the transferee is presumed to hold the property in a resulting trust for the party who paid the consideration for its purchase. Further, if a bankruptcy trustee has constructive notice of the resulting trust, it cannot be avoided under the trustee's strong-arm powers. But Debtor did not indicate on his schedules that he held the Property in a resulting trust, nor did he ever request any adjudication of these issues.

In re Guevarra, 2021 WL 1179619, at *2 n.4 (citations omitted).

We remanded the case to the bankruptcy court to consider the trustee's equitable estoppel argument. On remand, the bankruptcy court permitted the parties to file supplemental briefs. Guevarra, represented by new counsel, filed a supplemental brief that argued he was not the legal owner of the Property. As asserted in the supplemental brief, a resulting trust arose because Guevarra did not make any payments towards the purchase and had never lived on the Property. Guevarra filed his declaration to support his argument. Once again, he stated that he had never made any payments towards the purchase of the Property, never lived in it, and had always intended that it would be Daryl's property.

In his supplemental brief, the trustee argued that Guevarra should not be rewarded for his lengthy inaction in light of the trustee's costly administration of the asset. The trustee did not, however, dispute that Daryl lived on the Property, made all the payments on the loan, or that his uncle had merely intended to help him purchase his residence. Nor did he address the discussion of resulting trust cited in our decision remanding the matter and in Guevarra's supplemental briefing.

The bankruptcy court again ruled on the matter without argument. It sustained the objection to the amended exemption based on equitable estoppel. Guevarra timely appealed.

JURISDICTION

The bankruptcy court had jurisdiction under 28 U.S.C. §§ 1334 and 157(b)(2)(B). We have jurisdiction under 28 U.S.C. § 158.

ISSUE

***5** Did the bankruptcy court abuse its discretion when it applied equitable estoppel to sustain the trustee's objection to Guevarra's exemption claim?

STANDARD OF REVIEW

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[2]We review the bankruptcy court's decision whether to apply equitable estoppel for an abuse of discretion. *Parker v. Smith (In re Smith)*, BAP No. EC–16–1140–BJuTa, 2017 WL 1457942, at *4 (9th Cir. BAP Apr. 24, 2017) (citing *Leong v. Potter*, 347 F.3d 1117, 1121 (9th Cir. 2003)); *see also In re Guevarra*, 2021 WL 1179619, at *5 (citing California law and stating that the application of equitable estoppel is matter of discretion for the bankruptcy court).

[3]A bankruptcy court abuses its discretion if it applies an incorrect legal standard, or its factual findings are illogical, implausible or without support in the record. *TrafficSchool.com, Inc. v. Edriver Inc.*, 653 F.3d 820, 832 (9th Cir. 2011).

DISCUSSION

A. Law generally governing exemptions.

[4] [5]When a debtor files a chapter 7 petition, the debtor's legal and equitable interests in property as of the petition date become property of the bankruptcy estate, subject to the debtor's right to exempt certain property of the estate. *Schwab v. Reilly*, 560 U.S. 770, 774, 130 S.Ct. 2652, 177 L.Ed.2d 234 (2010). The Bankruptcy Code includes a list of federal bankruptcy exemptions but also permits states to "opt out" of the federal exemption scheme and offer their own list of exemptions. *Phillips v. Gilman (In re Gilman)*, 887 F.3d 956, 964 (9th Cir. 2018) (citing § 522(b)(2), (b)(3)(A), (d)).

[6] [7]California has opted out of the federal exemption scheme and permits its debtors only those exemptions allowable under state law. CCP § 703.130. As a result, though the bankruptcy court has jurisdiction to decide the merits of Guevarra's exemption claims, the allowance or disallowance of his claims is governed by California law. *In re Gilman*, 887 F.3d at 964 (citing *Diaz v. Kosmala (In re Diaz)*, 547 B.R. 329, 334 (9th Cir. BAP 2016)).

[8] [9]California exemptions are liberally construed in favor of the debtor. *Elliott v. Weil (In re Elliott)*, 523 B.R. 188, 192 (9th Cir. BAP 2014). And we must determine Guevarra's exemption rights as they existed on the date he filed his bankruptcy petition. *Wolfe v. Jacobson (In re Jacobson)*, 676 F.3d 1193, 1199 (9th Cir. 2012).

[10] [11] [12]Debtors in bankruptcy have a general right to amend their schedules, including their exemptions, at any time before the case is closed. Rule 1009(a). Bankruptcy courts have no equitable authority under federal law to restrict this right based on a perception of bad faith or prejudice to creditors. *Gray v. Warfield (In re Gray)*, 523 B.R. 170, 173-75 (9th Cir. BAP 2014) (citing *Law*, 134 S. Ct. at 1196-97). On the other hand, such equitable power might be derived from state law if state law provides an equitable basis for disallowing the amended exemption. *Id.* at 175 (citing *Law*, 134 S. Ct. at 1196-97).

Here, the bankruptcy court applied California equitable estoppel law to disallow Guevarra's amended wild card exemption. Guevarra challenges this application. Thus, we must consider the elements for applying equitable estoppel under California law and whether the bankruptcy court correctly determined that all the requisite elements were satisfied.

B. Equitable estoppel and exemption claims.

***6** [13] [14] [15]Both the Ninth Circuit and this panel generally have observed that equitable estoppel can be invoked to sustain objections to California exemptions. *In re Gilman*, 887 F.3d at 966; *In re Guevarra*, 2021 WL 1179619, at *5. When equitable estoppel is raised in an objection to an exemption, the objecting party bears the burden of proof to establish the elements of equitable estoppel. *In re Smith*, 2017 WL 1457942, at *5 (citing *Domarad v. Fisher & Burke, Inc.*, 270 Cal. App. 2d 543, 556, 76 Cal.Rptr. 529 (1969)); *see also Transp. Clearings-Bay Area v. Simmonds*, 226 Cal. App. 2d 405, 427–28, 38 Cal.Rptr. 116 (1964) (stating that "[t]he doctrine of estoppel must be applied strictly and established in every particular"). To successfully invoke equitable estoppel under California law, the objecting party must establish:

> "(a) a representation or concealment of material facts; (b) made with knowledge, actual or virtual, of the facts; (c) to a party ignorant, actually and permissibly, of the truth; (d) with the intention, actual or virtual, that the ignorant party act on it; and (e) that party was induced to act on it."

In re Guevarra, 2021 WL 1179619, at *5 (quoting *Simmons v. Ghaderi*, 44 Cal. 4th 570, 584, 80

Cal.Rptr.3d 83, 187 P.3d 934 (2008)).

Bankruptcy courts in California have applied equitable estoppel to deny exemptions in similar situations where a debtor amended exemptions after the bankruptcy estate administered an asset. In *In re Aubry*, 558 B.R. 333 (Bankr. C.D. Cal. 2016), the trustee reopened the debtor's case to administer a previously undisclosed annuity from which the debtor was receiving annual payments. Aubry did not amend her exemptions to exempt the annuity until after the trustee had recovered one of the annual annuity payments. She exempted the annuity nearly two years after she filed her bankruptcy and more than a year after the trustee had reopened her case. When her case was reopened, she had even amended her exemptions but had not exempted the annuity. *Id.* at 341-42.

The court held that Aubry was equitably estopped from claiming an exemption in the annuity. The court found that her failure to exempt the annuity when the trustee reopened and administered the undisclosed asset constituted a representation that she would not amend her exemptions. *Id.* at 346. It also held that her failure to exempt the annuity in a timely manner qualified as a concealment of her intent to exempt the annuity. *Id.* The court found that Aubry knew, or should have known, that she had the opportunity to exempt the annuity and her failure to do so would constitute knowledge that she was representing she would not exempt the asset. *Id.* at 346-47. It also held that the trustee had proven the remaining elements necessary to estop Aubry from amending her exemptions. *Id.* at 349-50.

A year after *Aubry,* the Ninth Circuit issued its unpublished decision in *Lua v. Miller (In re Lua),* 692 F. App'x 851, 852–53 (9th Cir. 2017), reversing the denial of an amended exemption based on equitable estoppel. In *Lua*, the debtor originally listed an interest in her residence as part of her schedules and exempted the interest under California's homestead exemption. She then amended her schedules to say that she "had no interest in the Property other than 'such community interest as may exist for the purposes of a divorce action.' " *In re Lua*, 529 B.R. 766, 769 (Bankr. C.D. Cal.), *aff'd*, 551 B.R. 448 (C.D. Cal. 2015), *rev'd and remanded*, 692 F. App'x 851 (9th Cir. 2017). The amended schedules stated that the residence was owned by her husband and two other members of his family. *Id.* In keeping with these amendments, Lua also amended her Schedule C to omit her prior homestead exemption. *Id.*

***7** The chapter 7 trustee spent almost three years litigating with Lua and her non-debtor husband to sell the residence. The court ultimately held the entirety of the residence was community property and ordered that it be turned over to the trustee. It was only after the trustee obtained an order compelling Lua to turn over possession of the residence that she finally vacated the property and permitted the trustee to sell it. *Id.* at 770-71. Roughly a month after Lua vacated the property, she filed her second amended schedules to claim a $100,000 homestead exemption under California law. *Id.* at 771.

The bankruptcy court held that Lua was equitably estopped from amending her exemption, and the district court affirmed. On appeal, the Ninth Circuit reversed. It explained that the debtor's first amended exemption "cannot form the basis of an estoppel because [it] set forth all of the existing facts known to Lua." 692 F. App'x at 852. The Ninth Circuit further found that "nothing in Lua's First Amended Schedules can be deemed a representation by Lua that she would not amend her exemptions again if circumstances changed." *Id.* at 853. The Ninth Circuit held that despite the trustee's administration of the residence, she was not equitably estopped from amending her exemption because her circumstances changed when "the bankruptcy court entered an order finding that the Property was 100% community property, providing Lua a new factual basis to claim a homestead exemption." *Id.*

[16]After *Lua,* the bankruptcy court in *In re Gonzalez*, 620 B.R. 296 (Bankr. C.D. Cal. 2019), also applied equitable estoppel to deny the debtor's amended homestead exemption. Gonzalez, a real estate broker, originally disclosed a residence and commissions held by his realty corporation. *Id.* at 302-04. Postpetition, Gonzales received and spent a significant amount of the outstanding commissions. The trustee informed Gonzalez that under California law he could exempt either the commissions under California's bankruptcy-like exemptions or the homestead under its general nonbankruptcy exemptions, but not both.[6] *Id.* at 304. After the trustee sued him for turnover of the commissions, Gonzalez amended his schedules to exempt roughly $28,000 in commissions under California's bankruptcy-like exemptions of CCP § 703.140(b). *Id.* at 305-06. Ultimately, the parties agreed that Gonzalez could exempt roughly $20,000 of the commissions and asked the court to decide whether the

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balance qualified as exempt tools of the trade. *Id.* at 306-07.

While the decision was pending, the trustee retained a real estate broker to sell Gonzalez's residence. Gonzalez did not object to the broker's employment but instead filed his third amended schedules to restate the value of his residence at a higher value and exempt the resulting equity under California's nonbankruptcy exemptions. *See* CCP § 704.010, *et seq.* The trustee objected to the homestead exemption. 620 B.R. at 308-09.

The bankruptcy court sustained the trustee's objection, holding that Gonzalez was equitably estopped from exempting the homestead. The court read *Lua* narrowly for the proposition that a debtor's omission of an exemption from her initial schedules did not by itself constitute a representation that she would not later amend her schedules to claim an exemption for purposes of equitable estoppel. *Id.* at 325. It pointed out that both the debtor and the trustee in *Lua* had access to the same set of facts. As a result, there could be no concealment of the true facts in that situation. *Id.* In contrast, the court noted that Gonzalez repeatedly advised the trustee that he affirmatively chose to elect the "bankruptcy-like" California exemptions under CCP § 703.140(b) to exempt his commissions to the exclusion of the homestead exemption available under the nonbankruptcy exemptions of CCP § 704.010, *et seq.* Additionally, it distinguished *Lua* by noting that Gonzalez did not involve a bona fide material change in circumstances that triggered his switch to the homestead exemption under California's non-bankruptcy exemptions. *Id.* at 325-26. Gonzalez's election and actions established the elements for equitable estoppel. *Id.* at 313-14, 319-20, 325-26.

***8** With these decisions in mind, we turn to the merits of the issue on appeal.

C. The bankruptcy court erred when it denied Guevarra's amended wild card exemption based on equitable estoppel.

[17] [18]"The doctrine of equitable estoppel is based on the theory that a party who by his declarations or conduct misleads another to his prejudice should be estopped from obtaining the benefits of his misconduct." *Cotta v. City & Cnty. of San Francisco*, 157 Cal. App. 4th 1550, 1567, 69 Cal.Rptr.3d 612 (2007) (quoting *Kleinecke v. Montecito Water Dist.,* 147 Cal. App. 3d 240, 245, 195 Cal.Rptr. 58 (1983)). Accordingly, the trustee was required to prove some misrepresentation or concealment of a material fact. *Vu v. Prudential Prop. & Cas. Ins. Co.,* 26 Cal. 4th 1142, 1149–1152, 113 Cal.Rptr.2d 70, 33 P.3d 487 (2001).

The bankruptcy court found that Guevarra had "concealed the 'wild card' exemption otherwise available to exempt his interest in the Property." The court explained that Guevarra did so by repeatedly declaring that he held no interest in the Property or that it was valueless, and by not taking the exemption in his original schedules. Guevarra's purported denial of any interest in the Property is the cornerstone of the trustee's argument to deny the amended exemption. It informs each element necessary to establish equitable estoppel. Therefore, we first address the denial of ownership before considering the court's finding that Guevarra concealed an intent to exempt his interest in the Property.

1. Guevarra's "representation" regarding his ownership interest.

[19] [20]Guevarra, or his counsel, indisputably stated on several occasions that he had no interest in the Property. But such statements were part of a broader, more nuanced resulting trust argument under California and bankruptcy law that Guevarra held bare legal title to the Property and held equitable title in trust for his nephew's benefit. Guevarra never articulated this argument to the court in such a direct manner until the supplemental briefing on equitable estoppel after our remand. But for purposes of equitable estoppel, when Guevarra presented his resulting trust theory to the court is largely irrelevant. Equitable estoppel focuses on the representation(s) to the party allegedly prejudiced. *See* *Simmons*, 44 Cal. 4th at 584-85, 80 Cal.Rptr.3d 83, 187 P.3d 934. Here, the relevant party is the trustee, and the record is clear that Guevarra early on informed the trustee, through his counsel, of the facts and law supporting the resulting trust argument.

Guevarra listed the Property in his original Schedule A/B, disclosing an interest in the Property. Though he provided a valuation of the Property, he valued his interest at zero. In the schedule, he explained that he merely co-signed on the loan for his nephew to acquire the Property. The record does not include what information, if any,

Guevarra provided the trustee at the meeting of creditors. So, we do not know what was asked, or said, about Guevarra's interest at that time. But the letter sent by the trustee's counsel afterwards reveals that Guevarra provided him with the Grant Deed which established Guevarra's joint tenancy interest.

More importantly, Guevarra never denied that the Grant Deed gave him a joint legal interest in the Property. Rather, he consistently argued that he had merely helped his nephew to purchase the Property. Guevarra maintained that his nephew wholly owned the Property despite the clear language of the Grant Deed. By December 2018, Guevarra's counsel had advised the trustee's counsel that the nephew had always lived at the Property and had made all the loan payments. Guevarra's counsel committed to sending the trustee proof to substantiate these facts, including Guevarra's rent for his residence at a different location.

***9** [21]Daryl's exclusive possession and payments were significant, material facts that Guevarra disclosed early and often to the trustee. These facts patently had the potential to drastically affect the nature of Guevarra's ownership under California law. As we recognized in our disposition of the trustee's bad faith argument, that Guevarra did not pay the purchase price for the Property triggered a presumption that he held his interest in a resulting trust for his nephew. *In re Guevarra*, 2021 WL 1179619, at *2 & n.4.

[22]A resulting trust under California law had the potential to prevent Guevarra's joint ownership from becoming property of the bankruptcy estate. *Id.* If Guevarra's joint interest in the Property was equitably held in trust for his nephew, he would be left with bare legal title. And bare legal title is effectively without value because the substantive equitable interest does not become property of the bankruptcy estate. § 541(d); *see also* *Mitsui Mfrs. Bank v. Unicom Comput. Corp. (In re Unicom Comput. Corp.)*, 13 F.3d 321 (9th Cir. 1994) ("[S]omething held in trust by a debtor for another is neither property of the bankruptcy estate under section 541(d), nor property of the debtor for purposes of section 547(b)."); *Savin v. Kafka (In re Kafka)*, Case No. 17-30013 HLB, 2018 WL 6132506, at *12 (Bankr. N.D. Cal. Nov. 21, 2018) (determining that debtor held bare legal title to the property and held interest in a resulting trust for the beneficial owners of the property); *Airwork Corp. v. Markair Express, Inc. (In re Markair, Inc.)*, 172 B.R. 638, 641-42 (9th Cir. BAP 1994) ("The resulting trust having been determined by law to exist, the trustee has no equitable rights in the trust, and the res is not property of the estate pursuant to § 541.").

The record does not reveal whether the trustee ever received the documentation promised by Guevarra's counsel. But the trustee's motion to sell demonstrates that the trustee fully understood the significance of Guevarra's argument. The trustee sought to sell Guevarra's joint interest in the Property based on the Grant Deed. Despite the clear existence of that interest, the trustee included considerable discussion about his strong-arm powers as trustee. The obvious purpose of this discussion was to show that the trustee's status as a bona fide purchaser for value under § 544(a)(3) could defeat any equitable interest Guevarra's nephew might have in his uncle's share of the Property. Given that the Grant Deed established their joint legal title, there was no reason for the trustee to include that discussion except to rebut Guevarra's argument that a resulting trust arose from his nephew's payments and possession of the Property. Indeed, the time records for the trustee's counsel show that he spent several hours researching constructive and resulting trusts before filing the motion to sell.

[23]We acknowledge that prior to his response to the trustee's exemption claim objection, Guevarra's terse arguments to the court never specifically and distinctly articulated his resulting trust theory. Instead, Guevarra only told the court he was a mere co-signer on the loan and that he made no payments for and did not live on the Property. But regardless of what the court understood at the time, there is no doubt as to what the trustee knew and understood at the time. In fact, at the sale motion hearing, the trustee did not dispute any of Guevarra's alleged facts regarding possession of and payments for the Property. Rather, he invoked his strong-arm powers under § 544(a)(3) and argued that his status as a bona fide purchaser for value could defeat any prior equitable interest. The trustee also argued that the trustee's actual knowledge of the facts was irrelevant. But as we recognized in our prior decision, under California law "if a bankruptcy trustee has constructive notice of the resulting trust, it cannot be avoided under the trustee's strong-arm powers." *In re Guevarra,* 2021 WL 1179619 at 2 n.4 (citing *In re Sale Guaranty Corp.,* 220 B.R. at 665-66).

***10** In short, there was no need for the trustee to invoke his strong-arm powers except as a means to respond to Guevarra's resulting trust argument. By that time, the trustee's discussions with Guevarra's counsel had made it clear to the trustee that Guevarra was asserting a resulting trust that limited his interest in the Property to bare legal title. The trustee's strong-arm powers may well have ultimately defeated Guevarra's resulting trust argument given the facts and circumstances of this case. *See*

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generally McGranahan v. Dillard (In re Dillard), Case No. 06-20596-A-7, 2007 WL 3237165 at *4 (Bankr. E.D. Cal. Oct. 30, 2007). But the ultimate outcome is not the issue. Whether or not successful, Guevarra's resulting trust argument, and the trustee's recognition of that argument, establishes that Guevarra did not merely deny his interest in the Property.

At bottom, no finder of fact reasonably could have found that Guevarra misled the trustee as to his ownership in the Property on the record before us. While Guevarra stated that he had no ownership interest of value, he explained the facts that created a presumption of a resulting trust under controlling law that supported his position. There was no misrepresentation of a material fact—only a dispute about the legal implications of those facts. Consequently, the bankruptcy court's finding that Guevarra knowingly misstated his ownership was clearly erroneous.

2. Guevarra's "concealment" of a present intent to exempt his interest in the Property.

[24]Though Guevarra's putative misrepresentation of his ownership of the Property predominated the trustee's objection to the amended exemption, the court found that Guevarra induced the trustee to sell his interest in the Property by concealing an intent to exempt that interest. The court cited Guevarra's repeated denials of his interest in the Property as evidence of this concealment. But as explained above, Guevarra disclosed his ownership interest and argued that it was not property of the estate, or was worthless, because he held bare legal title. Because he believed that he held bare legal title, his interest was valueless without the equitable interest which was not property of the estate. Accordingly, there was no practical reason for Guevarra to exempt bare legal title. Guevarra's resulting trust argument was consistent with his original decision not to exempt his interest in the Property.

In *Lua,* the Ninth Circuit rejected an argument similar to the trustee's present concealment argument. There, the debtor challenged her interest in real property for years based on her belief that she did not hold any community interest in her residence. The chapter 7 trustee in *Lua* had argued that her failure to take a homestead exemption was proof that she concealed her intent to exempt her residence. The Ninth Circuit held to the contrary that Lua's original schedules "cannot form the basis of an estoppel because they set forth all of the existing facts known to [the debtor]." *In re Lua,* 692 F. App'x at 852. Given a debtor's right to amend her schedules, including her exemptions, "nothing in Lua's First Amended Schedules can be deemed a representation by Lua that she would not amend her exemptions again if circumstances changed." *Id.* at 853.

The bankruptcy court attempted to distinguish *Lua.* It cited *Aubry* in support of its conclusion that Guevarra concealed his exemption "by omitting the exemption from the initial Schedules and thereafter testifying at the § 341 meeting that the initial Schedules were accurate." It also cited *Gonzalez* for the proposition that Guevarra had mislead the trustee by originally using the wild card to exempt "a Wells Fargo 401(k) bank account." Finally, it reasoned that like the trustee in *Aubry,* the trustee in Guevarra was harmed because he incurred considerable expense to sell the Property based on the debtor's choice not to exempt a valuable asset.

***11** [25]Though *Lua* is an unpublished decision, we find it persuasive and adopt its reasoning. The absence of an exemption for his interest in the Property in Guevarra's original schedules did not constitute a representation that he would not amend his exemption in the future. *In re Lua*, 692 F. App'x at 852-53; *see also In re Gilman*, 608 B.R. 714, 729 (Bankr. C.D. Cal. 2019) (following *Lua* and holding that the debtor's failure to disclose a prepetition escrow of a residence for sale in his initial schedules did not equitably estop the debtor from claiming an automatic homestead exemption in the residence), *aff'd*, 2020 WL 7087703 (C.D. Cal. Oct. 28, 2020). Nor are we persuaded that Guevarra's exemption of a 401(k) account under the wild-card exemption was meaningful as demonstrated by his subsequent amended exemption of the 401(k) account under the more applicable CCP § 703.140(b)(10)(E). In *Gonzalez* the debtor had the choice to exempt one of two assets under mutually exclusive exemptions. For whatever reason Guevarra originally decided to exempt his 401(k) account under the wild-card exemption, it did not preclude exemption under the more specific provision of CCP § 703.140(b)(10)(E).

Finally, Guevarra's case materially differs from *Aubry.* The trustee in *Aubry* incurred time and fees to administer an undisclosed annuity. For a year after discovery of the asset, the debtor did not challenge the estate's rights in the asset or exempt it despite filing amended exemptions when the case was reopened. Only after the trustee received an annual payment did the

debtor exempt the annuity. Here, as in *Lua,* the debtor challenged the estate's rights in the asset the estate sought to administer. Once Guevarra lost that challenge, his circumstances changed, and he was entitled to amend his exemption based on the court's decision to permit the estate to sell his interest in the Property. *In re Lua*, 692 F. App'x at 853 (holding that circumstances changed "when, at the request of the Trustee, the bankruptcy court entered an order finding that the Property was 100% community property, providing Lua a new factual basis to claim a homestead exemption"). Neither *Aubry* nor *Gonzalez* involved any legitimate change in circumstances that served as an impetus for the amended exemption. Rather, in both situations it was the trustee's administration of the nonexempt asset that prompted the belated exemption when it was available throughout the case. In contrast, the debtor in *Lua* and Guevarra both experienced bona fide changes in circumstances: the court's rejection of their respective legal positions that challenged whether the subject property was property of the estate.[7]

As in *Lua,* Guevarra provided the trustee with all the existing facts concerning his ownership. The parties merely disputed the legal significance of those facts. The trustee is not misled, and there is no concealment, where the parties disagree as to the legal significance of known facts. Nor can the trustee penalize a debtor for litigating his position, even when the debtor amends his or her exemptions if the debtor loses. Here, the court effectively disposed of Guevarra's resulting trust argument when it approved the sale of his interest in the Property. As a result of the court's decision, Guevarra's circumstances changed, and that change in circumstances provided him with a basis to claim an exemption he previously did not believe he had. Guevarra's situation was no different than the debtor in *Lua.* The record simply does not support any inference that Guevarra held a present intent to exempt a property interest that he believed was limited to bare legal title when he filed his original schedules and exemptions.

3. Given the absence of a misrepresentation or concealment, the other equitable estoppel elements also are absent.

***12** [26] [27]There being no misrepresentation of Guevarra's ownership, or concealment of a pre-existing intent to exempt his interest in the Property, the rest of the elements needed to establish equitable estoppel also fail. The trustee was required to prove that he was actually and permissibly ignorant of the truth. But "where the person pleading estoppel had knowledge of the facts, there is no reliance." *In re Lua*, 692 F. App'x at 852 (quoting *Sidebotham v. Robison,* 216 F.2d 816, 829 (9th Cir. 1954)). The trustee knew of Guevarra's interest under the Grant Deed as well as his resulting trust argument. And as a trustee he knew, or should have known, there was no need for Guevarra to exempt an interest that was limited to bare legal title because the estate did not have any beneficial interest in such property. *See* § 541(d) (providing that when debtor holds only legal title to property, no equitable interest in that property passes to the bankruptcy estate); *see also* *In re Markair, Inc.*, 172 B.R. at 641-42 (stating that trust res did not constitute estate property when the debtor had no equitable interest in the res to pass on to the trustee and the estate).

Similarly, the trustee is charged with knowing that if the court rejected Guevarra's resulting trust argument, Guevarra could amend his exemption in light of that ruling. *In re Gilman*, 608 B.R. at 729 ("[A] debtor's schedules cannot form the basis of an equitable estoppel claim because the parties are aware that the debtor may amend her schedules at any time."). That is exactly what happened here. As such, the trustee failed to establish that he was permissibly ignorant of either Guevarra's ownership or his ability to exempt that interest if the court rejected his resulting trust argument.

The record additionally provides no support for the court's findings that Guevarra induced the trustee to sell his interest while concealing an intent to exempt that interest. Based on the resulting trust argument, there was no need for Guevarra to exempt his interest if it was limited to bare legal title. That was the entire point of Guevarra's resulting trust argument: to prevent the trustee from selling his interest.

The bankruptcy court held that Guevarra intended to induce the trustee to sell his interest in the Property because he failed "to properly exempt his interest in the Property." In this instance, this amounts to nothing more than penalizing the debtor for raising an unsuccessful legal argument. The trustee was fully aware of Guevarra's argument, which was entirely consistent with his not exempting an interest that he argued was limited to bare legal title.

CONCLUSION

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[28] [29] [30] [31] [32]There is an obvious tension between the debtor's right to amend his exemptions and application of equitable estoppel. As we noted in our prior decision, we have interpreted *Law v. Siegel*, 571 U.S. 415, 134 S.Ct. 1188, 188 L.Ed.2d 146 (2014), "as overruling the bankruptcy court's authority to deny an exemption on grounds of bad faith." *In re Guevarra*, 2021 WL 1179619, at *4. Equitable estoppel is not a substitute for bad faith. Courts must be careful not to penalize debtors for exercising the statutory right to amend their exemptions or to read too much into a debtor's failure to exempt an asset. Without more, such an omission does not constitute a misrepresentation or concealment for purposes of equitable estoppel. Similarly, standing alone, the failure to exempt an asset does not impermissibly induce a trustee to administer an asset as he or she knows that debtors may amend their exemptions as a matter of right. Admittedly, this can place chapter 7 trustees in a tenuous position when faced with a valuable asset that the debtor has not exempted but could. Even so, we are not free to ignore the necessary implications of *Law v. Siegel* simply because they present a practical problem for chapter 7 trustees in administering estate assets.

As explained above, the record does not support the bankruptcy court's findings that Guevarra knowingly concealed his interest in the Property while the trustee was ignorant of that interest, or of Guevarra's right to amend his exemptions. Accordingly, we REVERSE the bankruptcy court's order sustaining the trustee's exemption claim objection based on the application of equitable estoppel.

All Citations

--- B.R. ----, 2022 WL 884595, 71 Bankr.Ct.Dec. 108

Footnotes

1 Unless specified otherwise, all chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101–1532, and all "Rule" references are to the Federal Rules of Bankruptcy Procedure.

2 We exercise our discretion to take judicial notice of the documents filed in Guevarra's bankruptcy case. *See* *Atwood v. Chase Manhattan Mortg. Co. (In re Atwood)*, 293 B.R. 227, 233 n.9 (9th Cir. BAP 2003).

3 After he succeeded in selling Guevarra's interest, the trustee voluntarily dismissed the adversary proceeding.

4 Counsel for the trustee submitted a fee application after the court approved the sale. His billing entries detail at least 3.3 hours researching Guevarra's interest in the Property and discussing the topic with the trustee. This included 1.8 hours researching constructive and resulting trusts.

5 Guevarra's amended Schedule C also still claimed a "wild card" exemption in his bank accounts, which he still valued at $310. As for his 401(k) account, he claimed that as exempt in his amended Schedule C under CCP § 703.140(b)(10)(E).

6 California permits bankruptcy debtors to choose either the bankruptcy exemptions of CCP § 703.140(b) or California's nonbankruptcy exemptions but not both. CCP § 703.140(a).

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7 We express no opinion whether omitting an asset completely from the debtor's schedules ever could be, by itself, sufficient grounds for equitable estoppel under California law.

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NOT FOR PUBLICATION
United States Bankruptcy Appellate Panel of the Ninth Circuit.

IN RE: Patrick Joseph GAVIN, Debtor.
Nimer Massis; Jennifer Nushwat, Appellants,
v.
Patrick Joseph Gavin, Appellee.

BAP No. NC-21-1130-SGB
|
Bk. No. 3:21-bk-30260
|
FILED March 14, 2022

Appeal from the United States Bankruptcy Court for the Northern District of California, Dennis Montali, Bankruptcy Judge, Presiding

Attorneys and Law Firms

Arasto Farsad, Farsad Law Office, P.C., San Jose, CA, for Debtor.

Justin C. Valencia, Office of the United States Trustee, Fresno, CA, for U.S. Trustee.

Before: SPRAKER, GAN, and BRAND, Bankruptcy Judges.

MEMORANDUM[*]

INTRODUCTION

***1** Debtor Patrick Joseph Gavin retained bankruptcy counsel over a weekend after receiving an adverse tentative ruling in a state court judgment enforcement action brought by creditors Nimer Massis and Jennifer Nushwat ("Creditors"). Gavin filed for chapter 13[1] relief to stay that proceeding and to prevent the tentative ruling from becoming a final decision. However, Gavin did not qualify for chapter 13, so he quickly sought to convert the case to chapter 11. Creditors opposed conversion, sought dismissal, and moved for sanctions against Gavin and his counsel. The bankruptcy court denied the motions to dismiss and for sanctions and converted the case. Creditors appeal those decisions.

None of Creditors' arguments persuade us that any of the bankruptcy court's rulings should be reversed. Therefore, we AFFIRM.

FACTS[2]

In 2019, Creditors were granted a state court default judgment for $77,778.25 against Gavin and his son for breach of contract. Creditors struggled to enforce the judgment and contend that Gavin actively resisted their collection efforts.[3] In furtherance of their collection efforts, Creditors in late 2020 and early 2021 sought to compel the sale of Gavin's real property located in Burlingame, California ("Burlingame Property"). Gavin opposed Creditors' effort and commenced a new lawsuit to challenge the default judgment and the underlying transaction alleging fraud.

On Friday, April 2, 2021, the state court issued a tentative ruling proposing to enter an order for the sale of the Burlingame Property. The hearing on the sale order application was set for the following Monday, April 5, 2021. Over the weekend, Gavin retained Arasto Farsad to file an emergency "skeletal" chapter 13 bankruptcy petition on Gavin's behalf. According to Farsad, Gavin had contacted him at the "last minute." Consequently, in order to protect and preserve Gavin's rights, and given the limited financial information he had received from Gavin at the time, he determined that filing the chapter 13 petition was the best course of action. Farsad filed Gavin's bankruptcy petition on Easter Sunday, April 4, 2021. As Farsad further explained:

> ***2** I had little to no possibility of access to the Debtor that weekend due to the holiday and also because the Debtor was / still is recovering from a recent surgery. It was quite difficult to both obtain and review the necessary documents in a careful manner in order to determine the Debtor's eligibility for a Chapter 13.

Farsad Decl. (April 9, 2021) at ¶ 2.

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The state court received notice of the bankruptcy filing. On Monday, April 5, 2021, the state court acknowledged the automatic stay and declined to enter an order for the sale of the Burlingame Property.

Less than a week after Gavin commenced his bankruptcy case, he moved to convert the case from chapter 13 to chapter 11. Farsad stated in his declaration in support of the motion that he filed the chapter 13 petition based on the exigent circumstances and limited information he was confronted with over the preceding weekend. With the opportunity to further review Gavin's financial situation over the next few days Farsad explained that he had determined Gavin exceeded the chapter 13 debt eligibility limits set forth in § 109(e). Accordingly, Gavin sought to convert his case to chapter 11 for the purpose of reorganizing his debts. Gavin noticed the conversion motion and provided the opportunity to request a hearing to the mailing matrix, which included Creditors' counsel.

Creditors opposed the conversion motion. They argued that Gavin's ineligibility for chapter 13 in violation of § 109(e) resulted in a void bankruptcy filing. Creditors considered Gavin's petition to be a nullity and of no legal effect. As a result, Creditors insisted that there was no pending bankruptcy case to convert. Creditors further maintained that the unauthorized emergency filing of a skeletal chapter 13 petition constituted an abuse of process.

Based on the opposition, Gavin noticed a hearing on the conversion motion for May 19, 2021.

On April 20, 2021, Creditors moved to dismiss the bankruptcy case and for annulment of the automatic stay. They simultaneously moved for sanctions under Rule 9011 against both Farsad and Gavin. Based on Farsad's admissions in his declaration in support of the conversion motion, Creditors argued that the skeletal filing of the chapter 13 petition for which Gavin was not eligible was done solely to stay the state court from issuing the sale order. Creditors maintained this constituted an abuse of process. They argued that this conduct justified dismissal of the bankruptcy case under § 1307(c), annulment of the automatic stay, and imposition of Rule 9011 sanctions.[4]

In further support of the sanctions motion, Creditors presented emails exchanged between their counsel, George Wynns, and Farsad on April 5 and 6, 2021, discussing the bankruptcy filing. Wynns advised Farsad in the first email that Gavin's secured debt greatly exceeded the § 109(e) limit and asserted that the bankruptcy case needed to be dismissed because Gavin was not eligible for chapter 13. Wynn also complained that the estimate of assets set forth in the petition as between "0 and $50,000" was obviously incorrect given the several encumbered parcels of real property Gavin owned. Farsad responded that because of the emergency nature of the filing he had not had the opportunity to follow his usual intake procedures and financial review. But he also stated that if Wynns was correct that Gavin exceeded the chapter 13 debt limits, he intended to move to convert the case to chapter 11.

***3** In the final email exchanged during that time, Wynns opined that there is no provision of the Bankruptcy Code permitting an emergency chapter 13 petition filing when the debtor is not qualified to file a chapter 13 petition under § 109(e). Wynns also provided specific information regarding Gavin's real property and the liens encumbering that property. According to Wynns, the secured debt exceeded $2,000,000.

Wynns further disagreed that the pending sale order qualified as an emergency. He pointed out that even if the sale order had been entered on April 5, 2021, no actual sale was imminent. Wynns stated his belief that any such sale would not have occurred for at least another one or two months because the Sheriff would have needed to receive the signed sale order and issue proper notice.

Wynns also executed a declaration in support of the sanctions motion. Wynns' declaration provided detailed information regarding the four parcels of real property Gavin owned and the numerous liens against those properties. He also detailed his efforts to enforce the Creditors' judgment against Gavin and how those judgment enforcement efforts directly led to the chapter 13 petition filing.

The motions to dismiss and for sanctions were scheduled to be heard together with Gavin's conversion motion on May 19, 2021.

On May 4, 2021, Gavin filed his schedules and statement of financial affairs ("SOFA") and a proposed chapter 13 plan. According to the schedules, Gavin had $6,687,280 in real property assets and $91,602 in personal property assets. He also listed $4,432,187 in secured debt, and $183,358 in general unsecured claims. His Schedule I listed $23,382 in monthly income and $6,280 in monthly expenses.

Gavin also opposed Creditors' motions. Gavin emphasized that he had no history of prior bankruptcy filings. And as soon as his counsel confirmed that his secured debt exceeded the eligibility limits for chapter 13,

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his counsel filed the motion to convert the case to chapter 11 within five days of his Easter Sunday emergency bankruptcy filing. Under these circumstances, Gavin maintained that he did not file for bankruptcy relief in bad faith and there was no cause for dismissal within the meaning of § 1307(c). According to Gavin, none of the traditional indicia of bad faith were present.

As for his opposition to the Rule 9011 sanctions motion, Gavin maintained that his emergency chapter 13 petition was neither frivolous nor filed for an improper purpose. Gavin insisted that given the time constraints, his counsel did the best he could with the limited financial information before him to file his bankruptcy petition under an appropriate chapter. Though the information included with the petition significantly undervalued Gavin's assets, he explained that his counsel did not intentionally underrepresent the value of his assets. According to Gavin, the petition preparation program automatically ticked the box for "0-$50,000" in assets because of the skeletal nature of his initial petition filing. Gavin observed that in the interim he had filed his schedules and SOFA, which contained more complete and more accurate financial information.

On May 18, 2021, the bankruptcy court entered an order taking all three matters off calendar and disposing of them without a hearing. The court granted the motion to convert and denied the motions to dismiss and for sanctions. According to the bankruptcy court, § 1307(d) specifically contemplated conversion to chapter 11 when debtors who initially file chapter 13 do not fall within § 109(e)'s debt limits.

***4** As for the motions to dismiss and for sanctions, the bankruptcy court denied them because the chapter 13 petition was filed under "pressing circumstances" — on the eve of the state court sale order hearing. The court rejected the argument that counsel's selection of the wrong chapter to file under was grounds for dismissal of the case or for sanctions given that counsel acted promptly to correct his error. The court also pointed out that Gavin made the corrections before Creditors suffered any prejudice or acted to their detriment. The court found particularly significant Creditors' inability to explain how they would have been in any more favorable situation if Gavin had originally filed a chapter 11 petition instead of mistakenly seeking relief under chapter 13.

On May 28, 2021, Creditors timely appealed.

JURISDICTION

The bankruptcy court had jurisdiction under 28 U.S.C. §§ 1334 and 157(b)(2)(A). We have jurisdiction under 28 U.S.C. § 158.[5]

ISSUES

1. Did the bankruptcy court abuse its discretion when it denied Creditors' dismissal motion?

2. Did the bankruptcy court abuse its discretion when it granted Gavin's conversion motion?

3. Did the bankruptcy court abuse its discretion when it denied Creditors' sanctions motion?

4. Did the bankruptcy court commit reversible error by deciding the matters on appeal without holding a hearing?

STANDARDS OF REVIEW

We review the bankruptcy court's order denying the dismissal motion for an abuse of discretion. *See Ellsworth v. Lifescape Med. Assocs., P.C. (In re Ellsworth)*, 455 B.R. 904, 914 (9th Cir. BAP 2011). We also review for an abuse of discretion the bankruptcy court's decision on Gavin's § 1307(d) motion to convert to chapter 11. *See In re Lester*, 409 B.R. 364, 371–72 (Bankr. W.D. Va. 2009). Orders regarding Rule 9011 sanctions likewise are reviewed for an abuse of discretion. *Fjeldsted v. Lien (In re Fjeldsted),* 293 B.R. 12, 18 (9th Cir. BAP 2003); *see also Cooter & Gell v. Hartmarx Corp.*, 496 U.S. 384, 405 (1990) ("an appellate court should apply an abuse of discretion standard in reviewing all aspects of a district court's [Civil] Rule 11 determination.").

The bankruptcy court abuses its discretion if it applies an incorrect legal rule or its factual findings are illogical, implausible, or without support in the record. *United States v. Hinkson*, 585 F.3d 1247, 1261–62 (9th Cir. 2009) (en banc).

Ordinarily, the bankruptcy court's assessment of the debtor's good faith or bad faith in filing a petition is a question of fact reviewed under the clearly erroneous standard. *Ho v. Dowell (In re Ho)*, 274 B.R. 867, 870 (9th Cir. BAP 2002). However, when the historical facts are undisputed and the bankruptcy court is called upon merely to determine whether the debtor's conduct

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amounts to good faith or bad faith, this Panel reviews the matter de novo as a mixed question of law and fact. *See Mendoza v. Curry (In re Duque)*, BAP No. CC-05-1069-MaMcB, 2005 WL 6960181, at *3 n.8 (9th Cir. BAP Dec. 30, 2005) (citing *Villanueva v. Dowell (In re Villanueva),* 274 B.R. 836, 840 (9th Cir. BAP 2002)).

DISCUSSION

A. The bankruptcy court did not abuse its discretion when it denied Creditors' motion to dismiss.

Creditors first argue that the bankruptcy court should have granted their motion to dismiss. The dismissal motion focused almost exclusively on Farsad's Easter Sunday petition filing and his admission within days that Gavin's secured debt exceeded § 109(e)'s eligibility limit. At the time of the filing, debtors could reorganize under chapter 13 only if they had less than $1,257,850 in secured debt. Because Gavin's secured debt substantially exceeded the allowed limit in chapter 13, Gavin had to file a motion to convert or dismiss. According to Creditors, these facts established that Gavin's petition filing was an abuse of the bankruptcy process and constituted cause for dismissal as a bad faith bankruptcy filing.

***5** A chapter 13 petition which is filed in bad faith may constitute "cause" for dismissal under § 1307(c). *Leavitt v. Soto (In re Leavitt)*, 171 F.3d 1219, 1224 (9th Cir. 1999); *Eisen v. Curry (In re Eisen)*, 14 F.3d 469, 470 (9th Cir. 1994). "To determine if a petition has been filed in bad faith courts are guided by the standards used to evaluate whether a plan has been proposed in bad faith." *In re Eisen*, 14 F.3d at 470. In making both determinations, a bankruptcy court needs to review the "totality of the circumstances." *Id.* However, cause under § 1307(c) does not mandate dismissal. Rather, courts still are required to consider whether dismissal or conversion is in the best interests of the creditors and the estate. *See Nelson v. Meyer (In re Nelson)*, 343 B.R. 671, 675 (9th Cir. BAP 2006). And though courts may not compel chapter 13 debtors to convert to chapter 11, § 1307(d) expressly provides such a right.

In *Leavitt*, the Ninth Circuit held that, when considering whether a chapter 13 case should be dismissed because it was filed in bad faith, the bankruptcy court should consider, among other factors:

> (1) whether the debtor misrepresented facts in his petition or plan, unfairly manipulated the Bankruptcy Code, or otherwise filed his chapter 13 petition or plan in an inequitable manner;
>
> (2) the debtor's history of filings and dismissals;
>
> (3) whether the debtor intended to defeat state court litigation; and
>
> (4) whether egregious behavior is present.

In re Leavitt, 171 F.3d at 1224 (cleaned up).

Creditors, here, contend that all of the *Leavitt* factors except for a history of bankruptcy filings and dismissals are met by Gavin's and Farsad's conduct. According to them, it is "obvious" from the course of events that the sole purpose of the bankruptcy filing was to defeat or impede Creditors' judgment collection efforts. As evidence, they point to the eleventh-hour bankruptcy filing, the decision to seek relief under chapter 13, Gavin's ineligibility for relief under that chapter, and the resulting motion to convert the case to chapter 11. From this, Creditors conclude that Gavin and Farsad unfairly manipulated the Bankruptcy Code, intended to defeat state court litigation, and engaged in egregious conduct. We disagree.

An eleventh-hour bankruptcy filing on the eve of a potentially decisive hearing in state court is not by itself sufficient to find bad faith. S*ee* *In re Ho,* 274 B.R. at 876 (bankruptcy court inappropriately dismissed chapter 13 case based on "the timing of Debtor's filing, just prior to the establishment of a trial date by the state court for the litigation"). Many bankruptcy cases are filed on the eve of adverse events such as foreclosure or the imminent entry of a judgment. Debtors do so for the financial breathing space that bankruptcy provides. This inherently delays the payment of creditors and alone is insufficient to sustain a finding of bad faith. As one bankruptcy court has explained:

> Filing a bankruptcy petition with the intent to frustrate creditors does not by itself establish an absence of intent to seek rehabilitation. Indeed, because a major purpose behind our bankruptcy laws is to afford a debtor some breathing room from creditors, it is almost inevitable that creditors will, in some sense, be "frustrated" when their debtor files

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> a bankruptcy petition. In reality, there is a considerable gap between delaying creditors, on the eve of foreclosure, and the concept of abuse of judicial purpose.

In re Marshall, 298 B.R. 670, 681 (Bankr. C.D. Cal. 2003) (quoting *Baker v. Latham Sparrowbush Assocs. (In re Cohoes Indus. Terminal, Inc.)*, 931 F.2d 222, 228 (2d Cir. 1991)). In other words, "[n]ot every 'litigation strategy' or delay caused by the filing of a Chapter 13 case constitutes cause for dismissal when the debtor demonstrates legitimate rehabilitative intent or underlying interests of creditors that might be served through the Chapter 13 case." Keith M. Lundin, Lundin on Chapter 13, § 152.5, at ¶ [7], LundinOnChapter13.com (last visited March 10, 2022) ("Lundin").

***6** Nor is the mistaken filing of the bankruptcy petition under chapter 13 specifically probative of bad faith under the totality of circumstances presented here. Contrary to Creditors' argument, Gavin was qualified to file for bankruptcy relief — just not under chapter 13. Creditors nonetheless insist that he misrepresented his eligibility for chapter 13. But for what purpose? There are degrees of misrepresentations. The bankruptcy court viewed Farsad's filing under the wrong chapter as an "innocent mistake." Not every mistake is nefarious.

Here, the court's finding that Farsad mistakenly placed Gavin into the wrong chapter is supported by the record. On a holiday weekend, Gavin represented to Farsad that pressing circumstances necessitated a bankruptcy filing without any meaningful opportunity for Farsad to review his financial situation. Additionally, Farsad corrected the mistaken filing within five days by filing the motion to convert the case to chapter 11. Finally, as the bankruptcy court observed, there is no evidence that Gavin gained any advantage by initially filing the petition under chapter 13, nor were Creditors harmed in any way by the filing under the wrong chapter. Significantly, Creditors have never explained why they would have been in any different or better position if Farsad had originally filed Gavin's skeletal petition as a chapter 11 petition.

We agree with the bankruptcy court that neither the timing of the filing of the petition, nor the mistaken decision to seek relief under chapter 13, are indicative in this instance of unfair manipulation of the Bankruptcy Code, an intention to defeat state court litigation, or egregious circumstances.[6] Creditors have not effectively challenged the underlying circumstances as found by the bankruptcy court. They simply attach deeper and sinister significance to these facts. But the prism through which they see these facts does not render the court's findings and inferences erroneous. Indeed, they are well supported by the record. Accordingly, we are not persuaded that the bankruptcy court abused its discretion by denying Creditors' motion to dismiss.

B. The bankruptcy court did not abuse its discretion when it granted Gavin's motion to convert.

Creditors next argue that because Gavin was ineligible to be a chapter 13 debtor, his bankruptcy petition was null and void. Thus, they believe that the bankruptcy court "lacked jurisdiction" over the matter. They argue that because Gavin did not qualify for chapter 13, there was no valid bankruptcy case to convert.

Several decisions have held that § 109(e) is jurisdictional. *See, e.g.*, *Ekeke v. United States*, 133 B.R. 450, 452 (S.D. Ill. 1991); *In re Wulf*, 62 B.R. 155, 158 (Bankr. D. Neb. 1986), *overruled by Rudd v. Laughlin*, 866 F.2d 1040, 1041 (8th Cir. 1989). These cases would seemingly support Creditors' argument. But the vast majority of decisions addressing the issue — including two from this panel — have concluded that § 109(e) is not jurisdictional. *See, e.g.*, *Duplessis v. Valenti (In re Valenti)*, 310 B.R. 138, 147–48 (9th Cir. BAP 2004) (citing *FDIC v. Wenberg (In re Wenberg)*, 94 B.R. 631, 637 (9th Cir. BAP 1988), *aff'd*, 902 F.2d 768 (9th Cir. 1990)); *see also In re Bello*, 609 B.R. 695, 703 (Bankr. E.D. Mich. 2019) (stating that when the chapter 13 debtor is determined to be ineligible under § 109(e), court still has the power either to dismiss the case or convert it to another chapter under the Code); Lundin, § 9.5, at ¶ [5] & n.10; § 146.1, at ¶ [5] & nn.9, 10 & 11 (listing additional cases). We view ourselves as bound by our prior decisions. *Salomon N. Am. v. Knupfer (In re Wind N' Wave)*, 328 B.R. 176, 181 (9th Cir. BAP 2005). Following *Valenti* and *Wenberg,* we hold that § 109(e) is not jurisdictional and that Gavin's ineligibility to be a chapter 13 debtor did not bar the bankruptcy court from converting the case to chapter 11.

***7** As a practical matter, prohibiting a bankruptcy court from exercising subject matter jurisdiction in a case where a debtor's eligibility is at issue would be unworkable in any chapter. More importantly, the non-jurisdictional nature of § 109(e) makes sense because the problem here is not with the bankruptcy filing but with the applicable chapter.[7]

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In sum, the Code, the relevant case law, and common sense, militate against Creditors' argument that the bankruptcy court lacked jurisdiction to convert Gavin's chapter 13 case to chapter 11. Consequently, we are not persuaded that the bankruptcy court abused its discretion by granting Gavin's conversion motion.

C. The bankruptcy court did not abuse its discretion when it denied Creditors' Rule 9011 sanctions motion.

Creditors additionally argue that the bankruptcy court erred when it denied their Rule 9011 sanctions motion. They claim that Farsad knew or should have known that Gavin did not qualify for chapter 13 based on his secured debt. Again, Creditors rely on Farsad's admission that he did not investigate Gavin's finances before deciding to file his chapter 13 case.

By filing the chapter 13 petition on Gavin's behalf, Farsad was certifying under Rule 9011(b): (1) that it was not filed for an improper purpose; (2) that the petition's legal contentions were warranted by existing law or by a nonfrivolous argument for a change to existing law; and (3) that the factual allegations in the petition had evidentiary support or were likely to have evidentiary support after a reasonable opportunity for investigation or discovery. See Rule 9011(b)(1)-(3); *see also* *Dressler v. The Seeley Co. (In re Silberkraus),* 336 F.3d 864, 870 (9th Cir. 2003) (describing nature of certifications).

When a party's Rule 9011 certifications turn out to be false, the bankruptcy court may impose sanctions, including reasonable attorney's fees and costs in bringing the sanctions motion. But the moving party must present evidence as to both frivolousness and improper purpose. *See* Rule 9011(c)(2); *In re Silberkraus*, 336 F.3d at 870 & n.5 (citing *Marsch v. Marsch (In re Marsch),* 36 F.3d 825, 830 (9th Cir. 1994)). A filing is frivolous if it is "both baseless and made without a reasonable and competent inquiry." *Townsend v. Holman Consulting Corp.*, 929 F.2d 1358, 1362 (9th Cir. 1990) (en banc). A bankruptcy filing is made for an improper purpose if it is filed "to harass or to cause unnecessary delay or needless increase in the cost of litigation." *In re Silberkraus*, 336 F.3d at 870 (quoting Rule 9011(b)). The assessment of these two factors is considered on a sliding scale "where the more compelling the showing as to one element, the less decisive need be the showing as to the other." *Id.* (quoting *In re Marsch*, 36 F.3d at 830).

***8** The bankruptcy court denied the motion for sanctions for the same reasons it overruled the objections to conversion: Gavin erroneously chose chapter 13 when he filed bankruptcy but promptly remedied that mistake without harm to Creditors. On appeal, Creditors again maintain that Gavin's admitted mistake compels reversal. In short, they focus on the baseless selection of chapter 13 while ignoring the other requirements for sanctions under Rule 9011.

As discussed above, Gavin did not file the *bankruptcy* in bad faith. Rather, he mistakenly selected chapter 13 when he was not qualified for that chapter. The prompt motion to convert to chapter 11 acknowledged and remedied that mistake. This is substantial evidence that it was a mistake resulting from the need to file the bankruptcy over a holiday weekend. An innocent mistake does not equate to an improper purpose. Creditors' sanctions motion failed wholly to establish an improper purpose.

The question regarding the propriety of Farsad's failure to select the appropriate chapter became a central issue, in large part, because Farsad quickly and candidly acknowledged that Gavin did not qualify for chapter 13. While Creditors established that Farsad's selection of chapter 13 was baseless, they also were required to prove that the filing was "made without a reasonable and competent inquiry." *Townsend*, 929 F.2d at 1362. As the plain language of Rule 9011(b) provides, a filer's certifications are made "to the best of the person's knowledge, information, and belief**, formed after an inquiry reasonable under the circumstances**." (Emphasis added.)

The reasonableness of Farsad's pre-filing inquiry must be measured against what a competent attorney hypothetically would have learned at the same time from a reasonable inquiry. *See* *Valley Nat'l Bank of Ariz v. Needler (In re Grantham Bros.)*, 922 F.2d 1438, 1442 (9th Cir. 1991); *see also* *Townsend*, 929 F.2d at 1364 ("whether a pleading is sanctionable must be based on an assessment of the knowledge that reasonably could have been acquired at the time the pleading was filed."). When an attorney must decide whether to file a paper but is confronted with significant time constraints, those time constraints must be considered in determining what constitutes a reasonable inquiry into the facts and the law. *See Homer v. Halbritter*, 158 F.R.D. 236, 238 (N.D.N.Y. 1994) (citing *Cooter & Gell*, 496 U.S. at 401–02).

Not all bankruptcy cases are created equally. As this case illustrates, debtors may wait until the last minute before

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contacting counsel to file bankruptcy. And debtors are allowed to file for bankruptcy with minimal documentation that must later be supplemented. *See* Rule 1007(a) and accompanying Advisory Committee Notes. Thus, in the context of bankruptcies filed under exigent circumstances, we have generally focused on showings of improper purpose in affirming sanctions orders under Rule 9011. *See McCandless v. U.S. Tr. (In re Carrera)*, BAP No. NC-15-1383-KiTaJu, 2016 WL 4400652, at *8 (9th Cir. BAP Aug. 16, 2016), *aff'd sub nom. Vizconde v. Burchard (In re Vizconde)*, 715 F. App'x 630 (9th Cir. 2017) (affirming sanctions orders where bankruptcy court found that emergency chapter 13 bankruptcy petitions were filed solely for the purpose of delay and with no intent to reorganize the debtors). Imposing Rule 9011 sanctions when debtors or their counsel file a bankruptcy petition without an improper purpose under exigent circumstances can carry with it the risk of chilling effective representation and zealous advocacy. *Cf. Radakovich v. Wilson (In re Radakovich)*, BAP No. WW–13–1254–KuPaJu, 2014 WL 4676009, at *5 (9th Cir. BAP Sept. 19, 2014).

***9** Creditors do not contest that courts must take into consideration the circumstances surrounding the filing when evaluating the reasonableness of counsel's inquiry under Rule 9011. Instead, they argue that there was no emergency. They believe that even if entry of the state court's sale order was imminent, the anticipated sale of the Burlingame Property was not.

Creditors apply an unduly strict reading of the exigent circumstances Farsad faced on Easter weekend in 2021. That Friday, the state court had advised it intended to enter an order to compel the sale of the Burlingame Property at the hearing on the sale motion set for that Monday. After receiving the tentative decision, Gavin contacted Farsad over the weekend to file bankruptcy before the hearing to stay that matter. The bankruptcy court found that the state court matter was pressing and treated it as exigent circumstances. The record supports this finding. Based on Gavin's desire to stay the state court action prior to entry of the order compelling the sale of the Burlingame Property, the court further found that Farsad "did not have sufficient time to obtain and review Debtor's financial documents before then." The record also supports these inferences. Indeed, one of Creditors' first emails to Farsad recognized that "Mr. Gavin was seeking to avoid an imminent court order by the San Mateo County Superior Court that would have ordered the sale of his real property ... in satisfaction of the judgment debt."

To be clear, we do not condone the filing of any case without sufficient investigation into a debtor's finances. But the Ninth Circuit has instructed that sanctions under Rule 9011 are measured using a sliding scale. In this instance there is no evidence that Gavin filed his bankruptcy, or selected chapter 13, for an improper purpose. On the other hand, he did not qualify for chapter 13. And the record is unclear as to exactly what investigation, if any, Farsad conducted before filing the petition with respect to Gavin's eligibility for chapter 13. Ordinarily, this would be substantial evidence supporting frivolousness and imposition of sanctions. But here, the bankruptcy court discounted that evidence in light of the pressing need to file the bankruptcy over the weekend and the evidence that Gavin was recovering from surgery.

It also bears comment that as the bankruptcy court found, Creditors were not harmed by the initial selection of chapter 13. Gavin and Farsad promptly acknowledged the mistake, converted the case to chapter 11, and have proceeded to reorganize. As Judge Jury noted in her concurrence in *Radakovich*, Rule 9011 states that a court **may** impose sanctions for a Rule violation, but it is not required to do so. *In re Radakovich,* 2014 WL 4676009, at *8 (Jury, J. concurring). The bankruptcy court had considerable discretion to consider the circumstances surrounding that mistake. Despite Farsad's error in filing Gavin's bankruptcy under chapter 13, the bankruptcy court found the absence of improper purpose sufficient to deny sanctions given the circumstances surrounding the failure to realize Gavin's ineligibility. This is not error or an abuse of discretion.

D. The bankruptcy court did not commit reversible error by not holding a hearing on the matters on appeal.

Finally, Creditors argue that the bankruptcy court should have held a hearing on the conversion, dismissal, and sanctions motions. They point out that the relevant Code sections governing the conversion and dismissal motions require "notice and a hearing." *See* § 1307(c), (d). Additionally, Rule 9011 motions qualify as contested matters and thus similarly require "reasonable notice and opportunity for hearing." *See* Rule 9014(a). Creditors believe that these notice requirements are jurisdictional and that the bankruptcy court's decision to decide the three motions without a hearing deprived them of due process. They are incorrect.

***10** In bankruptcy cases, adequate notice and adequate opportunity for hearing generally are flexible concepts that depend on the circumstances of the particular case.

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See § 102(1)(A).[8] This flexible approach to determining adequate notice and opportunity for hearing is consistent with the constitutional requirements of due process:

> [a]n elementary and fundamental requirement of due process in any proceeding which is to be accorded finality is notice reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections. The notice must be of such nature as reasonably to convey the required information and it must afford a reasonable time for those interested to make their appearance.

Mullane v. Cent. Hanover Bank & Tr. Co., 339 U.S. 306, 314 (1950) (citations omitted); *see also* *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976) ("The fundamental requirement of due process is the opportunity to be heard at a meaningful time and in a meaningful manner.").

Notwithstanding Creditors' arguments to the contrary, the standard for what amounts to constitutionally adequate notice is relatively minimal. Notice is constitutionally sufficient as long as it apprises the interested parties of the pending matter and affords them a reasonable opportunity to present their position. *Espinosa v. United Student Aid Funds, Inc.*, 553 F.3d 1193, 1202 (9th Cir. 2008) (citing *Mullane*, 339 U.S. at 314, 70 S. Ct. 652), *aff'd*, 559 U.S. 260 (2010).

Here, Creditors clearly had notice of Gavin's conversion motion and the opportunity to respond and file their own motions. In short, they complain that they were denied the opportunity to appear for oral argument. There is no indication that they sought an evidentiary hearing.[9] Nor have Creditors argued that there were any disputed material facts. Where the material facts are undisputed, no evidentiary hearing is required. *Caviata Attached Homes, LLC v. U.S. Bank, Nat'l Ass'n, (In re Caviata Attached Homes, LLC),* 481 B.R. 34, 45-46 (9th Cir. BAP 2012) (bankruptcy court properly dismissed chapter 11 case without conducting an evidentiary hearing where there were no disputed material facts).

Creditors fail to explain or demonstrate how the bankruptcy court's reliance on the parties' papers deprived them of a full and fair opportunity to be heard. Absent from the record is any indication of what they might have done differently. Creditors have not said what would have changed if the bankruptcy court had not disposed of the matters by its May 18, 2021 order but instead had waited until after the hearing scheduled for the next day to issue the same order.

***11** When, as here, there is no indication in the record that the absence of additional process prejudiced the litigants or otherwise deprived them of a fair opportunity to be heard, the decision on appeal cannot be reversed on due process grounds. *See* *Rosson v. Fitzgerald (In re Rosson)*, 545 F.3d 764, 776 (9th Cir. 2008), *partially abrogated on other grounds as recognized in Nichols v. Marana Stockyard & Livestock Mkt., Inc. (In re Nichols)*, 10 F.4th 956, 962 (9th Cir. 2021).

Accordingly, we reject as meritless Creditors' argument challenging the order on appeal based on an alleged lack of due process.

CONCLUSION

For the reasons set forth above, we AFFIRM the bankruptcy court's order granting Gavin's conversion motion and denying Creditors' dismissal and sanctions motions.

All Citations

Slip Copy, 2022 WL 768144

Footnotes

* This disposition is not appropriate for publication. Although it may be cited for whatever persuasive value it may have, *see* Fed. R. App. P. 32.1, it has no precedential value, *see* 9th Cir. BAP Rule 8024-1.

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1 Unless specified otherwise, chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101–1532. "Rule" references are to the Federal Rules of Bankruptcy Procedure, and "Civil Rule" references are to the Federal Rules of Civil Procedure.

2 We exercise our discretion to take judicial notice of documents electronically filed in Gavin's bankruptcy case. *See* *Atwood v. Chase Manhattan Mortg. Co. (In re Atwood)*, 293 B.R. 227, 233 n.9 (9th Cir. BAP 2003).

3 By way of example, Creditors obtained an assignment of rents order entitling them to collect rents from Gavin's rental properties, but they only managed to collect $4,600 before his bankruptcy filing. Creditors contend that in 2020 Gavin collected $99,480 in rents in violation of the state court's assignment of rents order. But Creditors did not present these allegations as part of their court papers in any of the three matters before the bankruptcy court, so we decline to consider them.

4 Because Creditors' appeal does not concern denial of stay annulment, there is no need for us to address that issue.

5 Arguably, all three rulings on appeal are interlocutory. To the extent they are, we hereby grant leave to appeal under Rule 8004(d) and the standards for granting leave to appeal enunciated in *Roderick v. Levy (In re Roderick Timber Co.)*, 185 B.R. 601, 604-05 (9th Cir. BAP 1995).

6 During oral argument, the parties confirmed that Gavin has currently proposed a plan that anticipates payment of all his creditors' claims in full, with interest, to which Creditors have not objected. As has been stated, "perhaps the best indicator of [a] Debtor's good faith" is his or her willingness to propose a plan that will treat his or her creditors fairly and equitably. *In re James*, 260 B.R. 498, 516 (Bankr. D. Idaho 2001); *see also* *In re Brown*, Case No. 05-49114, 2009 WL 565032, at *4-5 (Bankr. E.D. Tex. Mar. 5, 2009) (making similar observation); *In re Privitera*, Case No. 03-14601DWS, 2003 WL 21460027, at *1 n.8 (Bankr. E.D. Pa. June 12, 2003) ("The Debtor's performance in this bankruptcy case is the best evidence of his good faith in filing this petition.").

7 The bankruptcy court's subject matter jurisdiction derives from title 28 and not from any provision of title 11. And the plain language of title 28 specifically grants bankruptcy jurisdiction over *all* cases under title 11. 28 U.S.C. § 1334(a). This is so regardless of whether the debtor is eligible for relief under the particular chapter the petition is filed. Generally speaking, the appropriate remedy for a debtor's ineligibility under chapter 13 is dismissal or conversion, whichever is in the best interests of the creditors and the estate. *See generally* § 1307(c) (providing for dismissal or conversion to chapter 7 for "cause"). Alternately, § 1307(d) permits debtors such as Gavin to voluntarily convert their chapter 13 case to chapter 11 at their election.

8 In relevant part § 102(1)(A) (1) provides: "'after notice and a hearing', or a similar phrase ... means after such notice as is appropriate in the particular circumstances, and such opportunity for a hearing as is appropriate in the

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particular circumstances....”

9 When asked at oral argument on the appeal, Creditors’ counsel candidly conceded that he did not know whether they would have attempted to provide additional evidence. As the bankruptcy court took the hearings off calendar the day before they were scheduled for argument, this rings hollow. Regardless, Creditors have not identified any evidence that they were prevented from presenting to the bankruptcy court on any motion.

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United States Bankruptcy Appellate Panel of the Ninth Circuit.

IN RE: RS AIR, LLC, Debtor.
NetJets Aviation, Inc.; NetJets Sales, Inc.; NetJets Services, Inc., Appellants,
v.
RS Air, LLC, Appellee.

BAP No. NC-21-1227-BGT
|
Bk. No. 20-51604
|
Argued and Submitted on January 19, 2022 at Pasadena, California
|
APRIL 26, 2022

Synopsis
Background: Creditor appealed from orders of the United States Bankruptcy Court for the Northern District of California, M. Elaine Hammond, J., denying its objection to Chapter 11 debtor's Subchapter V election and later ruling upholding the eligibility decision in confirming the plan.

Holdings: The Bankruptcy Appellate Panel, Brand, J., held that:

[1] debtor was not required to be maintaining its core or historical operations on petition date to be eligible to proceed under Subchapter V of Chapter 11;

[2] profit motive was not required for debtor to be eligible to proceed under Subchapter V of Chapter 11;

[3] debtor, and not objecting party, had burden to prove eligibility to proceed under Subchapter V of Chapter 11;

[4] Bankruptcy Court's error in allocating burden to objecting creditor as to debtor's eligibility to proceed under Subchapter V of Chapter 11 was harmless, because debtor met its burden; and

[5] any error by Bankruptcy Court made in not considering exceptions to law of the case doctrine was harmless.

Affirmed.

Procedural Posture(s): On Appeal; Objection to Confirmation of Plan.

West Headnotes (16)

[1] Bankruptcy

Bankruptcy Court's interlocutory order denying creditor's objection to Chapter 11 debtor's Subchapter V election merged into the final confirmation order, for purposes of appeal.

[2] Bankruptcy

Question of whether a particular activity constitutes "commercial or business activities" for purposes of debtor's eligibility to proceed under Subchapter V of Chapter 11 is a legal question the Bankruptcy Appellate Panel (BAP) reviews de novo, and the bankruptcy court's determination whether debtor engaged in that particular activity is a factual question reviewed for clear error. 11 U.S.C.A. § 1182(1)(A).

[3] Bankruptcy

Bankruptcy court's factual findings are "clearly erroneous" if they are illogical, implausible, or without support in the record.

[4] Bankruptcy

Whether the bankruptcy court identified and applied the correct burden of proof is a question

of law the Bankruptcy Appellate Panel (BAP) reviews de novo.

[5] Bankruptcy

Bankruptcy Appellate Panel (BAP) reviews bankruptcy court's decision whether to apply law of the case doctrine for abuse of discretion.

[6] Bankruptcy

Bankruptcy court abuses its discretion if it applies wrong legal standard, or misapplies correct legal standard, or makes factual findings that are illogical, implausible, or without support in inferences that may be drawn from facts in record.

[7] Bankruptcy

Generally, a debtor is eligible to elect Subchapter V of Chapter 11 if the debtor: (1) is a "person"; (2) is engaged in commercial or business activities; (3) does not have aggregate debts in excess of the debt limit on the petition date; and (4) at least 50 percent of the debtor's debts arose from its commercial or business activities. 11 U.S.C.A. § 1182(1)(A).

[8] Bankruptcy

A limited liability company (LLC) is a "person," for purposes of determining debtor's eligibility to proceed under Subchapter V of Chapter 11. 11 U.S.C.A. § 1182(1)(A).

[9] Bankruptcy

Debtor need not be maintaining its core or historical operations on petition date to be eligible to proceed under Subchapter V of Chapter 11, but it must be presently engaged in some type of commercial or business activities. 11 U.S.C.A. § 1182(1)(A).

[10] Bankruptcy

Profit motive was not required for debtor to be eligible to proceed under Subchapter V of Chapter 11. 11 U.S.C.A. § 1182(1)(A).

[11] Bankruptcy

Debtor, and not objecting party, had burden to prove eligibility to proceed under Subchapter V of Chapter 11. 11 U.S.C.A. § 1182(1)(A).

[12] Bankruptcy

Bankruptcy Court's error in allocating burden to objecting creditor as to debtor's eligibility to proceed under Subchapter V of Chapter 11 was harmless, because debtor met its burden by demonstrating that it was engaged in commercial or business activities on the petition date, which was the only criterion challenged by creditor on eligibility. 11 U.S.C.A. §

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1182(1)(A).

[13] Bankruptcy

Doctrine of "law of the case" provides that court is generally precluded from reconsidering issue that has already been decided by same court, or higher court in identical case.

[14] Bankruptcy

To apply doctrine of law of the case, issue in question must have been decided either expressly or by necessary implication in previous disposition.

[15] Bankruptcy

Court may revisit previously resolved question when: first decision was clearly erroneous; intervening change in law has occurred; evidence on remand is substantially different; other changed circumstances exist; or manifest injustice would otherwise result.

[16] Bankruptcy

Any error by Bankruptcy Court made in not considering exceptions to law of the case doctrine in denying creditor's objection to Chapter 11 debtor's Subchapter V election and later ruling upholding the eligibility decision in confirming the plan was harmless, because no new evidence was presented at the final confirmation trial that the court should have considered or that would have changed the outcome.

Appeal from the United States Bankruptcy Court for the Northern District of California, M. Elaine Hammond, Bankruptcy Judge, Presiding

Attorneys and Law Firms

Kelly Singer of Squire Patton Boggs (US) LLP argued for appellants;

Jennifer C. Hayes of Finestone Hayes LLP argued for appellee.

Before: BRAND, GAN, and TAYLOR, Bankruptcy Judges.

OPINION

BRAND, Bankruptcy Judge:

INTRODUCTION

***1** Appellants NetJets Aviation, Inc., NetJets Sales, Inc., and NetJets Services, Inc. (collectively, "NetJets") appeal an order confirming the chapter 11[1] plan of debtor RS Air, LLC ("RS Air"). Specifically, NetJets appeals the bankruptcy court's prior order denying its objection to RS Air's subchapter V election, and the court's later ruling upholding the eligibility decision in confirming the plan.

NetJets argues that the bankruptcy court erred in determining that RS Air was eligible for subchapter V relief. According to NetJets, since RS Air had no profit motive, it was not "engaged in commercial or business activities" on the petition date pursuant to § 1182(1)(A).[2] NetJets argues that the bankruptcy court further erred by allocating the burden of proof to NetJets to establish that RS Air was not eligible for subchapter V. Finally, NetJets argues that the bankruptcy court erred in ruling that the

law of the case doctrine precluded the court from reconsidering RS Air's eligibility for subchapter V when new evidence at the final confirmation trial demonstrated that it was ineligible.

We hold that a profit motive is not required to satisfy § 1182(1)(A). We further hold that the burden is on the debtor to prove subchapter V eligibility. Although the bankruptcy court ruled otherwise on that issue, such error was harmless, because the record established that RS Air met its burden of establishing its eligibility to proceed under subchapter V. Finally, we conclude that any error the bankruptcy court made regarding its law of the case ruling was harmless, because no new evidence was presented at the final confirmation trial that the court should have considered or that would have changed the outcome. Accordingly, we AFFIRM.

FACTS

RS Air, a Delaware LLC doing business in California, was formed in 2001 by its sole member and manager, Stephen Perlman, for the purpose of using and providing aircraft transportation services, acquiring and selling interests in aircraft, and providing depreciation tax benefits to Perlman. From 2001 to 2017, RS Air's principal source of revenue from business operations was from providing flight services for Perlman and affiliated third parties and flying fragile technology prototypes to prevent damage from baggage handling on commercial flights. RS Air also obtained revenue from acquiring and selling fractional interests in aircraft.

***2** Beginning in 2001, RS Air entered into a series of agreements to purchase or lease from NetJets fractional interests in private jets. NetJets is a private business jet charter company that sells fractional jet interests, charter jet flight time, and aircraft management services. NetJets actively marketed depreciation tax benefits as a key benefit to fractional jet ownership.

The parties had a good business relationship until July 2017, when one of the jets fractionally owned by RS Air was involved in a non-injury runway crash, which RS Air contends NetJets failed to disclose and was caused by a NetJets pilot. RS Air ceased doing business with NetJets after the accident and was still not engaged in its normal flight operations when it filed for bankruptcy in November 2020. RS Air attributed its lack of operations to NetJets not allowing RS Air to use or sell any jets after the accident and the parties' falling out. Ultimately, the parties ended up in litigation in Ohio, with NetJets filing suit against RS Air for breach of contract and RS Air asserting counterclaims against NetJets for breach of contract and fraud.

B. The bankruptcy case and litigation over subchapter V eligibility

Just before trial was to begin in Ohio, RS Air filed a chapter 11 bankruptcy case and elected to proceed under subchapter V. NetJets is RS Air's largest, non-insider creditor and holds approximately 98% of the total non-insider debt.

1. Objection to subchapter V designation

NetJets objected to RS Air's election as a subchapter V debtor, arguing that RS Air was not eligible for subchapter V because it was not currently "engaged in commercial or business activities" pursuant to § 1182(1)(A). NetJets argued that RS Air had no flight operations since at least 2017, no revenue or income since as early as 2012, and no employees. In fact, argued NetJets, RS Air had never been a revenue-generating business, and its sole purpose was to serve as the intermediary through which Perlman acquired interests in and paid for the availability and use of private jets. NetJets argued that it was RS Air's burden to establish eligibility for subchapter V.

In opposition, RS Air argued that ongoing operations, employees, or historical profitability were not required for subchapter V eligibility. RS Air argued that it was currently engaged in business activities by (1) litigating with NetJets, (2) negotiating with NetJets to sell its fractional jet interests back to NetJets, (3) paying its aircraft registry fees, (4) remaining in good standing as a Delaware LLC, and (5) keeping its tax obligations current with the state of California and the federal government. RS Air also intended to resume normal flights operations with a different partner once able. RS Air argued that NetJets, as the movant, bore the burden of establishing that RS Air was not eligible for subchapter V.

The bankruptcy court overruled NetJets' objection to RS Air's subchapter V election ("Subchapter V Order"). First, it determined that NetJets, as the party challenging eligibility, had the burden to establish that RS Air was not eligible for subchapter V. Second, it found that RS Air was engaged in commercial or business activities on the

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petition date because RS Air: (1) transformed its business from flight services to investigation into and litigation with NetJets (its primary contractual party); (2) intended to resume fractional jet ownership with a different partner; (3) paid its aircraft registry fees; (4) remained in good standing as a Delaware LLC; and (5) filed its tax returns and paid taxes as required. The court rejected NetJets' argument that employees are required for eligibility, observing that many small businesses have no employees. Therefore, because NetJets did not meet its burden to establish that RS Air failed to satisfy the eligibility requirements of § 1182, RS Air would proceed as a subchapter V debtor.

2. RS Air's plan of reorganization

***3** At an earlier plan confirmation hearing, Perlman testified that, while some income is generated from providing flights to him or his related entities, RS Air would have no projected disposable income within the next five years, if ever. Instead, the primary financial benefit obtained is a tax deduction for aircraft depreciation that flows through Perlman. As a result, he would pay all administrative expenses and contribute new value of $50,000 (later increased to $100,000), which was more than the expected disposable income of $0.

At the final plan confirmation hearing, RS Air's financial expert testified that the net present value of RS Air's projected disposable income was $8,200. Because RS Air's value in a traditional disposable income analysis was projected to be a large negative number in the three- to five-year period postconfirmation, the financial expert created an alternative model to capture nontraditional kinds of value (e.g., tax benefits and aircraft flight services) that would not be included in a traditional analysis. The expert's alternative model recognized that RS Air was set up primarily to create value as a tax benefit from owning a fractional aircraft share and providing aircraft flight services, not to create value from profit on income.

In opposing confirmation, NetJets again argued that RS Air was not eligible for subchapter V, and therefore the Plan did not meet the good faith requirement of § 1129(a)(3). NetJets argued that RS Air was not a business with income, the expert's financial projections improperly included indirect items of value such as the depreciation tax benefit, and the expert's financial projections were based on non-GAAP and never-before-seen methodologies. NetJets contended that the real purpose of RS Air's subchapter V bankruptcy was to sustain a facade business with no operations or income to protect Perlman and affiliates and provide him with valuable tax benefits.

In confirming RS Air's third amended plan of reorganization (the "Confirmation Order"), the bankruptcy court found that the disposable income projections of Perlman and RS Air's financial expert were consistent with NetJets' argument that RS Air was not a business with income, but that whether RS Air generated income was not determinative for confirmation. The court decided that the law of the case doctrine precluded revisiting the issue of RS Air's subchapter V designation. However, the court noted that developing case law, which interpreted broadly the types of commercial or business activities that can satisfy § 1182(1)(A), supported its earlier decision that RS Air was engaged in commercial or business activities on the petition date. NetJets timely appealed the Confirmation Order, which included the prior Subchapter V Order. A motions panel granted NetJets' request for stay of the Confirmation Order pending appeal.

JURISDICTION

[1]The bankruptcy court had jurisdiction under 28 U.S.C. §§ 1334 and 157(b)(2)(L). We have jurisdiction under 28 U.S.C. § 158.[3]

ISSUES

1. Did the bankruptcy court err in determining that RS Air was "engaged in commercial or business activities" on the petition date?

2. Did the bankruptcy court err by allocating the burden to NetJets to prove that RS Air was not eligible for subchapter V?

***4** 3. Did the bankruptcy court abuse its discretion in determining that the law of the case doctrine precluded its review of the Subchapter V Order?

STANDARDS OF REVIEW

[2][3]The question of whether a particular activity constitutes "commercial or business activities" under §

1182(1)(A) is a legal question we review de novo, and the bankruptcy court's determination whether the debtor engaged in that particular activity is a factual question we review for clear error. *SeeInt'l Ass'n of Firefighters, Local 1186 v. City of Vallejo (In re City of Vallejo)*, 408 B.R. 280, 288-89 (9th Cir. BAP 2009) (we review questions of law and statutory interpretation of the Code de novo and the bankruptcy court's factual findings for clear error) (chapter 9 eligibility); *see alsoWatford v. Fed. Land Bank of Columbia*, 898 F.2d 1525, 1527 (11th Cir. 1990) (applying these standards of review to chapter 12 eligibility). Factual findings are clearly erroneous if they are illogical, implausible, or without support in the record. *Retz v. Samson (In re Retz)*, 606 F.3d 1189, 1196 (9th Cir. 2010).

[4]Whether the bankruptcy court identified and applied the correct burden of proof is a question of law we review de novo. *Boruff v. Cook Inlet Energy LLC (In re Cook Inlet Energy LLC)*, 583 B.R. 494, 500 (9th Cir. BAP 2018).

[5][6]We review the bankruptcy court's decision whether to apply the law of the case doctrine for an abuse of discretion. *See United States v. Lummi Indian Tribe*, 235 F.3d 443, 452 (9th Cir. 2000). A bankruptcy court abuses its discretion if it applies the wrong legal standard, or misapplies the correct legal standard, or makes factual findings that are illogical, implausible, or without support in inferences that may be drawn from the facts in the record. *SeeUnited States v. Hinkson*, 585 F.3d 1247, 1262 (9th Cir. 2009) (en banc).

DISCUSSION

A. The bankruptcy court did not err in determining that RS Air was "engaged in commercial or business activities" on the petition date.

[7][8]Under the Small Business Reorganization Act of 2019, commonly referred to as "subchapter V," Congress authorized eligible persons to avail themselves of streamlined chapter 11 bankruptcy relief designed to help small businesses.[4] Generally, a debtor is eligible to elect subchapter V if the debtor: (1) is a "person;"[5] (2) is "engaged in commercial or business activities;" (3) does not have aggregate debts in excess of the debt limit on the petition date; and (4) at least 50 percent of the debtor's debts arose from its commercial or business activities. § 1182(1)(A).

***5** The only question here is whether RS Air was "engaged in commercial or business activities" within the meaning of § 1182(1)(A). The Bankruptcy Code does not define the phrase and case law is sparse. With one exception, no appellate court has weighed in on the subject. The trial courts that have reviewed it are divided as to its meaning.

A majority of courts have held that a debtor need not be "actively operating" on the petition date, but must be "presently" engaged in commercial or business activities on the petition date to satisfy § 1182(1)(A). *See Nat'l Loan Invs., L.P. v. Rickerson (In re Rickerson)*, 636 B.R. 416, 424-25 (Bankr. W.D. Pa. 2021); *Lyons v. Family Friendly Contracting LLC (In re Family Friendly Contracting LLC)*, No. 21-14213-TJC, 2021 WL 5540887, at *3 (Bankr. D. Md. Oct. 26, 2021); *In re McCune*, 635 B.R. 409, 418–22 (Bankr. D.N.M. 2021); *In re Vertical Mac Constr., LLC*, No. 6:21-bk-01520-LVV, 2021 WL 3668037, at *2 (Bankr. M.D. Fla. July 23, 2021) ("operations" insinuates a fully functioning business but "activities" includes acts that are business in nature but fall short of an actual operating business); *In re Port Arthur Steam Energy, L.P.*, 629 B.R. 233, 236-37 (Bankr. S.D. Tex. 2021); *In re Blue*, 630 B.R. 179, 189-90 (Bankr. M.D.N.C. 2021); *In re Offer Space, LLC*, 629 B.R. 299, 305-07 (Bankr. D. Utah 2021); *In re Ikalowych*, 629 B.R. 261, 283-84 (Bankr. D. Colo. 2021); *In re Johnson*, No. 19-42063-ELM, 2021 WL 825156, at *6-8 (Bankr. N.D. Tex. Mar. 1, 2021); *In re Thurmon*, 625 B.R. 417, 422-23 (Bankr. W.D. Mo. 2020). Two courts have held that the debtor need not have been engaged in any commercial or business activities on the petition date to qualify for subchapter V, as long as the debtor was engaged in such activities at some point in the past. *See In re Blanchard*, No. 19-12440, 2020 WL 4032411, at *2 (Bankr. E.D. La. July 16, 2020) (finding that "engaged in" has no temporal limit); *In re Wright*, No. 20-01035-HB, 2020 WL 2193240, at *3 (Bankr. D.S.C. Apr. 27, 2020) (debtor need not be "currently" engaged in commercial or business activities on the petition date). Notably, those courts were two of the first to consider the issue.

[9]We agree with the majority, that the term "engaged in" is inherently contemporary in focus and not retrospective. Thus, a debtor need not be maintaining its core or historical operations on the petition date, but it must be "presently" engaged in some type of commercial or business activities to satisfy § 1182(1)(A).

The next question is, when a debtor is no longer operational, what types of "activities" satisfy the requirement that the debtor be engaged in commercial or business activities. In using the common meanings of the terms and other statutory construction methods, courts generally have held that the scope of commercial or business activities is very broad and apply a "totality of the circumstances" standard. *See* *In re Rickerson*, 636 B.R. at 425-26 (reasoning that "winding down" is a business activity and could be enough for § 1182(1)(A) but not deciding the issue because debtor's entities had been inactive for years prepetition, with no assets, no employees, no accounts, and the debtor had no intent to reactivate any of the entities); *In re Vertical Mac Constr., LLC*, 2021 WL 3668037, at *3 (concluding that maintenance of bank accounts, working with insurance adjusters and defense counsel to resolve claims, and selling assets all qualified as commercial or business activities); *In re Port Arthur Steam Energy, L.P.*, 629 B.R. at 237 (concluding that actively pursuing litigation against a third party, collecting outstanding accounts receivable, maintaining its facility, selling an asset, and filing tax returns all qualified as commercial or business activities); *In re Blue*, 630 B.R. at 190 (concluding that debtor was engaged in business activities by working as an IT consultant for a non-related entity and by winding down her former IT business); *In re Offer Space, LLC*, 629 B.R. at 306-07 (while debtor was no longer operating, had no employees, had no intention to reorganize, and intended to liquidate any remaining assets, debtor was engaged in commercial or business activities by having active bank accounts and accounts receivable, exploring counterclaims in a pending lawsuit, managing its stock, and winding down its business and taking steps to pay creditors and realize value for its assets); *In re Ikalowych*, 629 B.R. at 284-85 (concluding that the W-2 wage-earner debtor performing wind down work and dealing with tax accountants and tax issues for his defunct LLC qualified as commercial or business activities).

***6** Suffice it to say, courts are less likely to find sufficient commercial or business activities for purposes of § 1182(1)(A) where the debtor is an individual who owns a non-operating business, especially where the business has been dissolved under applicable state law. *See* *In re Rickerson*, 636 B.R. at 425-26 (concluding that individual whose entities had been inactive for years prepetition with no ongoing activity of any type and had no intent to reactivate any of the entities was not engaged in commercial or business activities); *In re Johnson*, 2021 WL 825156, at *7-8 (concluding that individual debtors were not engaged in commercial or business activities where husband's former companies were defunct and both debtors were now W-2 wage earners, even though husband was currently serving as president in a non-related business); *In re Thurmon*, 625 B.R. at 423 (concluding that individual debtors who sold their business prepetition, were retired, and did not intend to return to business were not engaged in commercial or business activities, and keeping their empty shell LLC in good standing and the existence of accounts receivable was insufficient).

The bankruptcy court found that RS Air was engaged in commercial or business activities on the petition date by litigating with NetJets, paying its aircraft registry fees, remaining in good standing as a Delaware LLC, and filing its tax returns and paying taxes. In addition, RS Air intends to resume fractional jet ownership and flight operations with a different partner once able. We conclude that the activities identified by the bankruptcy court are "commercial or business activities" within the meaning of § 1182(1)(A). And the bankruptcy court correctly found that RS Air was "engaged in" these activities on the petition date. While NetJets wishes to split hairs about the degree of RS Air's involvement in the Ohio litigation prior to and on the petition date, we do not view that factual issue as determinative.

NetJets argues that RS Air was not engaged in commercial or business activities either on or before the petition date because RS Air's activities lacked any motive to generate income or profit. NetJets contends that, to establish eligibility for subchapter V, the debtor must have a profit motive. Thus, the question is whether engaging in commercial or business activities incorporates a "pursuit of profit" requirement.

NetJets cherry-picks cases which it argues support its position that an eligible subchapter V debtor must have the intent to pursue profit. *In re Vertical Mac Constr., LLC*, 2021 WL 3668037, at *3 (noting that the term "commercial" is commonly understood to involve commerce, and includes "occupied with or engaged in commerce or work intended for commerce," "of or relating to commerce," and "viewed with regard to profit"); *In re Port Arthur Steam Energy, L.P.*, 629 B.R. at 236 (same); *In re Blue*, 630 B.R. at 189 (noting that "a person is engaged in commercial or business activities when she participates in the purchasing or selling of economic goods or services for a profit"); *In re Ikalowych*, 629 B.R. at 276 (holding that commercial or business activities means "any private sector actions related to buying, selling, financing, or using goods, property, or services, undertaken for the purpose of earning income"); *In re Johnson*, 2021 WL 825156, at

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*8 (a person engaged in commercial or business activities is "a person engaged in the exchange or buying and selling of economic goods or services for profit").

In addition to discussing the definition for the word "commercial," the courts above went on to discuss the definition for the word "business," which is defined as "a usually commercial or mercantile activity engaged in as a means of livelihood," or "dealings or transactions especially of an **economic nature**." *Business*, Merriam-Webster Online Dictionary, https://www.merriamwebster.com/dictionary/business (last visited Mar. 29, 2022) (emphasis added). Certainly, the depreciation tax benefits and the revenue generated by RS Air's flight operations or its acquiring and selling of its fractional aircraft interests are "dealings or transactions" of an "economic nature." Although NetJets tries to argue that no real tax benefit exists, that is contrary to its marketing strategy which touted tax benefits as a key advantage for fractional jet ownership.

***7** Further, NetJets fails to note that the *Ikalowych* court went on to observe that § 1182(1)(A) speaks only to whether the debtor was engaged in commercial or business activities – "not whether the [d]ebtor was making a profit, actively operating, or intending to operate in the future." 629 B.R. at 285. That court further heeded:

> Interpretation of statutory phrases can be aided by considering the definitions of each of the words in a phrase; but simply stringing separate dictionary definitions together is not enough and might lead in the wrong direction. Instead, the Court must consider context and purpose in applying definitions.

Id. at 278. The court in *Blue* was also careful not to limit the meaning of "commercial or business activities" to basic dictionary definitions. 630 B.R. at 188-89.

Finally, the issue of a "profit motive" was not directly addressed in these cases. The few courts that have addressed it have held that § 1182(1)(A) does not require a debtor to be engaged in for-profit business to qualify for subchapter V. In *Ellingsworth Residential Community Association*, 619 B.R. 519, 520 (Bankr. M.D. Fla. 2020), an unsecured creditor argued that the debtor – a nonprofit homeowners association – was not eligible for subchapter V because, as a nonprofit, it did not "engage in commercial or business activities." The bankruptcy court disagreed and found that, based on the plain and unambiguous language of the statute, no profit motive is required. *Id.* at 521. It went on to hold that the many commercial or business activities the nonprofit debtor engaged in fit the "broad" categorization of such activities. *Id.* (e.g., contracting for goods and services, hiring professionals, filing regular tax returns, collecting assessments from its homeowners).

On appeal, the district court affirmed. *Guan v. Ellingsworth Residential Cmty. Ass'n* (*In re Ellingsworth Residential Cmty. Ass'n*), No. 6:20-cv-1243-WWB, 2021 WL 3908525, at *3 (M.D. Fla. Aug. 19, 2021), *appeal dismissed*, No. 21-12970-AA, 2021 WL 6808445 (11th Cir. Nov. 4, 2021). The district court reasoned that, although corporations involved in commerce can, and frequently do, have a profit motivation, the plain and ordinary meaning of the terms "commercial or business activities" does not require it. For support, the district court cited to Black's Law Dictionary, which notes that "business activities" can be either "the carrying out of a series of similar acts for the purpose of realizing a pecuniary benefit, or otherwise accomplishing a goal." *Id.* (quoting *Doing Business*, Black's Law Dictionary (11th ed. 2019)). This broad definition would include not-for-profit businesses, and would not be limited to those having only a benevolent purpose.

The bankruptcy court in *Family Friendly Contracting LLC* also concluded that the plain and ordinary meaning of "commercial or business activities" does not require a profit motivation. 2021 WL 5540887, at *3. In so ruling, the court observed that courts have interpreted the phrase broadly in keeping with the SBRA's purpose and the language of § 1182(1)(A).

We note, and the *Ellingsworth* and *Family Friendly* courts observed, Congress chose not to exclude nonprofits or other persons who lack a profit motive from qualifying for subchapter V. And that makes sense, because churches, hospitals, and other nonprofit businesses are allowed to file for chapter 11 (or 7) relief. *SeeJBB Holdings, LLC v. Abundant Life Worship Ctr. of Hinesville, GA, Inc. (In re Abundant Life Worship Ctr. of Hinesville, GA, Inc.)*, No. 20-40959-EJC, 2020 WL 7635272, at *10 n.23 (Bankr. S.D. Ga. Dec. 16, 2020) (a church or other nonprofit entity can be a small business debtor) (citing *In re Ellingsworth Residential Cmty. Ass'n*, 619 B.R. at 521-22); *In re Charles St. African Methodist Episcopal Church of Bos.*, 478 B.R. 73 (Bankr.

D. Mass. 2012) (religious corporation's nonprofit status did not disqualify it as a "corporation" eligible for chapter 11); *see also* § 101(27A) defining "health care business" to include an entity "organized for profit or not for profit"); 2 COLLIER ON BANKRUPTCY ¶ 109.02 (Alan N. Resnick & Henry J. Sommer, eds. 16th ed. rev. 2021) ("a nonprofit corporation, like a for-profit corporation, is eligible to file for relief under the Code"). The only persons Congress excluded from subchapter V eligibility (other than by debt limitations) are those whose primary activity is the business of owning single asset real estate, corporate debtors subject to reporting requirements under certain sections of the Securities Exchange Act (15 U.S.C. §§ 78m or 78*o*(d)), or any debtor that is an affiliate of an issuer under 15 U.S.C. § 78c. *See* § 1182(1)(A) & (B).

***8**[10]Accordingly, we conclude that no profit motive is required for a debtor to qualify for subchapter V relief. To hold otherwise would wrongfully exclude nonprofits and other persons that lack such a motive. That RS Air had no profit motive did not render it ineligible for subchapter V.

B. The bankruptcy court erred by allocating the burden to NetJets to prove that RS Air was not eligible for subchapter V.

The parties dispute who had the burden of proof as to RS Air's subchapter V eligibility: RS Air or NetJets. The Bankruptcy Code and Rules are silent on this issue. The bankruptcy court determined that NetJets, as the party challenging eligibility, had the burden. NetJets contends this was error. We agree.

The bankruptcy court rejected the Missouri bankruptcy case cited by NetJets – *In re Thurmon* – as contrary to Ninth Circuit law. *Thurmon* held, based on Eighth Circuit law, that the debtor has the burden to establish subchapter V eligibility. 625 B.R. at 419 n.4. The bankruptcy court believed it was bound by *Scovis v. Henrichsen (In re Scovis)*, 249 F.3d 975 (9th Cir. 2001), which it cited for the proposition that the party challenging chapter 13 eligibility under § 109(e) bears the burden of proof. However, *Scovis* made no express, or even implied, ruling as to who has the burden of proof for establishing eligibility under § 109(e) outside of the context of plan confirmation. The bankruptcy court also relied on BAP cases involving motions to dismiss under § 707 and § 1112. *See Aspen Skiing Co. v. Cherrett (In re Cherrett)*, 523 B.R. 660, 668 (9th Cir. BAP 2014) (movant bears the burden to establish abusive chapter 7 filing under § 707(b)(1)); *Sullivan v. Harnisch (In re Sullivan)*, 522 B.R. 604, 614 (9th Cir BAP 2014) (movant bears the burden to establish "cause" for dismissal of chapter 11 case under § 1112(b)).

Neither this Panel nor the Ninth Circuit Court of Appeals has decided the issue of who has the burden on subchapter V eligibility. However, in an objection to the debtor's eligibility for chapter 9 relief, we held that the debtor has the burden of establishing eligibility under § 109(c). *In re City of Vallejo*, 408 B.R. at 289 (citing *In re Valley Health Sys.*, 383 B.R. 156, 161 (Bankr. C.D. Cal. 2008)). Other circuit courts, as well as courts within this circuit, have held that the debtor has the burden of establishing eligibility for chapter 12 relief under § 109(f). *See First Nat'l Bank of Durango v. Woods (In re Woods)*, 743 F.3d 689, 705 (10th Cir. 2014) (citing cases); *Tim Wargo & Sons, Inc. v. Equitable Life Assurance Soc'y of the U.S. (In re Tim Wargo & Sons, Inc.)*, 869 F.2d 1128, 1130 (8th Cir. 1989); *Baker v. Rosenberger (In re Rosenberger)*, No. 20-50093, 2020 WL 6940926, at *3 (Bankr. W.D. Va. Sept. 29, 2020) (debtor must put forward sufficient evidence to allow the court to find that she satisfies § 109(f) eligibility requirements, including the definitional § 101(18) requirement that she was "engaged in a farming operation" on the petition date); *In re Cooper*, No. 10-66447-fra12, 2011 WL 3882278, at *1 (Bankr. D. Or. Sept. 2, 2011); *In re Powers*, No. 10-14557, 2011 WL 3663948, at *1 (Bankr. N.D. Cal. Aug. 12, 2011) ("The party filing a petition under Chapter 12 bears the burden of proving eligibility."); *In re Pandol*, No. 10-19733-B-12, 2010 WL 9488147, at *1 (Bankr. E.D. Cal. Sept. 29, 2010) (debtor has the burden to establish that he is a "family farmer"). Finally, in involuntary cases, our circuit places the burden of proving eligibility on the petitioning creditors. *Cunningham v. Rothery (In re Rothery)*, 143 F.3d 546, 548 (9th Cir. 1998) ("The filing of an involuntary case requires the petitioning creditor to meet the burden of proof on the main elements under § 303."); *Hayden v. QDOS, Inc. (In re QDOS, Inc.)*, 607 B.R. 338, 343 (9th Cir. BAP 2019).

***9**[11]The reasoning of the courts placing the burden on the debtor to establish eligibility for relief in a chapter 12 case is persuasive for our purposes here, considering that chapter 12 contains the analogous requirement that a "family farmer" be "engaged in a farming operation" to be eligible. *See* § 101(18). Nearly every court deciding the issue of who bears the burden of proving eligibility for subchapter V has held that it is the debtor. *See In re Rickerson*, 636 B.R. at 422; *In re Family Friendly*

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Contracting LLC, 2021 WL 5540887, at *2; *In re Vertical Mac Constr.,* 2021 WL 3668037, at *2; *In re Port Arthur Steam Energy, L.P.*, 629 B.R. at 235; *In re Blue*, 630 B.R. at 187; *In re Offer Space, LLC*, 629 B.R. at 304; *In re Ikalowych*, 629 B.R. at 275; *In re Sullivan*, 626 B.R. 326, 330 (Bankr. D. Colo. 2021); *In re Johnson*, 2021 WL 825156, at *4; *In re Thurmon*, 625 B.R. at 419 n.4; *In re Blanchard*, 2020 WL 4032411, at *2; *In re Wright*, 2020 WL 2193240, at *2; *but see* *In re Body Transit, Inc.*, 613 B.R. 400, 409 n.15 (Bankr. E.D. Pa. 2020) (objecting party is the de facto moving party bearing the burden to prove the debtor is not entitled to subchapter V relief); *Hall L.A. WTS, LLC v. Serendipity Labs, Inc. (In re Serendipity Labs, Inc.)*, 620 B.R. 679, 680 n.3 (Bankr. N.D. Ga. 2020). We agree with the majority view and hold that the burden to prove eligibility for subchapter V should be placed on the debtor, especially considering the many advantages subchapter V offers debtors over a "traditional" chapter 11: total plan exclusivity (including modifications) and no disclosure statement requirement; the ability to obtain a discharge on the effective date; and the inapplicability of the absolute priority rule. It also makes sense to place the burden on the debtor because debtors are in the best position to prove that they are qualified to be in subchapter V.[6]

[12]Nevertheless, the bankruptcy court's error in allocating the burden to NetJets in the objection to eligibility was harmless because RS Air met its burden. RS Air demonstrated that it was engaged in commercial or business activities on the petition date, which was the only criterion challenged by NetJets on eligibility.

C. The bankruptcy court failed to recognize the exceptions to the law of the case doctrine, but such error was harmless.

[13][14][15]The doctrine of law of the case provides that a "court is generally precluded from reconsidering an issue that has already been decided by the same court, or a higher court in the identical case." *Thomas v. Bible*, 983 F.2d 152, 154 (9th Cir. 1993). To apply, "the issue in question must have been decided either expressly or by necessary implication in the previous disposition." *Id.* (cleaned up). But there are exceptions to this discretionary doctrine. A court may revisit a previously resolved question when: (1) the first decision was clearly erroneous; (2) an intervening change in the law has occurred; (3) the evidence on remand is substantially different; (4) other changed circumstances exist; or (5) a manifest injustice would otherwise result. *Id.* at 155 (citations omitted).

NetJets argues that the bankruptcy court abused its discretion by applying law of the case to its earlier ruling that RS Air was eligible for subchapter V, when new evidence presented at the final confirmation hearing defeated RS Air's eligibility. NetJets argues that the bankruptcy court failed to consider new evidence that: (1) RS Air had not reported any income since at least 2004; (2) Perlman's alleged tax benefit flowing from his ownership of RS Air was not a benefit and but rather a loss because the cost of producing the benefit exceeded the amount of the tax benefit itself; (3) the financial model supporting RS Air's income calculations treated expenses as "income," did not comply with GAAP, and was inconsistent with the definition of "disposable income" under the Code; and (4) RS Air's disposable income would be negative using a strict definition of "disposable income." NetJets contends that the bankruptcy court's decision was particularly egregious because the subchapter V designation was an interlocutory ruling. *See* *Amarel v. Connell*, 102 F.3d 1494, 1515 (9th Cir. 1996) (interlocutory orders are subject to modification at any time prior to final judgment); *Hydranautics v. FilmTec Corp.,* 306 F. Supp. 2d 958, 968 (S.D. Cal. 2003) (court may reconsider and revise an interlocutory decision for any reason, even absent new evidence or an intervening change in the law).

***10**[16]The problem facing NetJets is that all of the alleged new evidence it argues that the bankruptcy court should have considered relates to the fact that RS Air had no net profit. As we stated above, a profit motive or net profit is not required for subchapter V eligibility. In addition, much of this evidence was not "new." In overruling NetJets' initial objection, the bankruptcy court found that RS Air was created to receive a depreciation tax benefit marketed by NetJets rather than to generate a net profit. At a prior confirmation hearing, Perlman testified that RS Air would likely have no projected disposable income within the next five years, if ever. We also find it somewhat disingenuous for NetJets to complain about this purported new evidence that was consistent with its long-standing argument that RS Air was not a business with income, and consistent with RS Air's position that jet share ownership's primary business value is a tax benefit, not income. Accordingly, any failure by the bankruptcy court in not considering the exceptions to law of the case was harmless error.

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CONCLUSION

For the reasons stated above, we AFFIRM both the Subchapter V Order and the Confirmation Order.

All Citations

--- B.R. ----, 2022 WL 1288608

Footnotes

1 Unless specified otherwise, all chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532.

2 As relevant here, § 1182(1)(A) provides that the term "debtor" "means a person engaged in commercial or business activities ... that has aggregate noncontingent liquidated secured and unsecured debts as of the date of the filing of the petition or the date of the order for relief in an amount not more than $7,500,000 (excluding debts owed to 1 or more affiliates or insiders) not less than 50 percent of which arose from the commercial or business activities of the debtor." NetJets does not challenge RS Air's eligibility based on debt limits.

3 The interlocutory Subchapter V Order merged into the final Confirmation Order. *See* *United States v. Real Prop. Located at 475 Martin Lane*, 545 F.3d 1134, 1141 (9th Cir. 2008) (under merger rule, interlocutory orders entered prior to the judgment merge into the judgment and may be challenged on appeal).

4 The SBRA became effective on February 19, 2020. *See*11 U.S.C. §§ 1181, et seq. Small Business Reorganization Act of 2019 (HR 3311), Pub. L. No. 116-54, 133 Stat. 1079 (Aug. 23, 2019). The statute as originally enacted defined the debtor under § 101(51D), in the same way as a small business debtor who does not elect to proceed under subchapter V. As part of the Coronavirus, Aid, Relief, and Economic Security Act (HR 748), Pub. L. No. 116-136, 134 Stat. 281, 116th Cong. 2d Sess. (Mar. 27, 2020), the definition was changed to temporarily increase the debt limit to $7,500,000 for debtors who elected subchapter V and included a sunset of one year. The one-year sunset for this temporary amendment was extended to March 27, 2022, by the COVID-19 Bankruptcy Relief Extension Act of 2021, Pub. L. No. 117-5 (Mar. 27, 2021). In this case, § 1182(1)(A) applies for the definition of a subchapter V debtor.

5 An LLC is a "person." *Gilliam v. Speier (In re KRSM Props., LLC)*, 318 B.R. 712, 717 (9th Cir. BAP 2004).

6 We note the case of *Ho v. Dowell (In re Ho)*, 274 B.R. 867 (9th Cir. BAP 2002), cited by RS Air. The thrust of that case was a debtor's eligibility to proceed under chapter 13 given the debt limits set by § 109(e). The concurrence noted that a creditor has the burden to persuade the court to grant a motion to dismiss a chapter 13 case for § 109(e) ineligibility, whereas the debtor has the burden of demonstrating § 109(e) eligibility for purposes of plan confirmation. *Id.* at 882-83. The majority did not comment on this issue. In any case, we are not bound by *Ho*. The statement is dicta in a concurrence. Further, the bankruptcy court's ruling on RS Air's subchapter V eligibility was not in the context of a motion to dismiss where one might expect the movant to have the burden.

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2022 WL 1198232
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NOT FOR PUBLICATION
United States Bankruptcy Appellate Panel of the Ninth Circuit.

IN RE: BCB CONTRACTING SERVICES, LLC, Debtor.
Brian K. Stanley, Appellant,
v.
Anthony H. Mason, Chapter 7 Trustee; Payam D. Khoshbin, Appellees.

BAP No. AZ-21-1254-BSF
|
Bk. No. 2:19-bk-15555-DPC
|
FILED APRIL 21, 2022

Appeal from the United States Bankruptcy Court for the District of Arizona, Daniel P. Collins, Bankruptcy Judge, Presiding

Before: BRAND, SPRAKER, and FARIS, Bankruptcy Judges.

MEMORANDUM[*]

INTRODUCTION

***1** Appellant Brian K. Stanley appeals an order sanctioning him under Rule 9011[1] and § 105(a).[2] Stanley was the attorney for the debtor, BCB Contracting Services, LLC ("Debtor"). The bankruptcy court found that the chapter 7 petition Stanley filed on behalf of Debtor was frivolous and filed for an improper purpose and that Stanley engaged in bad faith conduct during the case. The court sanctioned Stanley $15,523.31, the amount of attorney's fees and costs incurred by the chapter 7 trustee that were previously awarded by the court but remained outstanding due to lack of estate funds. We AFFIRM on the basis that sanctioning Stanley was a proper exercise of the bankruptcy court's inherent authority.

FACTS

A. Prepetition events

Debtor was organized as an Arizona limited liability company in 2012 for the purpose of excavating, grading, and oil surface contracting. Barbara Holbrook was a member of Debtor, as reflected in the Arizona Corporation Commission ("ACC") records. Creditor Payam Khoshbin became a member of Debtor in 2014. After Khoshbin's withdrawal in 2016, Holbrook became the sole member and manager of Debtor and remained so thereafter.

In 2017, Debtor, represented by Stanley, filed a complaint in state court against Khoshbin alleging claims for conversion, interference with contract relations, and an accounting. Khoshbin asserted a counterclaim for an accounting alleging, among other things, that Debtor's members used bank accounts unknown to him to hide Debtor's revenues.

In June 2018, while the Khoshbin litigation was pending, Stanley assisted Holbrook in creating a successor company known as BCB Excavating Services LLC ("BCB Excavating") through which Holbrook (and her husband) could continue the same business as they did through Debtor. Holbrook was the sole member and manager of BCB Excavating. BCB Excavating and Debtor shared the same mailing address, phone and fax numbers, and also shared the same email address until at least April 2019, when Stanley advised Holbrook to establish a new email address for BCB Excavating. Debtor's equipment was transferred to BCB Excavating for use in its business operations without providing anything of value to Debtor in exchange.

Several months into the Khoshbin litigation, Stanley advised Holbrook that Debtor should "walk away" from the lawsuit. He withdrew as Debtor's counsel and advised Holbrook to withdraw as the member of Debtor, which would be accomplished by filing with the ACC an Articles of Amendment to Debtor's Articles of Organization. In March 2019, the ACC rejected Holbrook's filing, stating: "Barbara Holbrook is the ONLY Member listed on the LLC. If you wish to remove this Member, You Must assign a New Member OR Manager to the LLC." Stanley doubted the correctness of the ACC's statement, but Holbrook opted not to pursue the matter. Accordingly, Holbrook proceeded as though

she was still a member of Debtor.

***2** Khoshbin obtained a judgment against Debtor for $167,367.47, plus attorney's fees. Khoshbin then served subpoenas on BCB Excavating and the Holbrooks seeking information about Debtor's assets and any transfers made to BCB Excavating. Stanley, representing BCB Excavating and the Holbrooks, filed objections to the subpoenas and moved to quash. The state court overruled the objections, denied the motions to quash, and ordered BCB Excavating and the Holbrooks to comply with the Khoshbin subpoenas by December 12, 2019. On December 3, 2019, Stanley sent to Holbrook the following email:

> As you might have guessed, I'm asking because the state superior court judge ruled against us on the subpoenas. We could challenge his ruling by means of a special action (cost, $2 to 5K) and if we prevailed there Csontos [Khoshbin's counsel] would have to go back and pursue a more difficult path toward seeking information from you. Alternatively, we could just go ahead with putting BCB Contracting into Ch. 7 bankruptcy ($1,250 to start - and that should be about it unless Csontos/Khoshbin gets involved in the bankruptcy case and succeeds in getting the bankruptcy trustee to try to pursue you for money or property allegedly diverted from BCB Contracting).

Stanley sent Holbrook two additional emails expressing the urgency to put Debtor into bankruptcy to avoid compliance with the Khoshbin subpoenas. Holbrook agreed to proceed with the bankruptcy filing for Debtor.

B. Postpetition events

On December 11, 2019, Debtor, represented by Stanley, filed a chapter 7 bankruptcy case. Debtor was insolvent and subject to at least two outstanding judgments totaling $275,866.74. Holbrook signed, as Debtor's sole member, the petition, schedules, statement of financial affairs ("SOFA"), and the amended SOFAs. The initial Schedule A/B reported Debtor's assets of $34,252.51 in cash and a 14-foot cargo trailer valued at $5,000.

Anthony Mason was appointed as the chapter 7 trustee ("Trustee") in Debtor's case. His investigation revealed that not all of Debtor's equipment had been reported on the schedules and that certain transfers of funds from Debtor to BCB Excavating also went unreported. After Trustee's discovery, the schedules were amended to reflect Debtor's unreported equipment, which Trustee later sold for $3,750, but the SOFA was never amended to include the unreported transfers. Major discrepancies also existed between Debtor's reported gross revenues for 2018 and 2019 in the initial SOFA and the Holbrooks' federal tax returns for those years, but no amended SOFA ever cured those discrepancies.

Debtor, BCB Excavating, the Holbrooks, and Stanley also resisted Trustee's investigative efforts. Debtor failed to provide him with any requested information prior to the § 341(a) meeting of creditors. Trustee had to file motions to compel to obtain documents that were the subject of his Rule 2004 examinations, and Debtor failed to even appear at the examination. Even after Trustee prevailed on his motions to compel, BCB Excavating still failed to produce bank statements. He had to subpoena bank records to discover some of the undisclosed and unscheduled transfers from Debtor to BCB Excavating.

On May 26, 2020, Stanley moved to withdraw as counsel for Debtor. The bankruptcy court approved Stanley's withdrawal.

1. The special action and action against Trustee

Sometime in May 2020, Stanley and Holbrook discussed the ACC's earlier statement that her attempted withdrawal from Debtor as its last member had been ineffectual. Stanley believed that if they could file a special action and get the ACC to change its position and make it retroactive to March 27, 2019, it would mean that Holbrook was not a member of Debtor when the bankruptcy petition was filed in December 2019. Consequently, because she had no authority to file it, Debtor's bankruptcy case would have to be dismissed. Holbrook agreed to have Stanley file the special action.

***3** One week after his withdrawal as Debtor's bankruptcy attorney, Stanley, on behalf of Holbrook, filed the special action in state court. Ultimately, the ACC agreed that its earlier statement was erroneous and further agreed to

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correct the error and give effect to Holbrook's withdrawal from Debtor retroactively as of March 27, 2019.

Stanley did not inform Trustee of the special action. Upon discovering its existence, Trustee filed a notice of bankruptcy. Thereafter, Holbrook, represented by Stanley, sued Trustee in federal district court for declaratory relief to establish that she did not violate the automatic stay when she filed the special action. When Trustee's requests to Stanley to voluntarily dismiss the action failed, he moved to dismiss it. The district court granted Trustee's dismissal motion, finding that the action was barred by *Barton v. Barbour*, 104 U.S. 126 (1881). Trustee then sought sanctions in the bankruptcy court against Stanley[3] for attorney's fees and costs, which the court granted. It found that the action against Trustee was frivolous, filed for an improper purpose, and filed in bad faith. The district court affirmed the bankruptcy court's sanctions order.

2. Motions to dismiss Debtor's chapter 7 case

Meanwhile, and now armed with the ACC's changed position as to Holbrook's withdrawal from Debtor, Stanley filed on behalf of BCB Excavating and the Holbrooks a motion to dismiss Debtor's bankruptcy case. They argued that the case had to be dismissed for lack of personal jurisdiction because Holbrook lacked authority to file it due to her retroactive removal as a member of Debtor.

Trustee agreed that dismissal was appropriate but for different reasons. Besides the misrepresentations and omissions made in Debtor's schedules and SOFAs and the lack of cooperation during the case, Holbrook had stated under penalty of perjury in the petition and SOFAs that she was the sole member of Debtor. However, argued Trustee, she was asserting in the special action that she had resigned as a member nine months before the chapter 7 filing. Trustee argued that it was bad faith to assert that Holbrook was a member of Debtor when seeking refuge in the bankruptcy court, yet assert the opposite in the special action, which was filed for the sole purpose of getting Debtor's bankruptcy case dismissed. The first motion to dismiss was denied without prejudice.

Later, Stanley, on his own behalf, moved to dismiss Debtor's bankruptcy case. His motion was nearly identical to the first motion that he filed on behalf of BCB Excavating and the Holbrooks and was based upon the same argument: that the bankruptcy court lacked personal jurisdiction over Debtor because Holbrook lacked authority on the petition date to file the case. The bankruptcy court denied the second motion to dismiss, finding that Stanley lacked standing; he was neither counsel for Debtor nor a creditor.

3. Trustee's motion for sanctions

Trustee then moved for sanctions against Stanley[4] under Rule 9011[5] and the court's "inherent authority under § 105(a)."[6] He argued that sanctions were warranted for many of the same reasons he articulated in response to the first motion to dismiss. Trustee argued that the petition was filed in bad faith because it was not filed to address Debtor's debts; rather, it was filed to avoid compliance with the Khoshbin subpoenas and to unnecessarily delay the ultimate enforcement of two judgments entered against Debtor. Trustee argued that Stanley further abused the bankruptcy process by filing the special action as a means to sabotage the bankruptcy case, create an improper exit strategy, and allow Holbrook to escape examination as Debtor's representative. Trustee requested compensatory sanctions of $15,523.31, plus an additional $50,000 as a deterrence. Khoshbin joined in Trustee's motion.

***4** Stanley opposed the sanctions motion, disputing Trustee's allegation of bad faith. He argued that the filing of the first motion to dismiss was not bad faith; rather, it was due to a change in circumstances. After the ACC corrected its records retroactively to March 2019, argued Stanley, it was clear that Holbrook lacked authority to file Debtor's bankruptcy petition in December 2019 and, hence, that the bankruptcy court lacked personal jurisdiction. Stanley also argued that Debtor's chapter 7 case was a proper filing; there was nothing improper about an insolvent company invoking the automatic stay to stop collection efforts and letting a bankruptcy trustee liquidate the company and apply the net proceeds, if any, to the claims of its creditors.

At the evidentiary hearing, Stanley testified that he did not verify or ascertain the accuracy of what Holbrook reported in the bankruptcy papers she signed under penalty of perjury. Importantly, he did not ask for any tax returns or bank statements even though he knew Khoshbin's subpoena suggested that fraudulent transfers were made from Debtor to BCB Excavating. However, when Stanley asked Holbrook about any prepetition transfers before filing, Holbrook told him that no such transfers had been made. Stanley testified that when he saw Debtor's bank statements that were subpoenaed by

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Trustee, he became concerned that perhaps some fraudulent transfers had occurred and that the Holbrooks were potentially liable.

In response to the court's questions during opening argument, Stanley stated that he, as a debtor's attorney, would not have an obligation to run a credit report, to do a real property search to see if the debtor owned any properties, to do a UCC search for liens against any of the debtor's personal property, or to do a search for any pending litigation involving the debtor.

The bankruptcy court entered an order sanctioning Stanley and awarding Trustee his attorney's fees and costs of $15,523.31; it declined to award any of the requested $50,000. Focusing on its findings under § 105(a), the court found that Stanley acted in bad faith: (1) by initiating the chapter 7 case for the improper purpose of gaining a tactical advantage over Khoshbin in the Khoshbin litigation; (2) by his reckless misstatements of fact in the schedules and SOFAs; and (3) by his conduct throughout the proceeding.

JURISDICTION

The bankruptcy court had jurisdiction under 28 U.S.C. § 157(b)(1) and (b)(2)(A). We have jurisdiction under 28 U.S.C. § 158(b).

ISSUE

Did the bankruptcy court abuse its discretion in sanctioning Stanley under § 105(a)?

STANDARDS OF REVIEW

We review an award of sanctions for an abuse of discretion. *Caldwell v. Unified Cap. Corp. (In re Rainbow Mag., Inc.)*, 77 F.3d 278, 283 (9th Cir. 1996) (reviewing sanctions imposed under Rule 9011 and the bankruptcy court's inherent power to sanction); *Shalaby v. Mansdorf (In re Nakhuda)*, 544 B.R. 886, 898 (9th Cir. BAP 2016), *aff'd*, 703 F. App'x 621 (9th Cir. 2017). A bankruptcy court abuses its discretion if it applies the wrong legal standard, or misapplies the correct legal standard, or if it makes factual findings that are illogical, implausible, or without support in the record. *United States v. Hinkson*, 585 F.3d 1247, 1262 (9th Cir. 2009) (en banc).

"A finding of bad faith, prerequisite to assessment of attorneys' fees under the court's inherent power, will be overturned only if clearly erroneous." *Bader v. Itel Corp. (In re Itel Sec. Litig.)*, 791 F.2d 672, 674 (9th Cir. 1986) (cleaned up). A factual finding is clearly erroneous if it is illogical, implausible, or without support in the record. *Retz v. Samson (In re Retz)*, 606 F.3d 1189, 1196 (9th Cir. 2010).

We may affirm on any ground supported by the record, regardless of whether the bankruptcy court relied upon, rejected, or even considered that ground. *Fresno Motors, LLC v. Mercedes Benz USA, LLC,* 771 F.3d 1119, 1125 (9th Cir. 2014).

DISCUSSION

***5** In addition to Rule 9011, bankruptcy courts have the power to sanction under (1) their statutory civil contempt authority under § 105(a), and (2) their inherent sanction authority. *See* *Law v. Siegel*, 571 U.S. 415, 420-21 (2014) (a bankruptcy court has statutory authority under § 105(a) to issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of the Code, **and** it possesses inherent power to sanction abusive litigation practices); *Knupfer v. Lindblade (In re Dyer)*, 322 F.3d 1178, 1196 (9th Cir. 2003). In *Dyer*, the Ninth Circuit Court of Appeals discussed the important distinction between these two powers and emphasized that they are not interchangeable:

> Civil contempt authority allows a court to remedy a violation of a specific order (including 'automatic' orders, such as the automatic stay or discharge injunction). The inherent sanction authority allows a bankruptcy court to deter and provide compensation for a broad range of improper litigation tactics.

322 F.3d at 1196 (citing *Fink v. Gomez*, 239 F.3d 989, 992-93 (9th Cir. 2001)).

The inherent power to sanction bad-faith conduct is broader than Rule 9011 sanctions and "extends to a full range of litigation abuses." *Miller v. Cardinale (In re Deville)*, 280 B.R. 483, 495 (9th Cir. BAP 2002), *aff'd sub nom. Miller v. Cardinale (In re DeVille)*, 361 F.3d 539 (9th Cir. 2004) (citing *Chambers v. NASCO, Inc.*, 501 U.S. 32, 46 (1991)). A court may sanction under its inherent power even when the same conduct may also be punishable under another sanctioning statute or rule, such as Rule 9011. *Id.* (citing *Chambers*, 501 U.S. at 49).

Unlike civil contempt under § 105(a), to impose sanctions under its inherent authority, the bankruptcy court must find either bad faith, conduct tantamount to bad faith, or recklessness "with an additional factor such as frivolousness, harassment, or an improper purpose." *Fink*, 239 F.3d at 994. Counsel's goal to gain a tactical advantage in another case is sufficient to support a finding of bad faith and improper purpose. *Id.* at 992 (citing *In re Itel Sec. Litig.*, 791 F.2d at 675). Additionally, a court may sanction under its inherent authority a party who has engaged in bad-faith conduct over the course of a case. *See* *Goodyear Tire & Rubber Co. v. Haeger*, 137 S. Ct. 1178, 1184-85 (2017).

Although the bankruptcy court stated that it was relying on § 105(a) to impose sanctions against Stanley, it is clear that the court applied its inherent power to sanction him. It made the explicit finding of bad faith, and the additional findings of frivolousness and recklessness with an improper purpose. Specifically, the court found that Stanley acted in bad faith by initiating the chapter 7 case for the improper purpose of gaining a tactical advantage over Khoshbin in the Khoshbin litigation − i.e., using Debtor's bankruptcy to avoid the Khoshbin subpoenas and to improperly delay the collection of judgments against Debtor, and using the automatic stay as a substitute for appealing the denial of the motions to quash. In addition, the court found that Stanley acted in bad faith by making reckless misstatements of fact in the schedules and SOFAs.

The court also found that Stanley acted in bad faith by his conduct throughout the proceeding. While it did not describe the conduct, the record reflects, and Trustee had argued, that Stanley engaged in abusive litigation tactics after the case was filed. Debtor (and Holbrook) got the benefit of the automatic stay to thwart Khoshbin's collection efforts yet failed to fulfill the debtor's duties imposed by the Code. Debtor, represented by Stanley, failed to provide Trustee with the necessary financial information for the § 341(a) meeting of creditors. Trustee also had to file motions to compel before documents that were the subject of his Rule 2004 examinations were produced. And when that failed with respect to bank records, Trustee had to subpoena them.

***6** Immediately after his withdrawal as Debtor's bankruptcy attorney, Stanley filed the special action as a means to get Debtor's bankruptcy case dismissed after it became apparent that putting Debtor in chapter 7 was not such a great idea and certainly not in the best interest of his clients Holbrook and Debtor's successor company BCB Excavating. Stanley then, without seeking leave from the bankruptcy court, sued Trustee in federal district court over what he erroneously viewed as Trustee's improper involvement in the special action. When Stanley refused to voluntarily dismiss what Trustee warned was a frivolous lawsuit against him, Trustee had to file a motion to dismiss. The district court dismissed the action as barred by *Barton*. Stanley was later sanctioned by the bankruptcy court for the frivolous filing, which the district court affirmed. Stanley also filed the meritless second motion to dismiss Debtor's chapter 7 case, which he clearly lacked standing to file.

Stanley argues that the bankruptcy court did not impose sanctions under its inherent authority or § 105(a); rather, it foreshadowed the conditional sanctioning of him based on what an appellate court might do later. While the court's ruling is oddly worded, it appears to us that it did in fact, in the alternative, impose sanctions against Stanley under its inherent authority although it erroneously cited § 105(a). Despite its citation to § 105(a), the court applied the correct law and made the appropriate findings, including a finding of bad faith, for imposing inherent authority sanctions.

Stanley argues that a "bad faith" finding under the court's inherent authority requires conduct amounting to fraud or akin to it. That is simply not the law, and he fails to cite any authority so holding. Stanley also argues that the bankruptcy court erred by relying on § 105(a) for its decision, asserting that the court could only impose sanctions under § 105(a) if he violated some other provision of the Code. As we have concluded that the bankruptcy court sanctioned Stanley under its inherent authority, we need not address this issue.

Lastly, Stanley argues that there was no basis for the bankruptcy court to sanction him under its inherent authority because it could do so adequately under Rule 9011. Although the Supreme Court in *Chambers* warned

that a court must "exercise caution" when invoking its inherent power and "ordinarily should rely on the Rules" when sanctioning, it also added that if "neither the statute nor the Rules are up to the task, the court may safely rely on its inherent power." 501 U.S. at 50. The bankruptcy court found that Stanley engaged in bad faith conduct throughout the proceeding. Since much of that conduct did not consist of a writing filed with the court, and Rule 9011 does not reach such conduct, the court's reliance on its inherent power was appropriate.

Once a finding of bad faith has been made, a court may award attorney's fees and costs as a sanction to compensate the prevailing party for expenses incurred by his or her opponent's bad faith litigation tactics. *Chambers*, 501 U.S. at 45-46; *Fink*, 239 F.3d at 991. The bankruptcy court sanctioned Stanley $15,523.31, the amount of attorney's fees previously awarded to Trustee but remaining unpaid by the estate due to lack of funds. These fees were apparently incurred due to the bad faith filing and had already been reviewed for reasonableness when awarded. Stanley has not argued that the amount of sanctions was improper, so we have no reason to question it.

While the bankruptcy court erroneously relied on § 105(a) to sanction Stanley under its inherent authority, such error was harmless. The record supports its decision to sanction Stanley under its inherent authority, which is not dependent upon § 105(a). Accordingly, we conclude that the bankruptcy court did not abuse its discretion in sanctioning Stanley and awarding Trustee his attorney's fees and costs of $15,523.31.

CONCLUSION

***7** For the reasons stated above, we AFFIRM.

All Citations

Slip Copy, 2022 WL 1198232

Footnotes

* This disposition is not appropriate for publication. Although it may be cited for whatever persuasive value it may have, *see* Fed. R. App. P. 32.1, it has no precedential value, *see* 9th Cir. BAP Rule 8024-1.

1 Unless specified otherwise, all chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and all "Rule" references are to the Federal Rules of Bankruptcy Procedure.

2 Although the bankruptcy court said it was sanctioning Stanley under § 105(a), it appears to have relied on its inherent power to do so. We discuss that issue more below.

3 By this time, Trustee had settled with Holbrook, which we discuss more below.

4 Trustee initially sought sanctions against Debtor, BCB Excavating, the Holbrooks, and Stanley. Before the evidentiary hearing, Trustee settled with everyone except Stanley.

5 Since we are affirming the bankruptcy court's decision to impose sanctions under its inherent authority, we do not discuss any further the arguments raised or the court's ruling with respect to sanctions under Rule 9011.

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6 Section 105(a) provides, in relevant part: "The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."

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KeyCite Blue Flag – Appeal Notification
Appeal Filed by MARK STUART, ET AL v. CITY OF SCOTTSDALE, ET AL, 9th Cir., December 17, 2021

632 B.R. 531
United States Bankruptcy Appellate Panel of the Ninth Circuit.

IN RE: Mark E. STUART, Debtor.
Mark E. Stuart, Appellant,
v.
City of Scottsdale; Russell Brown, Chapter 13 Trustee; City of Scottsdale Attorney's Office, Appellees.

BAP No. AZ-21-1063-FLS
|
Bk. No. 2:19-bk-05481-BKM
|
Filed November 10, 2021

Synopsis
Background: After city obtained a prepetition state-court judgment against debtor and garnished three of his bank accounts, causing bank to freeze account funds, debtor filed Chapter 13 petition and subsequently moved for sanctions, asserting that city's refusal to lift the garnishment immediately violated the automatic stay. City objected and, following bankruptcy court's entry of minute order determining that city had violated the stay and allowing debtor to proceed with evidentiary hearing on damages, moved for reconsideration. The United States Bankruptcy Court for the District of Arizona, Brenda K. Martin, J., granted reconsideration, vacated its earlier minute order, and denied the stay violation motion. Debtor appealed.

Holdings: The Bankruptcy Appellate Panel (BAP), Faris, J., held that:

[1] under *City of Chicago, Illinois v. Fulton*, 141 S.Ct. 585, city did not violate the automatic stay when, upon debtor's bankruptcy filing, it failed to move to quash the writ of garnishment or cause bank to unfreeze the accounts;

[2] city did not "continue" a proceeding against debtor in violation of the automatic stay;

[3] city did not seek to enforce a prepetition judgment against debtor in violation of the automatic stay;

[4] city did not take any act to obtain possession of estate property in violation of the automatic stay; and

[5] city did not take any other "act" against debtor in violation of the automatic stay.

Affirmed.

Procedural Posture(s): On Appeal; Motion for Damages, Contempt, or Sanctions for Violation of Automatic Stay; Motion for Reconsideration.

West Headnotes (16)

[1] **Bankruptcy** Enforcement of Injunction or Stay

Bankruptcy court's initial stay violation ruling, by which it determined that judgment creditor's failure to lift its garnishment of debtor's bank accounts upon his filing of Chapter 13 petition violated the automatic stay but left the question of damages for a later evidentiary hearing, was not a final order to which the rule governing relief from judgment or order applied; the bankruptcy court was free to review and change its own interlocutory order, whether or not the rule permitted it to do so. 11 U.S.C.A. § 362(a); Fed. R. Civ. P. 60(b); Fed. R. Bankr. P. 9024.

[2] **Bankruptcy** Conclusions of law; de novo review

Bankruptcy court's determination that the automatic stay was violated was a question of law subject to de novo review. 11 U.S.C.A. § 362(a).

[3] **Bankruptcy** Conclusions of law; de novo review

"De novo review" requires that the Bankruptcy Appellate Panel (BAP) consider a matter anew, as if no decision had been made previously.

[4] **Bankruptcy** Clear error

Bankruptcy Appellate Panel (BAP) reviews bankruptcy court's underlying factual findings for clear error.

[5] **Bankruptcy** Clear error

Bankruptcy court's factual findings are "clearly erroneous" if they are illogical, implausible, or without support in the record.

[6] **Bankruptcy** Clear error

If two views of the evidence are possible, bankruptcy court's choice between them cannot be "clearly erroneous."

[7] **Bankruptcy** Proceedings, Acts, or Persons Affected

Automatic stay is designed to effect immediate freeze of status quo by precluding and nullifying postpetition actions, judicial or nonjudicial, in nonbankruptcy fora against debtor or affecting property of estate. 11 U.S.C.A. § 362(a).

[8] **Bankruptcy** Damages and attorney fees

"Willful" violation of automatic stay, as required for recovery of actual damages, is satisfied if party knew of stay, and its actions in violation of stay were intentional. 11 U.S.C.A. §§ 362(a), 362(k)(1).

[9] **Bankruptcy** Judicial proceedings in general

Under *City of Chicago, Illinois v. Fulton*, 141 S.Ct. 585, city, which held prepetition state-court judgment against Chapter 13 debtor and had garnished three of his bank accounts, did not violate the automatic stay when, upon debtor's bankruptcy filing, it failed to move to quash the writ of garnishment or cause bank to unfreeze the accounts; by its inaction, city did not "exercise control over" estate property, and it had no affirmative duty to ensure the return of such property to debtor. 11 U.S.C.A. § 362(a)(3).

[10] **Bankruptcy** Judicial proceedings in general

Where creditor has executed prepetition writ of garnishment against debtor's bank account, it is under no affirmative obligation to release funds upon debtor's filing of bankruptcy petition and, in order to avoid violating automatic stay, need only maintain status quo. 11 U.S.C.A. § 362(a)(3).

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[11] **Bankruptcy** Proceedings, Acts, or Persons Affected

Nothing in subsection of Bankruptcy Code providing that filing of bankruptcy petition creates a stay of any act to, inter alia, exercise control over property of the estate requires actual or physical possession of estate property. 11 U.S.C.A. § 362(a)(3).

[12] **Bankruptcy** Judicial proceedings in general

City, which held prepetition state-court judgment against Chapter 13 debtor and had garnished three of his bank accounts, did not "continue" a proceeding against debtor in violation of the automatic stay when, upon his bankruptcy filing, it promptly sought a stay of the parties' pending state-court action and took no further steps to advance that case, but failed to move to quash the writ of garnishment or cause bank to unfreeze the accounts; leaving the state-court action and the garnishment in place did not disturb the status quo, and so was sufficient to avoid "continuation" of the action. 11 U.S.C.A. § 362(a)(1).

[13] **Bankruptcy** Proceedings, Acts, or Persons Affected

Creditor's failure to affirmatively release frozen bank account funds, in and of itself, is not a violation of the subsection of the Bankruptcy Code providing that filing of bankruptcy petition creates a stay of the commencement or continuation of a prepetition action against the debtor. 11 U.S.C.A. § 362(a)(1).

[14] **Bankruptcy** Judicial proceedings in general

City, which held prepetition state-court judgment against Chapter 13 debtor and had garnished three of his bank accounts, did not seek to enforce the judgment against debtor or estate property in violation of the automatic stay when, upon debtor's bankruptcy filing, it failed to move to quash the writ of garnishment or cause bank to unfreeze the accounts; city took no position on whether state court should order release of the account funds, but repeatedly stated that it would not oppose such release, nor did it otherwise take any affirmative action to enforce the judgment or further the garnishment. 11 U.S.C.A. § 362(a)(2).

[15] **Bankruptcy** Judicial proceedings in general

City, which held prepetition state-court judgment against Chapter 13 debtor and had garnished three of his bank accounts, did not take any act to obtain possession of estate property in violation of the automatic stay when, upon debtor's bankruptcy filing, it failed to move to quash the writ of garnishment or cause bank to unfreeze the accounts; on the petition date, city already had obtained the writ of garnishment and bank had frozen the accounts, such that there was no further "act to obtain possession," and city's acts or omissions merely preserved the status quo, and did not capture any more funds postpetition. 11 U.S.C.A. § 362(a)(3).

[16] **Bankruptcy** Judicial proceedings in general

City, which held prepetition state-court judgment against Chapter 13 debtor and had garnished three of his bank accounts, did not take any other "act" against debtor in violation of the automatic stay when, upon debtor's bankruptcy filing, it failed to move to quash the writ of garnishment or cause bank to unfreeze

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the accounts; city, which promptly stayed the parties' pending state-court action and stated multiple times that it did not oppose release of the frozen funds, did not do anything to enhance its position and only sought to maintain the status quo. 11 U.S.C.A. § 362(a)(6).

The bankruptcy court correctly held that the City did not violate the automatic stay. We AFFIRM. We publish to explain the effect of *Fulton* on a prepetition bank account garnishment.

FACTS

***533** Appeal from the United States Bankruptcy Court for the District of Arizona, Brenda K. Martin, Bankruptcy Judge, Presiding

Attorneys and Law Firms

Chris D. Barski of Barski Law PLC, Scottsdale, argued for appellant Mark E. Stuart;

Vail C. Cloar of Dickinson Wright PLLC, Phoenix, argued for appellee City of Scottsdale.

Before: FARIS, LAFFERTY, and SPRAKER, Bankruptcy Judges.

OPINION

FARIS, Bankruptcy Judge:

INTRODUCTION

After the City of Scottsdale garnished three of his bank accounts, debtor Mark E. Stuart filed a chapter 13[1] petition. Mr. Stuart argued that the automatic stay required the City to lift the garnishment immediately. Relying on *City of Chicago v. Fulton*, —— U.S. ——, 141 S. Ct. 585, 208 L.Ed.2d 384 (2021), the bankruptcy court ruled against Mr. Stuart. Mr. Stuart appeals, ***534** arguing that *Fulton* is inapplicable to this case and that the City engaged in "acts" that violated multiple subsections of § 362(a).

A. Prepetition events

Mr. Stuart has long pursued the City in various "public interest" cases. He lost one such case (the "State Court Action"), and in 2015 the state court awarded the City a final judgment exceeding $30,000 in sanctions and costs, plus interest (the "State Court Judgment"). The Arizona Court of Appeals affirmed the State Court Judgment.

In April 2019, the City served a writ of garnishment on Bank of America ("BOA"), where Mr. Stuart had three accounts. BOA froze the accounts, which held a total of $8,879.95.

Mr. Stuart sought to quash the writ, arguing that the bank accounts were community property not subject to the City's claims. The state court agreed that the State Court Judgment was unenforceable against any community property. However, it noted that Mr. Stuart had previously obstructed discovery, making it impossible for the City to determine the existence and nature of his property, and allowed the City an opportunity to conduct discovery. Before the City could take any further action, Mr. Stuart filed his bankruptcy petition.

B. Mr. Stuart's bankruptcy case and the City's response

On Saturday, May 4, 2019, Mr. Stuart filed a chapter 13 petition.[2] His attorney contacted BOA by fax dated May 6 (the next business day) and requested that it release the frozen funds. BOA responded the following day that it would retain the funds unless it was directed otherwise by the City or the bankruptcy court.

On May 7, Mr. Stuart's counsel contacted the City and demanded that the City direct BOA to release the frozen funds. The attorney handling the matter was out of town and did not respond immediately. Nevertheless, the City filed a motion to stay litigation in the State Court Action

that same day. It requested that "all pending matters in this case, including any scheduled hearings, be stayed pending resolution from [sic] the bankruptcy proceedings." The state court granted the motion.

Also on May 7, Mr. Stuart, proceeding pro se, filed a document informing the state court of the stay and requesting that the state court quash the writ of garnishment.

On May 13, the responsible attorney for the City sent an e-mail to Mr. Stuart's counsel, BOA's counsel, and others. He said that he had been out of the office the previous week and stated that he believed that "the funds being held by the bank pursuant to the garnishment became property of the bankruptcy estate. Accordingly, the City of Scottsdale does not have a current possessory interest in them ...." He concluded that "the City will abide whatever disposition of those funds is made in accordance with the Bankruptcy Statutes/Rules."

Counsel for BOA responded that he would direct BOA to release the funds ***535** once the City quashed the writ of garnishment. Counsel for the City wrote back that "[t]he City has requested a stay of the proceedings in state court. The City does not oppose release of the funds by the Bank."

The City also filed a response to Mr. Stuart's request to quash the writ. It took the position that the court should "deny Stuart's request as the court has already provided Stuart to [sic] the relief which he is entitled, i.e., a stay of the proceedings. However, the City does not oppose release of the funds by [BOA] and does not object to a court order instructing [BOA] to release the funds." It argued that, under § 362(a), it was not required to dismiss the garnishment proceedings, only to stay them, which the court had already done. Because funds had not left Mr. Stuart's accounts, there was nothing to "return." Nevertheless, it repeated that it "does not object to an order from this Court authorizing [BOA] to release any hold on funds that may have arisen as a result of the garnishment."

On May 14, the state court issued a minute order that: (1) granted Mr. Stuart's request to quash the writ; (2) denied the City's request for a stay, because all matters were previously stayed; and (3) denied Mr. Stuart's request for a return of the funds, because the monies remained in his accounts. BOA unfroze the three bank accounts shortly thereafter.

C. The motions for sanctions for the City's stay violation

Mr. Stuart filed a motion for sanctions ("Stay Violation Motion") against the City[3] based on the alleged violation of the automatic stay.[4] He asserted that there was no dispute that the City knew of the automatic stay yet refused to dismiss the state court garnishment action. He argued that the City had an affirmative duty to remedy the violation by releasing the frozen account funds. He alleged that the garnishment and the stay violation caused him and his wife severe psychological distress, including anxiety, depression, and sleeplessness.

The City objected to the Stay Violation Motion. It argued that it never held the garnished funds and never took any action after the bankruptcy filing, including continuing the garnishment action or exercising control over estate property. It contended that BOA held the funds and that the City had done all that was required of it, i.e., move to stay the State Court Action. It was not required to dismiss any judicial action, only "maintain the status quo ante." It pointed out that Mr. Stuart did not identify any act that violated the automatic stay. The City took the position that it had "nothing to do with" the return of the frozen funds and stated (falsely) that it had "filed a request to quash the writ."

Mr. Stuart filed a reply brief and asserted that sanctions were warranted under § 362(a)(1), (2), (3), and (6).

At the hearing on the Stay Violation Motion, the bankruptcy court recognized that the City immediately sought to stay the State Court Action but nevertheless faulted the City for not seeking to quash the writ of garnishment. The bankruptcy ***536** court cited an unpublished Ninth Circuit decision, *Best Service Co. v. Bayley (In re Bayley)*, 678 F. App'x 593 (9th Cir. 2017), for the proposition that the City violated the automatic stay "by failing to promptly direct Bank of America to return the funds and/or promptly requesting the writ be quashed ...." It said that its decision was a "preliminary ruling" subject to an evidentiary hearing to determine damages.

The court entered a minute order determining that the City violated the automatic stay ("Stay Violation Ruling"). It allowed Mr. Stuart to proceed with an evidentiary hearing for a determination of damages against the City and its attorneys in the State Court Action.[5]

Mr. Stuart filed a motion for sanctions ("Sanctions Motion") under § 362(k) against the City and two of its attorneys. He sought damages for physical and

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psychological distress for himself and his non-debtor wife, Virginia Stuart, as well as costs associated with the Stay Violation Motion, totaling $20,783. Additionally, he requested $30,000 in punitive damages and attorneys' fees and costs. The City opposed the motion.

D. The City's motion for reconsideration

Prior to the hearing, the City filed a motion for reconsideration ("Reconsideration Motion") of the Stay Violation Ruling under Civil Rule 60(b), made applicable in bankruptcy via Rule 9024. It argued that the U.S. Supreme Court's recent *Fulton* decision "clarified that the mere retention of property post-petition does not comprise a violation of the automatic stay as a matter of law." It contended that *Fulton* dictated that the City needed only to refrain from disturbing the status quo and was not required to release the garnished funds or direct BOA to release the funds.

Mr. Stuart opposed the Reconsideration Motion, arguing that *Fulton*'s narrow holding under § 362(a)(3) was inapplicable to this case because the City denied ever possessing Mr. Stuart's property. Rather, Mr. Stuart focused on the continuation of the writ of garnishment, which he contended was an act to collect and enforce the State Court Judgment under § 362(a)(1), (2), (3), and (6).

The bankruptcy court held a hearing on the Reconsideration Motion. It took the matter under advisement and issued a supplemental minute entry/order granting the Reconsideration Motion. It noted that "the crux of its [Stay Violation Ruling] was that the City of Scottsdale had an affirmative duty to ensure the release of funds frozen by Bank of America based on the City of Scottsdale's pre-petition garnishment action." It clarified that its "focus was on the retention of estate property as being in violation of the stay" and that "the Court ruled that the City of Scottsdale's failure to direct or otherwise secure release of the frozen funds violated the stay under § (a)(3)." It held that, "[u]nder *Fulton* that conclusion is now wrong.... [M]ere retention of an estate asset is not an act in violation of § 326(a)(3) [sic] and there is no requirement that an entity take affirmative action 'to relinquish control of the debtor's property at the moment a bankruptcy petition is filed.' " (Quoting *Fulton*, 141 S. Ct. at 591.)

The bankruptcy court then examined subsections (a)(1), (2), (3), and (6) and declined to find any stay violation.

As to subsection (a)(1), the bankruptcy court held that ***537** *Eskanos & Adler, P.C. v. Leetien*, 309 F.3d 1210 (9th Cir. 2002), did not help Mr. Stuart's position because the duty under subsection (a)(1) is to discontinue an action. It noted that the City promptly sought a stay of the State Court Action upon learning of the petition and only opposed the motion to quash the writ, requesting instead that the matter remain stayed. It further rejected his argument that garnishment actions are different from other collection actions.

Regarding subsection (a)(2), the court held that the City's failure to quash the writ was not an act to enforce a judgment. It distinguished *Bayley*, which it earlier relied on, because the City did not direct any third party to retain estate property and did not take any other "act" to compel or enforce the State Court Judgment. It stated that the City "ceased ongoing collection activities."

Regarding subsection (a)(3), the court held that the City did not "obtain possession" of estate property. It stated that Mr. Stuart failed to explain what the City did to "obtain possession" of the frozen funds and that he could have sought turnover of the funds under § 542.

Finally, the court held that subsection (a)(6) was equally inapplicable because the refusal to dismiss a lawsuit was not an "act to collect a claim." The City did not take any action other than to request a stay of the proceedings, and the mere retention of property is not an "act."

The bankruptcy court thus entered an order ("Reconsideration Order") that granted the Reconsideration Motion, vacated its earlier minute order, and denied the Stay Violation Motion.[6]

Mr. Stuart timely appealed.

JURISDICTION

The bankruptcy court had jurisdiction under 28 U.S.C. §§ 1334 and 157(b)(2)(A). We have jurisdiction under 28 U.S.C. § 158.

ISSUE

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Whether the bankruptcy court erred by holding that the City did not violate the automatic stay.

STANDARDS OF REVIEW

[1]The City styled its motion as a motion for reconsideration under Rule 9024, and the bankruptcy court applied the incorporated standards of Civil Rule 60(b). But, as the bankruptcy court acknowledged, the Stay Violation Ruling was not a final order because it did not decide the question of damages. Rule 9024 therefore did not apply. The bankruptcy court was free to review and change its own interlocutory order whether or not Rule 9024 permitted it to do so. *See City of L.A., Harbor Div. v. Santa Monica Baykeeper*, 254 F.3d 882, 887 (9th Cir. 2001) ("Although [Civil] Rule 60(b) has since changed, the lessons learned from our interpretation of it have not – a district court's authority to rescind an interlocutory order over which it has jurisdiction is an inherent power rooted firmly in the common law and is not abridged by the Federal Rules of Civil Procedure.").

[2] [3]Therefore, we review the Reconsideration Order de novo. *Yellow Express, LLC v. Dingley (In re Dingley)*, 514 B.R. 591, 595 (9th Cir. BAP 2014) ("A bankruptcy court's determination that the automatic stay was violated is a question of law subject to de novo review."), *aff'd on other grounds*, 852 F.3d 1143 (9th Cir. 2017). ***538** "De novo review requires that we consider a matter anew, as if no decision had been made previously." *Francis v. Wallace (In re Francis)*, 505 B.R. 914, 917 (9th Cir. BAP 2014).

[4] [5] [6]We review the court's underlying factual findings for clear error. *Knupfer v. Lindblade (In re Dyer)*, 322 F.3d 1178, 1191 (9th Cir. 2003). Factual findings are clearly erroneous if they are illogical, implausible, or without support in the record. *Retz v. Samson (In re Retz)*, 606 F.3d 1189, 1196 (9th Cir. 2010). If two views of the evidence are possible, the court's choice between them cannot be clearly erroneous. *Anderson v. City of Bessemer City*, 470 U.S. 564, 573-74, 105 S.Ct. 1504, 84 L.Ed.2d 518 (1985).

DISCUSSION

A. The filing of a bankruptcy petition stays certain postpetition actions.

[7]The automatic stay "is designed to effect an immediate freeze of the *status quo* by precluding and nullifying post-petition actions, judicial or nonjudicial, in nonbankruptcy fora against the debtor or affecting the property of the estate." *Mwangi v. Wells Fargo Bank, N.A. (In re Mwangi)*, 764 F.3d 1168, 1173 (9th Cir. 2014) (quoting *Hillis Motors, Inc. v. Haw. Auto. Dealers' Ass'n*, 997 F.2d 581, 585 (9th Cir. 1993)).

The subsections of § 362(a) describe the actions that are subject to the automatic stay. In this case, Mr. Stuart alleges that the City violated subsections (1), (2), (3), and (6). As is relevant to this case, those sections provide that the filing of a bankruptcy petition creates a stay of:

> (1) the commencement or continuation ... of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;
>
> (2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;
>
> (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;
>
> ...
>
> (6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title[.]

§ 362(a).

[8] Section 362(k)(1) provides that "an individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages." "A willful violation is satisfied if a party knew of the automatic stay, and its actions in violation of the stay were intentional." *Eskanos & Adler, P.C.*, 309 F.3d at 1215.

B. The bankruptcy court correctly held that, under

***Fulton*, the City did not violate § 362(a)(3).**

[9]The bankruptcy court held that, under *Fulton*, the City did not violate § 362(a)(3) when it failed to move to quash the writ of garnishment or cause BOA to unfreeze the bank accounts. We discern no error.

Prior to *Fulton*, this circuit interpreted § 362(a)(3) to require the creditor to take affirmative steps to turn over property of the estate, even if it is held by a third party. In an unpublished decision, the Ninth Circuit held:

> ***539** Upon the filing of Bayley's bankruptcy petition, Best Service had an affirmative duty to turn over all property to the bankruptcy estate, even if it was in the Sheriff's possession. *See* *Cal. Emp't Dev. Dep't v. Taxel (In re Del Mission Ltd.)*, 98 F.3d 1147, 1151 (9th Cir. 1996); *Knaus v. Concordia Lumber Co. (In re Knaus)*, 889 F.2d 773, 775 (8th Cir. 1989). However, by directing the Sheriff to hold the levied funds, Best Service both "enforce[d]" its pre-petition judgment, *see* 11 U.S.C. § 362(a)(2), and "exercise[d] control over property of the estate," *see* *id.* § 362(a)(3). Best Service should have "cease[d] its collection procedures and notif[ied] the Sheriff to return [Bayley's] property." *In re Hernandez*, 468 B.R. 396, 405 (Bankr. S.D. Cal. 2012). But because it did not, the district court properly concluded that Best Service was in violation of the automatic stay.

In re Bayley, 678 F. App'x 593. The *Bayley* decision cited *Del Mission*, in which the Ninth Circuit held that "the knowing retention of estate property violates the automatic stay of § 362(a)(3)[,]" 98 F.3d at 1151, and that the state's knowing retention of disputed taxes violated the automatic stay, *id.* at 1152.

In the consolidated cases addressed in *Fulton*, the City of Chicago impounded the debtors' vehicles for nonpayment of fines. The debtors filed chapter 13 petitions and requested that the city return their vehicles, but the city refused. The bankruptcy court held that the city's refusals violated § 362(a)(3) because it had acted to "exercise control over" the debtors' vehicles, and the Court of Appeals for the Seventh Circuit affirmed. 141 S. Ct. at 589.

The Supreme Court began its analysis by looking at the plain language of the statute. It stated:

> The language used in § 362(a)(3) suggests that merely retaining possession of estate property does not violate the automatic stay. Under that provision, the filing of a bankruptcy petition operates as a "stay" of "any act" to "exercise control" over the property of the estate. Taken together, the most natural reading of these terms – "stay," "act," and "exercise control" – is that § 362(a)(3) prohibits affirmative acts that would disturb the status quo of estate property as of the time when the bankruptcy petition was filed.

Id. at 590. It then said that the individual words suggested "that § 362(a)(3) halts any affirmative act that would alter the status quo as of the time of the filing of a bankruptcy petition." *Id.*[7]

The Court pointed to § 542, which concerns turnover of estate property, in support of its decision. It stated that § 542 "would be surplusage if § 362(a)(3) already required an entity affirmatively to relinquish control of the debtor's property at the moment a bankruptcy petition is filed." *Id.* at 591. Rather, it clarified that "§ 362(a)(3) prohibits collection efforts outside the bankruptcy proceeding that would change the status quo, while § 542(a) works within the bankruptcy process to draw far-flung estate property back into the hands of the debtor or trustee." *Id.*

The Court rejected the notion that § 362(a)(3) contained "an affirmative turnover obligation," instead holding that the reference to exercise of control "simply extended the stay to acts that would change the status quo with respect to intangible property and acts that would ***540** change the status quo with respect to tangible property without 'obtain[ing]' such property." *Id.* at 592. The Court concluded "that mere retention of estate property after the filing of a bankruptcy petition does not violate § 362(a)(3) of the Bankruptcy Code." *Id.*[8]

Fulton cited the Ninth Circuit's decision in *Del Mission* as a case on one side of the circuit split that the Court resolved. *Id.* at 590 n.1. Because the Court

adopted the view of the courts on the other side of the split, *Fulton* overruled *Del Mission* and other decisions taking the same position, such as *Bayley*.

The bankruptcy court here held that its Stay Violation Ruling was at odds with *Fulton*. It clarified that the Stay Violation Ruling was based on a violation of § 362(a)(3) for the City's failure to affirmatively seek to quash the writ of garnishment and unfreeze the three bank accounts. It had cited *Bayley* in support of its decision, which in turn relied on *Del Mission*. We agree with the bankruptcy court that its initial holding was no longer viable after *Fulton*. Simply stated, the City's inaction did not violate § 362(a)(3).

The bankruptcy court for the Middle District of Pennsylvania recently reached the same conclusion on similar facts. In *Margavitch v. Southlake Holdings, LLC (In re Margavitch)*, Case No. 5:19-bk-05353-MJC, 2021 WL 4597760 (Bankr. M.D. Pa. Oct. 6, 2021), the creditors served a prepetition writ of execution on the debtor's bank that froze his bank accounts. When the debtor filed a chapter 13 petition, the creditors refused to release the funds or otherwise terminate the attachment lien but took no other action to collect on the debt. The debtor sought sanctions for violation of the automatic stay. *Id.* at *2.

On cross-motions for summary judgment, the bankruptcy court held that *Fulton* dictated that the creditors' inaction did not violate the automatic stay. Considering § 362(a)(3), the court held that:

> Defendants admittedly took no post-petition affirmative action as to the garnished accounts. They maintained the status quo as of the petition date. They were not required to withdraw the attachment because to do so would put them in a more disadvantageous position than they had been as of the petition date and they were entitled to maintain the status quo.

Id. at *6 (citations omitted). The bankruptcy court further considered the other subsections of § 362(a) and concluded that the creditors' inaction did not amount to a stay violation.

[10]*Margavitch* is directly on point and comports with our analysis here. Where a creditor has executed a prepetition writ of garnishment against a debtor's bank account, it is under no affirmative obligation to release the funds and need only maintain the status quo.

[11]Mr. Stuart attempts to distinguish *Fulton* by arguing that it applied only to the exercise of control over estate property,[9] while the stay violation in this case arose from the City's opposition to his efforts to quash the writ of garnishment.

***541** Mr. Stuart is correct, but only to a point. It is true that *Fulton* considered only the retention of estate property under § 362(a)(3). However, *Fulton* dictates that the City had no affirmative duty to ensure the return of estate property to Mr. Stuart.

C. The bankruptcy court did not err in holding that the City did not otherwise violate the automatic stay.

We agree with the bankruptcy court that the City did not violate any other subsection of § 362(a).

1. The City did not "continue" a proceeding against Mr. Stuart under § 362(a)(1).

[12]Section 362(a)(1) prohibits the "continuation ... of a judicial, administrative, or other action or proceeding against the debtor ...." Mr. Stuart thinks that, in order to avoid the "continuation of" its action against him, the City had to quash the garnishment. We disagree.

In *Eskanos & Adler, P.C.*, the Ninth Circuit held that a creditor must "dismiss or stay" pending collection actions:

> The continuation against judicial actions includes the maintenance of collection actions filed in state court.... A party violating the automatic stay, through continuing

> a collection action in a non-bankruptcy forum, must automatically **dismiss or stay such proceeding** or risk possible sanctions for willful violations pursuant to § 362(h).

309 F.3d at 1214 (emphasis added). The court emphasized that "the automatic stay requires an immediate freeze of the status quo by precluding and nullifying post-petition actions." *Id.*

This leaves the question whether it is sufficient to simply stay a case or whether dismissal is required. In the *Eskanos* case, the creditor filed a new action against the debtor after the petition date. The Ninth Circuit repeatedly referred to it as a "post-petition collection action." *Id.* at 1213. In such a case, the creditor has disturbed the status quo existing at the petition date by filing a new lawsuit. In order to restore the status quo, the creditor must dismiss the postpetition action. But in this case, the action was pending and the garnishment existed when Mr. Stuart filed his petition. Leaving the action and the garnishment in place did not disturb the status quo. *Cf. Perryman v. Dal Poggetto (In re Perryman)*, 631 B.R. 899, 903–04 (9th Cir. BAP 2021) (holding that a postpetition " 'continuance' or status hearing in a stayed nonbankruptcy proceeding" is not a "continuation of a judicial proceeding" under § 362(a)(1) because those "actions did not disturb the status quo"). Therefore, staying the case was sufficient to avoid "continuation" in violation of § 362(a)(1).

The City fulfilled its duty by taking prompt steps to stay the case. Mr. Stuart filed his petition on a Saturday; the City learned of the bankruptcy petition on the following Monday or Tuesday, May 6 or 7; and it filed a motion to stay the State Court Action on Tuesday, May 7.[10]

Mr. Stuart argues that the City "actively objected to the release of funds." This misstates the record. Although the City stated that it opposed quashing the writ of garnishment, it indicated in e-mail correspondence and twice in its response to Mr. ***542** Stuart's motion "that it does not oppose release of the funds by [BOA] and does not object to a court order instructing [BOA] to release the funds."

Mr. Stuart argues that a creditor has an affirmative obligation to dismiss an existing writ of garnishment. He primarily relies on *In re Mims*, 209 B.R. 746 (Bankr. M.D. Fla. 1997), where the bankruptcy court held that the creditor had an affirmative duty to release bank accounts frozen pursuant to a prepetition writ of garnishment. The court said that "a garnishment action is unique insofar as it requires affirmative action to comply with the requirements of the automatic stay." *Id.* at 748.

In contrast, the bankruptcy court for the Middle District of Pennsylvania held in *Margavitch* that "§ 362(a)(1) was not violated because Defendants did nothing to further or 'continue' the garnishment process. Nothing has been alleged in the record indicating that the status quo was somehow changed regarding the [bank accounts] after the bankruptcy petition was filed." 2021 WL 4597760, at *8.

[13]Neither party has cited any binding Ninth Circuit authority that dictates whether a creditor has an affirmative duty to dismiss a prepetition writ of garnishment under § 362(a)(1), and we have found none. We think that the decision in *Margavitch* comports more closely than *Mims* with the Ninth Circuit's holding in *Eskanos*, which merely requires a creditor to "dismiss or stay" a judicial proceeding. In this case, the City promptly sought a stay of the State Court Action and took no further steps to advance that case. The failure to affirmatively release the frozen bank account funds, in and of itself, is not a violation of § 362(a)(1). *See id.*[11]

2. The City did not seek to enforce a prepetition judgment against Mr. Stuart under § 362(a)(2).

[14]Mr. Stuart contends that the City violated § 362(a)(2) when it sought to enforce the State Court Judgment by continuing the writ of garnishment. We disagree.

Subsection (a)(2) prohibits "the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title[.]" § 362(a)(2).

Mr. Stuart again argues that the City opposed his efforts to quash the writ of garnishment. But as we discussed above, the City took no position on whether the state court should order the release of the account funds. The bankruptcy court was correct that the City did not do anything to enforce the State Court Judgment. *See In re Margavitch*, 2021 WL 4597760, at *8 ("[T]he failure to

withdraw a valid pre-petition attachment lien cannot be construed as, or equated with, taking an affirmative action to enforce a judgment. The Court concludes that Defendants' passive maintenance of its valid pre-petition attachment lien in no way changed the status quo and therefore, did not constitute a violation of § 362(a)(2).").

Mr. Stuart claims that the City's stated intent clearly indicated that it meant to pursue the State Court Judgment in violation ***543** of the automatic stay. The City represented to the state court that it was concerned that, if Mr. Stuart obtained the frozen funds, he could quickly dismiss his bankruptcy case, thus frustrating the purpose of the garnishment. The City's concern with a hypothetical situation is irrelevant; it only reflected the City's desire to maintain the status quo.

Mr. Stuart relies on the Ninth Circuit's unpublished decision in *Bayley*. In that case, the Ninth Circuit upheld the finding of a stay violation under subsection (a)(2), where the creditor "direct[ed] the Sheriff to hold the levied funds ...." 678 F. App'x 593. In contrast, in the present case, the City did not direct BOA as to the postpetition disposition of the frozen funds and in fact repeatedly stated that it would not oppose the release of the funds. In other words, unlike in *Bayley*, the City did not take any affirmative action to enforce or further the garnishment.

Similarly, *In re Banks*, 253 B.R. 25 (Bankr. E.D. Mich. 2000), is distinguishable. The creditor obtained relief from the automatic stay but was unaware that the order lifting the stay was itself stayed for ten days pursuant to Rule 4001(a)(3). The creditor obtained and executed on a writ of restitution during the ten-day period and refused to vacate it. In other words, the creditor took action postpetition in violation of the automatic stay (before the bankruptcy court's order lifting the automatic stay went into effect). The bankruptcy court found that the creditor violated § 362(a)(1). *Id.* at 30. In the present case, the City both obtained and executed the writ of garnishment prepetition, which did not violate the automatic stay. It did not take any action postpetition to enforce the writ.

3. The City did not take any act to obtain estate property under § 362(a)(3).

[15]Mr. Stuart further argues that the City's state court filings constituted an act to obtain possession of the garnished funds. He contends that the City had power and authority over the frozen funds, so it had an affirmative obligation to withdraw the writ and make the funds available to Mr. Stuart. We agree with the bankruptcy court that the City took no "act" in violation of the automatic stay.

Section 362(a)(3) prohibits "any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate[.]"

As the bankruptcy court correctly held, *Fulton* precludes Mr. Stuart's argument that the City took any act to "exercise control over property of the estate." We also agree with the bankruptcy court that the City did not take any "act to obtain possession of property of the estate" when it did not immediately move to quash the writ of garnishment. On the petition date, the City had already obtained the writ of garnishment, and BOA had frozen the three bank accounts. There was no further "act to obtain possession." The City's acts (or omissions) merely preserved the status quo.[12]

***544 4. The City did not take any other "act" against Mr. Stuart in violation of § 362(a)(6).**

[16]Finally, Mr. Stuart argues that the City's refusal to dismiss the writ of garnishment and desire to freeze the bank accounts indefinitely violated subsection (a)(6). For the reasons discussed above, we disagree.

Section 362(a)(6) prohibits "any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title[.]" Mr. Stuart repeats arguments that he raised in connection with the other subsections.

As we explained above, the City did not do anything to enhance its position and only sought to maintain the status quo. *See In re Margavitch*, 2021 WL 4597760, at *7 ("[T]he mere retention of a valid pre-petition state court attachment or lien without more, is not a violation of § 362(a)(4)-(6)."). The City did not take any act to "collect, assess, or recover" a claim against Mr. Stuart, because everything was stayed. Further, it stated multiple times that it did not oppose the release of the frozen funds.

CONCLUSION

Because the City immediately asked the state court to stay the case and did nothing to change the status quo that existed when Mr. Stuart filed his bankruptcy petition, it did not violate the automatic stay. We AFFIRM.

All Citations

632 B.R. 531, 71 Bankr.Ct.Dec. 12, 2021 Daily Journal D.A.R. 12,145

Footnotes

1 Unless specified otherwise, all chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, all "Rule" references are to the Federal Rules of Bankruptcy Procedure, and all "Civil Rule" references are to the Federal Rules of Civil Procedure.

2 Mr. Stuart apparently faxed a copy of the petition to the City on May 4, a Saturday, but the offices were closed, and the City did not receive it until Monday.

3 Mr. Stuart also sought sanctions against the City's attorneys. In the remainder of this opinion, the term "City" generally includes its attorneys.

4 The Stay Violation Motion was the third such motion filed by Mr. Stuart against the City. The BAP affirmed the bankruptcy court's denial of his previous motions. *Stuart v. City of Scottsdale (In re Stuart)*, BAP No. AZ-19-1332-LBT, 2020 WL 4334120 (9th Cir. BAP July 28, 2020).

5 The bankruptcy court held that the City's bankruptcy counsel did not violate the automatic stay and entered a separate order denying the Stay Violation Motion as to them. That order is not part of this appeal.

6 While the Sanctions Motion was pending, Mr. Stuart filed a motion for leave to amend to add Mrs. Stuart as a party. The court's Reconsideration Order denied that motion. Mr. Stuart does not challenge that part of the order on appeal.

7 The Court acknowledged that an omission can be an "act" in some contexts but maintained that "the language of § 362(a)(3) implies that something more than merely retaining power is required to violate the disputed provision." 141 S. Ct. at 590.

8 The Court explicitly limited its holding to § 362(a)(3), 141 S. Ct. at 592, and Justice Sotomayor stated in her concurrence that the Court did not decide whether the city's actions violated any other subsection of § 362(a),

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id. (Sotomayor, J., concurring).

9 Mr. Stuart argues that *Fulton* cannot apply, because the City never had physical possession of the bank account funds. We reject this argument; nothing in § 362(a)(3) requires actual or physical possession of estate property. *See In re Margavitch*, 2021 WL 4597760, at *6 (rejecting this exact argument).

10 Mr. Stuart further argues that the City was "disingenuous" when it filed the motion for stay, because the State Court Action was already stayed by a previous order. To the contrary, the City's actions suggest that it understood its duty to discontinue any prepetition collection action and sought to make clear that it intended to comply with the automatic stay.

11 Many of Mr. Stuart's arguments conflate a judicial proceeding with the retention of estate property. While discussing subsection (a)(1), he cites cases imposing on creditors an obligation to return property under subsection (a)(3). For example, he relies on both *In re Hernandez*, 468 B.R. 396 (Bankr. S.D. Cal.), *aff'd*, 483 B.R. 713 (9th Cir. BAP 2012), and *In re Johnson*, 262 B.R. 831 (Bankr. D. Idaho 2001). However, those cases cited *Del Mission* and other cases relying on § 362(a)(3) regarding the retention of estate property; those cases were effectively overturned by the U.S. Supreme Court's *Fulton* decision.

12 We emphasize that the City's garnishment did not capture any more funds postpetition. The result would likely be different, as in certain cases cited by Mr. Stuart, *e.g.*, *In re LeGrand*, 612 B.R. 604 (Bankr. E.D. Cal. 2020), if this were a wage garnishment which attached to the debtor's postpetition wages or a bank account garnishment that encompassed postpetition deposits to the account. Here, neither BOA nor the City was actively collecting any debt from Mr. Stuart; staying the State Court Action and maintaining the freeze on the accounts was merely a continuation of the status quo as it existed on the petition date and collected nothing further from Mr. Stuart.

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Cases From Outside of the Ninth Circuit

31 F.4th 1014
United States Court of Appeals, Seventh Circuit.

In the MATTER OF: Marcella M. MANCE, Debtor,
City of Chicago, Appellant,
v.
Marcella M. Mance, Appellee.

No. 21-1355
|
Argued October 29, 2021
|
Decided APRIL 21, 2022

Synopsis
Background: Chapter 7 debtor sought to avoid city's lien on her vehicle for unpaid parking tickets. The United States Bankruptcy Court for the Northern District of Illinois, Jacqueline P. Cox, J., 611 B.R. 857, ruled that the lien was judicial and avoidable. City appealed. The United States District Court for the Northern District of Illinois, Andrea R. Wood, J., 625 B.R. 384, affirmed. City appealed.

[Holding:] The Court of Appeals, Hamilton, Circuit Judge, held that city's impoundment lien on debtor's vehicle was obtained by adjudicating traffic violations and did not arise solely by force of statute, and therefore was a "judicial lien."

Affirmed.

Procedural Posture(s): On Appeal; Motion to Avoid Lien on Exemption Impairment Grounds.

West Headnotes (11)

[1] **Bankruptcy**Conclusions of law; de novo review

Classification of a lien under the Bankruptcy Code is a question of law that the Court of Appeals reviews de novo.

[2] **Bankruptcy**Liens and security interests in general

Bankruptcy Code sorts liens into three mutually exclusive categories: statutory liens, judicial liens, and security interests.

[3] **Bankruptcy**Judicial liens; attachment and garnishment

Bankruptcy Code's definition of a judicial lien, as obtained by judgment, levy, sequestration, or other legal or equitable process or proceeding, has an element of causation inherent in the phrase "obtained by." 11 U.S.C.A. § 101(36).

[4] **Bankruptcy**Statutory Liens
BankruptcyJudicial liens; attachment and garnishment

Classification of a lien as "judicial" and thus avoidable, or as "statutory" depends on the events, if any, that must occur before the lien attaches. 11 U.S.C.A. §§ 101(36, 53), 522(f).

[5] **Mechanics' Liens**Time of Accrual or Commencement

Statute provides a mechanic a lien on improved property as soon as payment for the mechanic's work on the property is due and goes unpaid; the mechanic need not go to a judge to secure a lien,

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rather, the lien arises solely by statute once the condition, namely, a lack of payment, occurs.

[6] **Bankruptcy** Mechanics' or laborers' liens

Mechanic's lien may be perfected by filing the lien with a county clerk or similar official, but that filing is not considered a legal or equitable process or proceeding within the Bankruptcy Code's definition of a "judicial lien." 11 U.S.C.A. § 101(36).

[7] **Mechanics' Liens** Time of Accrual or Commencement

Mechanics' lien attaches to property automatically when debtor fails to make payment for services due; no judicial or similar process is needed.

[8] **Bankruptcy** Judicial liens

City's impoundment lien on Chapter 7 debtor's vehicle was obtained by adjudicating traffic violations and did not arise solely by force of statute, and therefore was a "judicial lien," and not a "statutory lien," that debtor could avoid on exemption-impairment grounds. 11 U.S.C.A. §§ 101(36, 53), 522(f).

[9] **Bankruptcy** Statutory Liens

Fact that lien resulted from process that is purely creature of statute is not sufficient to classify lien as "statutory" under Bankruptcy Code. 11 U.S.C.A. § 101(53).

[10] **Constitutional Law** Parking and towing

In case of traffic violation that results in immediate tow of vehicle, city must offer adequate postdeprivation procedures to conform with due process. U.S. Const. Amend. 14.

[11] **Bankruptcy** Taxes

Tax liens are unquestionably "statutory" liens under Bankruptcy Code. 11 U.S.C.A. § 101(53).

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division. No. 1:20-cv-01266 — **Andrea R. Wood**, *Judge.*

Attorneys and Law Firms

Daniel P. Lindsey, Miriam Veronica Hallbauer, David S. Yen, Attorneys, Legal Aid Chicago, Chicago, IL, for Debtor-Appellee.

Myriam Z. Kasper, Attorney, Office of the Corporation Counsel, Chicago, IL, Ellen W. McLaughlin, Attorney, City of Chicago Law Department, Chicago, IL, for Appellant.

Before Sykes, Chief Judge, and Kanne and Hamilton, Circuit Judges.

Opinion

Hamilton, Circuit Judge.

This appeal presents a new chapter in a long-term effort

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by the City of Chicago to collect parking fines and other traffic fees from drivers who seek bankruptcy protection. Some of the City's tactics have worked and others have not. See *In re Fulton*, 926 F.3d 916, 924 (7th Cir. 2019) (City's refusal to turn over vehicles to petitioners during bankruptcy proceedings violated automatic stay), vacated and remanded sub nom. *City of Chicago v. Fulton*, —— U.S. ——, 141 S. Ct. 585, 208 L.Ed.2d 384 (2021); *In re Steenes*, 942 F.3d 834, 839 (7th Cir. 2019) (vehicular tickets incurred during course of a Chapter 13 bankruptcy are administrative expenses that must be paid in full).

The issue in this appeal is whether the City's possessory lien on a vehicle that it impounds due to unpaid tickets should be deemed a "judicial lien" or a "statutory lien" under the Bankruptcy Code. If the lien is judicial, all parties agree, it is avoidable in bankruptcy under 11 U.S.C. § 522(f). If the lien is instead deemed statutory, it is not avoidable under the same provision.

We agree with the bankruptcy and district courts that the City's possessory lien on impounded vehicles is properly classified as judicial and therefore avoidable. Part I lays out the stakes of this particular issue. Part II explains how judicial and statutory liens are defined in the Bankruptcy Code. Part III outlines the specific procedures the City must follow before it can impose a lien on an impounded vehicle. Part IV explains why a lien that flows from these procedures is judicial.

I. *The Stakes*

This case may appear to be a technical dispute with modest stakes, but it's a test case that is important to the City and will affect many drivers. Outstanding debt for Chicago traffic tickets surpassed $1.8 billion last year.[1] On average, the City issues around three million tickets a year, and by one recent estimate, revenue from those tickets in 2016 exceeded a quarter of a billion dollars and constituted seven percent of the City's operating budget. Melissa Sanchez & Sandhya Kambhampati, *Driven into Debt: How Chicago Ticket Debt Sends Black Motorists into Bankruptcy*, ProPublica Ill. (Feb. 27, 2018), https://features.propublica.org/driven-into-debt/chicago-ticket-debt-bankruptcy.

As the dockets in this court and the Northern District of Illinois show, aggressive ticketing practices may help push many drivers into bankruptcy. *Id.* (explaining that "[p]arking, traffic and vehicle compliance tickets prompt so many bankruptcies the court [in Chicago] [led] the nation in Chapter 13 filings" at the time); see also *Table F-2—Bankruptcy Filings (December 31, 2019)*, U.S. Courts, https://www.uscourts.gov/statistics/table/f-2/bankruptcy-filings/2019/12/31 (last visited Apr. 21, 2022) (Northern District of Illinois led nation in non-business Chapter 13 filings with 15,851 cases in 2019). Even with recent reforms to ticketing practices, bankruptcy filings remain high by comparison to other districts. *Table F-2—Bankruptcy Filings (December 31, 2021)*, U.S. Courts, https://www.uscourts.gov/statistics/table/f-2/bankruptcy-filings/2021/12/31 (last visited Apr. 21, 2022) (in 2021 the Northern District of Illinois had the second most non-business Chapter 13 filings (5,198)).

When a vehicle owner's parking-ticket debt accumulates, the City has the legal right to impound the vehicle and can eventually sell the vehicle to help pay off the debt. If the impoundment lien can be discharged in bankruptcy, however, the owner may be able to recover her vehicle through the bankruptcy court. Classifying an impoundment lien as judicial or statutory can make the difference between, on one hand, allowing drivers to avoid a debt and denying the City the sums owed, and on the other hand the owner permanently losing the vehicle and putting more money in the hands of the City.

The foundation for this particular issue was laid in 2016. See *Fulton*, 926 F.3d at 920. The City Council passed a new ordinance that granted the City a lien on impounded vehicles for ticket debts. Municipal Code of Chicago ("M.C.C.") § 9-92-080(f). Once a driver incurs the needed number of outstanding tickets and final liability determinations, the City is authorized to impound her vehicle and to attach a possessory lien. The amount of the lien is based on how much the driver owes in unpaid traffic tickets, plus additional fees. § 9-100-120(d)(2).

Many drivers cannot afford to pay their outstanding tickets and fees, let alone the liens imposed on their cars through this process. As a result, some drivers declare bankruptcy and seek to avoid them. Debtor-appellee Marcella Mance, for instance, incurred several unpaid parking tickets and saw her car impounded and subject to a possessory lien that totaled $12,245, more than four times her car's value. Facing this liability with a monthly income of $197 in food stamps, Mance filed for bankruptcy under Chapter 7 and sought to avoid the lien under 11 U.S.C § 522(f). When a vehicle owner files for bankruptcy through Chapter 7, she can avoid a lien under § 522(f) if the lien qualifies as judicial and its value exceeds the value of her exempt property (in this

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case, her car). Conversely, if the lien is statutory, it is not avoidable under the same provision.[2]

The bankruptcy and district courts concluded that the lien was judicial and avoidable. Both courts reasoned that the lien was tied inextricably to the prior adjudications of Mance's parking and other infractions, so it did not arise solely by statute, as the Bankruptcy Code requires for a statutory lien. As the district court explained in its opinion in this case: "There is simply no way to disaggregate the final determinations of liability from the lien resulting from immobilization. ... Without the requisite number of judgments, the City would have no right to immobilize the vehicles and no liens could arise." *City of Chicago v. Howard*, 625 B.R. 384, 390 (N.D. Ill. 2021).[3]

II. *Lien Definitions in the Bankruptcy Code*

[1] [2]The classification of a lien under the Bankruptcy Code is a question of law that we review de novo. *In re Willett*, 544 F.3d 787, 790 (7th Cir. 2008). The Code sorts liens into three mutually exclusive categories—statutory liens, judicial liens, and security interests. *In re Financial Oversight & Management Board for Puerto Rico*, 899 F.3d 1, 10 (1st Cir. 2018); *In re Wigfall*, 606 B.R. 784, 786–87 (Bankr. N.D. Ill. 2019); see also S. Rep. No. 95-989, at 25 (1978), as reprinted in 1978 U.S.C.C.A.N. 5787, 5811 ("Those three categories are mutually exclusive and are [exhaustive] except for certain common law liens."). Only the first two are relevant here. The parties agree that Mance satisfies all the requirements for discharge under 11 U.S.C. § 522(f) if her lien is considered judicial, so the classification is decisive.

A. *The Statutory Text*

We begin our analysis with the statutory text. The Bankruptcy Code defines judicial and statutory liens in 11 U.S.C. § 101. Here is each definition in full:

> (36) The term "judicial lien" means lien obtained by judgment, levy, sequestration, or other legal or equitable process or proceeding.
>
> ...
>
> (53) The term "statutory lien" means lien arising solely by force of a statute on specified circumstances or conditions, or lien of distress for rent, whether or not statutory, but does not include security interest or judicial lien, whether or not such interest or lien is provided by or is dependent on a statute and whether or not such interest or lien is made fully effective by statute.

§ 101(36), (53).

[3]Both definitions focus on the events (or the lack thereof) that precede creation of the lien. The two definitions use distinct language to describe how the two different types of liens arise. We see this in the use of "arising solely" for statutory liens versus "obtained by" for judicial liens. "Solely" seems clear enough and signals that prior legal proceedings leading to a lien would exclude the lien from the category of statutory liens. The definition of a judicial lien—"obtained by judgment, levy, sequestration, or other legal or equitable process or proceeding," § 101(36)—has an "element of causation inherent in the phrase 'obtained by.' " See *Field v. Mans*, 516 U.S. 59, 66, 116 S.Ct. 437, 133 L.Ed.2d 351 (1995) (interpreting § 523(a)(2), which prohibits discharge of certain debts "obtained by ... false pretenses, a false representation, or actual fraud"). The statutory definition of a judicial lien indicates that the term applies when the lien is caused by or results from the broad categories of process identified in the latter part of the definition. These textual differences are noted in the history of the Bankruptcy Reform Act of 1978. The House and Senate reports on the Act explained: "A statutory lien is only one that arises automatically, and is not based on an agreement to give a lien or on judicial action." H.R. Rep. No. 95-595, at 314 (1977), as reprinted in 1978 U.S.C.C.A.N. 5963, 6271; S. Rep. No. 95-989, at 27, as reprinted in 1978 U.S.C.C.A.N. at 5811; see also 5 Collier on Bankruptcy ¶ 545.01 (16th ed. 2021).

[4]Under these definitions, classification of a lien depends on the events, if any, that must occur before the lien attaches. *In re Schick*, 418 F.3d 321, 324 (3d Cir. 2005) ("The relevant inquiry is to determine the nature of the [ ] lien, i.e., whether it arises solely by force of statute, or whether it results from some type of judicial process or proceeding."); see also 2 Collier on Bankruptcy ¶ 101.53 ("[A] judicial lien arises only by virtue of judicial proceedings in the absence of which there would not be such a lien. The statutory lien by definition arises without any judicial proceeding." (footnote omitted)).

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B. *Illustrations*

[5] [6] [7]Common examples of statutory and judicial liens are generally consistent with this focus on the prior events needed for the lien to arise and attach to property. Take mechanics' liens first, often cited as an example of a statutory lien. See, e.g., *Schick*, 418 F.3d at 324; *In re Cunningham*, 478 B.R. 346, 350 (Bankr. N.D. Ind. 2012) ("Case law throughout the country has routinely determined that a mechanic's lien, or similar liens arising by means of a state's statutory enactment, are at their base statutory liens."); see also *id.* at 351 (collecting cases); H.R. Rep. No. 95-595, at 314, as reprinted in 1978 U.S.C.C.A.N. at 6271 (listing mechanics' liens in the examples of statutory liens, as well as materialmen's liens, warehousemen's liens, and tax liens). In simple terms, a statute provides a mechanic a lien on improved property as soon as payment for the mechanic's work on the property is due and goes unpaid. The mechanic need not go to a judge to secure a lien; rather, the lien arises solely by statute once the condition—a lack of payment—occurs. A mechanic's lien may be perfected by filing the lien with a county clerk or similar official, but that filing is not considered a "legal or equitable process or proceeding" within the definition of a judicial lien. 11 U.S.C. § 101(36); see *Schick*, 418 F.3d at 326, citing *In re Fennelly*, 212 B.R. 61, 65 (D.N.J. 1997) ("The mere ministerial act of recording the lien does not create the requisite legal process or proceeding required to be a judicial lien."). The critical point is that a mechanic's lien attaches to the property automatically when the debtor fails to make a payment for the services due. Accord, *Wigfall*, 606 B.R. at 787. No judicial or similar process is needed.[4]

Contrast this example of a statutory lien with the textbook judicial lien: a court-ordered money judgment. There are several ways a dispute could make its way into a court and result in a money judgment. But before the lien can arise at all, a court must enter judgment for the winning creditor. That party then records it as a lien on the losing party's property. Because the lien is "obtained by" a court proceeding, it is considered judicial. 2 Collier on Bankruptcy ¶ 101.36; see also *Schick*, 418 F.3d at 328 ("[F]or a lien to be judicial, there must be some judicial or administrative process or proceeding that ultimately results in the obtaining of the lien.").

As we will see next, Chicago's impoundment lien in this case lies somewhere in between these easy illustrations. We find decisive the substantial quasi-judicial proceedings needed for the City to obtain an impoundment lien. The City's possessory lien thus did not arise "solely" by statute.

III. *The City's Lien Program*

To classify the City's impoundment lien, we examine how it arises or is obtained, beginning with unpaid tickets and continuing through the process of impoundment and attachment of the lien.

First, the owner must accrue the required number of traffic violations and final determinations. A car may be impounded only after an owner has three or more "final determinations of liability," or two final determinations that have been outstanding for more than a year, "for parking, standing, compliance, automated traffic law enforcement system, or automated speed enforcement system violation[s]." M.C.C. § 9-100-120(b).

The underlying traffic violation undergoes an administrative process before it turns into a final determination of liability. First, a police officer or other official observes and records a traffic or parking violation. The official then gives the operator of the vehicle a notice of the violation (e.g., by hand or by placing it on the vehicle). § 9-100-030(b)(i)–(ii). If, however, the operator drives away before the official can serve the notice, the City mails the owner of the vehicle a notice of the traffic violation. § 9-100-030(b)(iii). Alternatively, an automated speed or traffic system records a violation and the City sends a notice to the registered owner. § 9-100-045.

The owner can contest the charged violation in an in-person proceeding or by writing. §§ 9-100-050, -055, -070, -080. If the owner loses or fails to contest the violation, a determination of liability is entered. § 9-100-090. The owner can then file an appeal under the Illinois Administrative Review Law. *Id.*; see also *Van Harken v. City of Chicago*, 305 Ill.App.3d 972, 239 Ill.Dec. 223, 713 N.E.2d 754, 759 (1999). If she loses on appeal or fails to contest the liability determination, the City obtains a "final determination." § 9-100-100. In *Fulton*, we concluded that these final determinations of liability amounted to "money judgments." See 926 F.3d at 930–31, vacated on other grounds, —— U.S. ——, 141 S. Ct. 585, 208 L.Ed.2d 384 (2021).

At that point, the owner must pay the fine for the violation. § 9-100-100(b). "The fines for violations of the City's Traffic Code range from $25 (*e.g.*, parallel parking violation) to $500 (*e.g.*, parking on a public street without displaying a wheel tax license emblem)." *Fulton*, 926

F.3d at 920, citing § 9-100-020(b)–(c). These fines can grow quickly. "Failure to pay the fine within twenty-five days automatically doubles the penalty" in most cases. *Id.*, citing § 9-100-050(e).

If the fines go unpaid, the next enforcement step for the City is impoundment. That step requires more legal process. The City must issue notice of the impending vehicle immobilization to the owner. § 9-100-120(b). The owner then has twenty-one days to either pay the fines or petition for a hearing and appear in person to prove that she is not liable for the outstanding tickets. If the owner fails to file a timely petition or if her petition is denied, a final determination of eligibility is entered.

After such a determination of liability and eligibility for impoundment, the City may physically immobilize the car (with a "boot," for example). § 9-100-120(c). If the owner does not obtain release of the immobilizing device within twenty-four hours or request additional compliance time, the City can finally tow the car to an impoundment facility. *Id.* When the vehicle is immobilized or impounded, the outstanding ticket debt becomes a lien on the vehicle: "Any vehicle impounded by the City or its designee shall be subject to a possessory lien in favor of the City in the amount required to obtain release of the vehicle." § 9-92-080(f); § 9-100-120(j) (same for immobilized vehicles).[5]

Turning to the details of this case, at the time of appellee Mance's bankruptcy filing, the City's lien on her vehicle totaled $12,245 on a car allegedly worth $3,000. The amount of the lien is based on the amount of the outstanding tickets, the fees accumulated from storage and towing costs, and even attorney fees incurred by the City in the immobilization process, among other costs. § 9-100-120(d)(2).[6]

IV. *Classification of the City's Lien*

A. *The Lien Is "Obtained by" Adjudicating the Traffic Violations*

[8]The very last step of the lien attachment is automatic. Under the terms of the city ordinance, the lien arises upon impoundment, without further action by a judge or quasi-judicial official. On that basis, the City contends the impoundment lien is a statutory lien, asserting that it arises "solely" by statute. Like our colleagues on the bankruptcy and district courts, however, we see the issue differently. Under the statutory definitions of the two types of liens, we do not think we can ignore all the prior legal process that must occur before the City's possessory lien arises. The lien is "obtained by ... other legal or equitable process or proceeding," 11 U.S.C. § 101(36), in that the lien arises from and is based upon the prior quasi-judicial adjudications and money judgments that determine the lien's validity and amount. The lien is judicial and avoidable in bankruptcy.

The City asks us to treat this prior process as irrelevant. The City relies on the language "shall be subject to a possessory lien" in the ordinance. The City treats the needed number of tickets, final adjudications, and later impoundment as mere "conditions" that trigger the lien. In the City's view, those conditions should have no bearing on the classification of the lien because they do not govern how the lien "arises."

[9]The City's narrow focus on only the very last step leading to attachment of an impoundment lien is not consistent with the statutory definition of a judicial lien. A judicial lien is not a statutory lien, "whether or not such interest or lien is provided by or is dependent on a statute and whether or not such interest or lien is made fully effective by statute." 11 U.S.C. § 101(53). This language makes clear that the fact that a lien resulted from a process that is "purely a creature of statute" is not sufficient to classify the lien as statutory. *In re Weatherspoon*, 101 B.R. 533, 535 (Bankr. N.D. Ill. 1989) (citation omitted). Put differently, "[t]he fact that a statute describes the characteristics and effects of a lien does not by itself make the lien a statutory lien." 2 Collier on Bankruptcy ¶ 101.53. That description fits the City's impoundment lien in this case. A statute (the ordinance) authorizes the lien and describes its characteristics and effects, but we must still consider whether the lien arises "solely by force of a statute on specified circumstances or conditions." § 101(53).

Under both definitions, the relevant inquiry is not whether a statute authorizes or governs the lien but what is necessary for the lien to arise. If the lien requires a "judgment, levy, sequestration, or other legal or equitable process or proceeding," the lien is judicial. If the lien arises "solely" by statute once specific conditions are met, the lien is statutory. In the case of a Chicago impoundment lien, without the judicial or quasi-judicial procedures needed for final determinations for each traffic violation and without the quasi-judicial impoundment procedures, the City could not impose a lien on the indebted driver's vehicle. While the lien is authorized by and defined by statute, the City's possessory lien does not

arise "solely" by statute.

[10]To be sure, as Mance acknowledged at oral argument, liens on some impounded vehicles should be treated as statutory liens. If a driver has committed a violation under M.C.C. § 9-92-030, such as blocking an alleyway, obstructing traffic, parking in a "tow zone," or the like, the vehicle can be towed on the spot, without any prior judicial process. *Id.* The City then sends the vehicle owner notice after the fact. § 9-92-070. When a vehicle is towed for one of these violations, it is also subject to a lien. § 9-92-080(f) ("Any vehicle impounded by the City or its designee shall be subject to a possessory lien in favor of the City in the amount required to obtain release of the vehicle."); see also § 2-14-132(*l*) (same). Such violations lead to immediate impoundment liens that do not require advance notice to drivers or any other quasi-judicial procedures before they can be imposed. Instead, a car is automatically impounded upon a violation and subject to a lien.[7]

That automatic process is quite different from what happened here. For Mance, several legal proceedings had to be completed before impoundment. Vehicle owners who incur liens like Mance's therefore face judicial liens and can avoid them under 11 U.S.C. § 522(f). Vehicle owners whose violations resulted in immediate impoundment, by contrast, face statutory liens and cannot avoid them under the same provision.

Next, the City argues that if we agree with appellee Mance, we will create a circuit split with the Third Circuit's decision in *In re Schick*, 418 F.3d 321 (3d Cir. 2005). We are not convinced. There is a critical difference between the processes leading to the liens in the two cases.

Schick concluded that a lien held by the New Jersey Motor Vehicles Commission was a statutory lien. Under New Jersey law, a vehicle owner who committed a traffic violation faces potential surcharges in various situations, such as reaching a certain number of violation points or having been convicted of refusing to take a breathalyzer test, among other examples. The amount of the surcharges was dictated by "statute and administrative regulations." 418 F.3d at 324. If a driver failed to pay the surcharges, the Commission was entitled to a lien on the driver's property in the amount of the surcharges and interest. The Third Circuit concluded that such a lien held by the Commission was statutory and therefore not avoidable under 11 U.S.C. § 522(f).

The statutory scheme analyzed in *Schick* was markedly different from the impoundment process leading to Chicago's lien. The New Jersey statute pertained to only the surcharges, not the underlying vehicle violations. This bifurcated structure contributed to the court's view that "the underlying traffic proceeding charging the driver with a motor vehicle offense [was] too remote to constitute the required judicial process or proceeding necessary to find a judicial lien." 418 F.3d at 326. The underlying proceeding therefore bore "*no relation* to the creation of the lien in favor of the [Commission], which instead [arose] as a result of the filing of the certificate of debt and its docketing by the Clerk of the Superior Court." *Id.* (emphasis added).

Here, by contrast, the statutory structure does not separate the underlying vehicle violation and any fees imposed after the final determinations of the tickets, let alone the impoundment process. These steps are all tied together. Unlike the situation in *Schick*, Chicago's administrative structures for challenging tickets and pending impoundments are not too far removed from the impoundment lien. They are essential prerequisites for a valid impoundment lien, and they determine the amount of the lien.

In *Schick* the amount of the surcharge—and therefore the amount of the lien—was "set forth either in the statute or administrative regulation and [was] *not determined by the underlying proceeding against the driver*." 418 F.3d at 326 (emphasis added). The opposite is true here. The amount of the Chicago impoundment lien is determined precisely in and by the underlying proceedings. Indeed, to secure release, the driver must pay immobilization and impoundment costs, as well as "all amounts, including any fines, penalties, administrative fees ..., if any, and related collection costs and attorney's fees ... remaining due on each final determination for liability issued to the owner." M.C.C. § 9-100-120(d)(2). The City says correctly that the total amount of the lien is not limited to the underlying traffic fees, but all of the additional charges pertain to and result directly from the quasi-judicial processes leading up to the lien. In this respect, the situation here is similar to money judgments, which routinely include interest, court costs, and sometimes attorney fees and other associated costs, yet are considered judicial despite these tacked-on fees because the resulting liens do not arise "solely" by statute. The same is true here. The additional fees do not eliminate the link to the underlying traffic violations and adjudications. They strengthen it.

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B. *Tax Liens*

The City also argues that adopting Mance's position will call the classification of tax liens into question. Congress included tax liens in its examples of statutory liens in the legislative history of the Bankruptcy Code. H.R. Rep. No. 95-595, at 314, as reprinted in 1978 U.S.C.C.A.N. at 6271 ("Tax liens are also included in the definition of statutory lien."). The City contends, however, that federal tax liens result from judicial and quasi-judicial processes (under 26 U.S.C. §§ 6212(a), 6213(a), 6214(a), and 7482) that are similar to the processes leading to a Chicago impoundment lien. If these procedures must be followed before imposing a federal tax lien, yet everyone acknowledges that a tax lien is statutory, the City asks, how could our lien be judicial based on similar prior procedures?

[11]Tax liens are unquestionably statutory. E.g., *Financial Oversight & Management Board*, 899 F.3d at 11; *Schick*, 418 F.3d at 324; *IRS v. Diperna*, 195 B.R. 358, 360 (E.D.N.C. 1996); *In re O'Neil*, 177 B.R. 809, 811 (Bankr. S.D.N.Y. 1995). Our decision does not call this classification into question. We are merely evaluating the text of statutory provisions also provided by Congress to determine where the City's lien best fits under those definitions. Classifying the City's lien as judicial flows directly from the text. Congress is entitled to single out a particular category of liens and classify it accordingly. We do not disturb that prerogative or conclusion with this opinion.

Because Chicago's impoundment lien on Mance's vehicle did not arise solely by force of statute, the lien is a judicial lien for purposes of Mance's bankruptcy.

AFFIRMED.

All Citations

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Footnotes

1 Melissa Sanchez, *Chicago Mayor Lori Lightfoot Proposes Further Traffic Ticket Reforms to Help Low-Income Motorists*, ProPublica (Sept. 22, 2021, 5:10 PM), https://www.propublica.org/article/chicago-mayor-lori-lightfoot-proposes-further-traffic-ticket-reforms-to-help-low-income-motorists.

2 These figures come from Mance's Chapter 7 bankruptcy petition, i.e., Form 106. We accept Mance's declarations for the purposes of this appeal.

3 Mance's case was consolidated with that of another debtor (Cupree Howard) in the district court and initially on appeal. We dismissed Howard's appeal as moot before oral argument.

4 Perfection is necessary for the statutory lien's continued effectiveness and protection against other creditors. It also has implications under 11 U.S.C. § 545, which allows a bankruptcy trustee to avoid certain statutory liens. But the fact that a lien must be perfected does not transform it into a judicial lien. See 2 Collier on Bankruptcy ¶ 101.53 ("[M]erely because [statutory liens] require some form of judicial filing for their perfection against other creditors or continued effectiveness, they are not transformed into judicial liens. While the filing of the lien may determine whether it is perfected to the extent that it may not be avoided by the trustee under section 545, it does not transmute a statutory lien into a different kind of lien."

5 The City impounded and sold nearly 50,000 cars from 2011 to 2019. Elliott Ramos, *Chicago Seized and Sold Nearly*

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50,000 Cars Over Tickets Since 2011, Sticking Owners with Debt, WBEZ Chi. (Jan. 7, 2019, 5:01 AM), https://www.wbez.org/stories/chicago-seized-and-sold-nearly-50000-cars-over-tickets-since-2011-sticking-owners-with-debt/1d73d0c1-0ed2-4939-a5b2-1431c4cbf1dd.

6 The City offers various repayment plan options for eligible drivers that might eliminate some of those fees. See § 9-100-120(d)(1); see also §§ 9-100-160 (installment payment plans), -170 (Clear Path Relief Pilot Program). The parties have not indicated to the court that Mance is enrolled in any of those programs.

7 In the case of a violation that results in an immediate tow, the city must offer adequate post-deprivation procedures to conform with due process. See *Miller v. City of Chicago*, 774 F.2d 188, 192–96 (7th Cir. 1985) (City not required to provide notice to owners before towing stolen vehicles to satisfy due process); *Sutton v. City of Milwaukee*, 672 F.2d 644, 645–46, 648 (7th Cir. 1982) (pre-towing notice and opportunity to be heard not required to tow illegally parked cars, but adequate post-deprivation procedures are needed to provide due process); see also *Gable v. City of Chicago*, 296 F.3d 531, 539–40 (7th Cir. 2002) (due process rights not violated when City deprived plaintiffs of impounded vehicles because City was not deliberately indifferent and adequate post-deprivation remedies were available).

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