CONSUMER LAW UPDATE

Selected Cases Reported
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Automatic Stay

Denying Chapter 13 debtor's use of online portal for mortgage payments violated stay. The debtor requested only injunctive relief with no damage recovery, and the Court examined whether the debtor's prepetition access to the mortgage servicer's payment portal was akin to a contractual right that became property of the estate. The confirmed plan provided that arrearages would be paid through the trustee but that ongoing mortgage payments would be paid by the debtor, and the servicer's unilateral termination of the debtor's portal access made her direct payments more difficult. The servicer's denial of portal access was a stay violation. The opinion notes that a per se rule mandating such portal access would require appropriate congressional or regulatory action. In re Klemkowski, 664 B.R. 681 (Bankr. D. Md. 2024), Judge Harner.

In a case filed within one year of prior case dismissal, stay could not be extended after thirty days expired. The Bankruptcy Court had no authority under section 362(c)(3) to extend the stay after thirty days from the filing date. The opinion discusses application of Rule 9006(a)(1) in the calculation of the thirty-day period. The debtor's counsel had not moved for temporary extension of the stay or for expedited hearing on a motion to extend the stay, and the thirty days expired prior to hearing. In re Hardin, 664 B.R. 707 (Bankr. D. S.C. 2024), Judge Gasparini.

Appeals

Dismissal of pro se debtors' appeal was abuse of district court's discretion. When the debtors' appeal of the bankruptcy court's dismissal order was related to the court's grant of their attorney's withdrawal, the district court abused its discretion in dismissing the appeal. The Circuit Court's concurring opinion observes that when debtors' counsel withdraws from representation, there is a continuing duty to monitor the case until the withdrawal is granted. "The lesson is clear: when a lawyer moves for leave to withdraw, he must stay vigilant to any developments that might affect his clients while the motion is pending. The duty of representation does not disappear until the court grants the motion, and any lapse can trigger serious procedural consequences. The court, too, must recognize how the timing of its decisions can impact parties caught in the uncertainty of

shifting representation. The trustee shares this duty, ensuring that the administration of the bankruptcy estate is not imperiled due to such transitions." In re Parrott, 118 F.4th 1357, 1367 (11th Cir. 2024).

Avoidance

Lien avoidable under section 522(f) notwithstanding judgment based on fraud. Chapter 7 debtors claimed homestead exemption and moved to avoid judgment liens under section 522(f), but creditors asserted that the judgments were based on debts incurred by fraud. Citing *Law v. Siegel,* the Court lacked equitable authority to contravene the statutory provision in section 522(f). That section contains no fraud exception to lien avoidance. In re Mirabal, 2024 WL 4941044 (Bankr. D. N.M. Dec. 2, 2024), Judge Thuma. See also In re Dulaney, ___ B.R. ___, 2024 WL 5156296 (Bankr. S.D. Ohio Dec. 18, 2024), Judge Nami Khorrami, for analysis of requirements to avoid lien under section 522(f), including whether consent judgment created a judicial lien or a consensual security interest.

Discharge

Denial of discharge of taxes under section 523(a)(1)(C). Applying the Sixth Circuit's standards for exception from discharge of taxes under section 523(a)(1)(C), "the government must prove, by a preponderance of the evidence, that the debtor (i) engaged in evasive conduct; and (ii) acted with knowledge or deliberation in that evasion. *Stamper v. United States* (*In re Gardner*), 360 F.3d 551, 557-558 (6th Cir. 2004); *United States v. Storey*, 640 F.3d 739, 744–45 (6th Cir. 2011). The standard of proof notwithstanding, because an exception to discharge is a harsh remedy, actions brought to achieve this end should be 'strictly construed in favor of the debtor.' *Storey*, 640 F.3d at 743." Finding that the Chapter 7 debtor had engaged in conduct intended to evade IRS's tax collection, IRS satisfied section 523(a)(1)(C)'s exception from discharge. In re Stein, ___ B.R. ___, 2024 WL 4846081 (Bankr. W.D. Ky. Nov. 20, 2024), Judge Merrill.

Defense costs to county were nondischargeable under section 523(a)(7). Applying California's Government Claims Act, county's defense costs related to Chapter 7 debtor's action were nondischargeable governmental fines, penalties or forfeitures. In addition, the defense costs would be nondischargeable under section 523(a)(6). The debtor's

action had been dismissed as having been filed without reasonable cause and in bad faith. In re Harrington, ___ B.R. ___, 2024 WL 4836395 (Bankr. E.D. Cal. Nov. 19, 2024), Judge Klein.

Denial of discharge reversed. Affirming the District Court's decision that the Bankruptcy Court's findings of fact were clearly erroneous, the Sixth Circuit remanded for the Bankruptcy Court to enter discharge. The Chapter 7 trustee had objected to discharge under sections 727(a)(2)(A) and (B), based upon the debtors' application of tax overpayments for 2018 and 2019 to the following years' tax liabilities, with the trustee alleging that the overpayments were done with intent to hinder the trustee's collection of property of the estate. The Circuit Court construed section 727(a)(2)'s language to require "actual intent" of the "consequences of an act, not simply the act itself," 119 F.4th at 1046 (quoting Kawaauhau v. Geiger, 523 U.S. 57, 61-62 (1998)). Here, the evidence only showed that the debtors intended to pay tax creditors in preference to other creditors, and their preference intention did not satisfy section 727(a)(2)(B)'s requirement of intent to "hinder, delay, or defraud creditors." In re Wylie, 119 F.4th 1043 (6th Cir. 2024). See also In re Wylie, ___B.R. ___, 2024 WL 4532911 (Bankr. E.D. Mich. Oct. 18, 2024), Judge Tucker, for determination that one debtor's prepetition transfer of property to his mother was avoidable under section 548(a)(1)(B) when transfer was for less than reasonably equivalent value but transfer that preferred his mother over other creditors was not made with actual intent to hinder, delay or defraud other creditors.

Reopening case to allow proceeding to revoke discharge was denied. The creditor "failed to show cause for the delay between the deadline for objecting to discharge, the granting of the discharge, the closing of the case, and the filing of the Motion" to reopen the Chapter 7 case. As a result, the creditor did not satisfy section 727(d), which requires the objecting party to "show due diligence in investigating and responding to possible fraudulent conduct once he or she is aware of it or is in possession of facts such that a reasonable person in his or her position should have been aware of a possible fraud. (quoting *In re Vereen*, 219 B.R. 691, 696 (Bankr. D.S.C. 1997)." The motion to reopen was denied. In re Hoffman, 663 B.R. 292 (Bankr. D. S.C. 2024), Judge Burris.

Property of Estate and Exemptions

Retirement plan excluded from Chapter 7 estate. Agreeing with decisions from the Fifth and Seventh Circuits, a plain reading of section 541(c)(2) excludes from the bankruptcy estate retirement plans governed by ERISA, even if the plan is allegedly not tax qualified. ERISA's anti-alienation bar protects the plan from inclusion in the bankruptcy estate. McDonnell v. Gilbert (In re Gilbert), 120 F.4th 114 (3d Cir. 2024).

Community property was part of a bankruptcy estate. In a Chapter 7 case properly filed in Mississippi, the debtor's interest in California real property owned with non-filing spouse as community property under California law became property of the bankruptcy estate. The spouse, who was not a debtor in the Chapter 7 case, could not claim exemption in the property, and the Mississippi debtor's prior attempt to claim exemption in the property had been denied. It was not yet determined if the community property could be administered by the trustee or if the property had consequential value to the estate, because under section 726(c) "community property should be segregated from other property of the estate into a separate 'sub-estate' that is distributed in descending priority from subsections (c)(2) (A) through (D)." In re Freeman, 664 B.R. 334 (Bankr. N.D. Miss. Oct. 22, 2024), Judge Woodard.

Foreclosure was final before Chapter 13 filing. Applying Tennessee's Statute of Frauds and Uniform Electronics Transaction Act, a combination of documents, including emails between the parties, established that the pre-bankruptcy nonjudicial foreclosure sale was final, and the foreclosed home did not become property of the estate. In re Smith, 664 B.R. 740 (Bankr. E.D. Tenn. 2024), Judge Bauknight.

Chapter 13 Issues

Disposable Income

Ninth Circuit allows deduction of debtor's retirement contributions under section 541(b)(7). Creating a Circuit split on the issue, in a two to one decision, the Ninth Circuit held that under the plain language of section 541(b)(7)'s "hanging paragraph," which was enacted as part of BAPCPA, voluntary retirement contributions from the debtor to

employer-managed retirement plans are properly deducted from the calculation of disposable income. In so holding the Circuit panel overruled the BAP's decision in *Parks v. Drummond,* 475 B.R. 703 (B.A.P. 9th Cir. 2012), and disagreed with Circuit authority from the Sixth Circuit, *Burden v. Seafort,* 669 F.3d 662 (6th Cir. 2012). The opinion reviews bankruptcy court rulings on the issue after BAPCPA, as well as the pre-BAPCPA case law on retirement contributions. The majority of the panel concluded that section 541(b)(7)'s "statutory text unambiguously excludes voluntary contributions from a debtor's disposable income in a Chapter 13 case. The hanging paragraph reads: "except that such amount under this subparagraph shall not constitute disposable income as defined in section 1325(b)(2).'" The panel further concluded that Congress had intended to change the pre-BAPCPA consensus among courts that retirement contributions were included in disposable income. The panel then discussed three other interpretations on section 541(b)(7): "(1) includes all voluntary retirement contributions, both pre- and postpetition, under the definition of disposable income in Chapter 13; (2) excluded voluntary retirement contributions from the definition of disposable income, so long as the debtor was making those contributions prior to filing the Chapter 13 bankruptcy petition; and (3) exempts the six-month average of voluntary retirement contributions made prior to the declaration of bankruptcy." The panel concluded that the *Parks* approach did not give section 541(b)(7) "any meaning." The panel also rejected the *Seafort* approach as lacking "any textual support in the Bankruptcy Code, [with] no foundation in the Code to limit a debtor's disposable income to the debtor's prepetition contribution amount." The dissenting judge found the hanging paragraph to be ambiguous, adopting the Sixth Circuit's approach. Saldana v. Bronitsky, 122 F.4th 333 (9th Cir. 2024).

Fees and Costs

Reimbursement of force-place insurance premium was limited to reasonable cost to cover creditor's lien. The mortgage creditor sought reimbursement of its costs for force-place insurance, but the proof established that the creditor over-insured the property, incurring unnecessary costs. The reimbursement request must be reasonable, and the underlying mortgage did not provide for insuring over the amount of the lien. In re Blakey, 664 B.R. 221 (Bankr. W.D. Penn. 2024), Judge Taddonio.

Rule 3002.1 and HELOC documents support reasonable fees. Chapter 13 debtor moved to reduce fees charged by HELOC lender for its counsel's charge of $150 per payment change notice and $125 for each postpetition fee notice. The Court found the charges to be reasonable and allowable under Rule 3002.1 and the relevant HELOC documents. In re Cruz, 663 B.R. 792 (Bankr. D. Md. 2024), Judge Chavez-Ruark.

Plan default

Grace period to cure default did not offend the five-year plan limit. In an unpublished opinion, the District Court affirmed grant to the debtor of a grace period to cure plan default on the bifurcated mortgage claim. The objecting creditor argued that the grace period extended the plan beyond the 60 months permitted by sections 1322(d)(1) and 1329(c). Applying *In re Klaas,* 858 F.3d 820 (3d Cir. 1917), the District Court agreed with the Bankruptcy Court that a grace period was not equivalent to a plan extension beyond the statutory limit. While the Code limits plan confirmation or modification to the 60-month limit, under *Klaas* the Bankruptcy Court has discretion to allow debtors a grace period to cure plan arrearages. The opinion notes that the Tenth Circuit had rejected *Klaas* in *In re Kinney,* 5 F.4th 1136 (10th Cir. 2021). In re Harry, 2024 WL 4880300 (D. N.J. Nov. 24, 2024).

Discharge Injunction

Violation of section 524(i) may trigger emotional distress damages. First holding that the Chapter 13 debtors had sufficiently stated a cause of action against the mortgage servicer and note holder for failure to properly credit plan payments to cure defaults, the Bankruptcy Appellant Panel then held that on remand the creditor may be liable for emotional distress damages for violations of the discharge injunction, including section 524(i). "We have previously held that bankruptcy courts can award emotional distress damages as compensation for civil contempt. *Ocwen Loan Servicing, LLC v. Marino (In re Marino)*, 577 B.R. 772, 787 (9th Cir. BAP 2017), *aff'd in part & appeal dismissed in part*, 949 F.3d 483 (9th Cir. 2020), and we disagree with the bankruptcy court that *Taggart v. Lorenzen*, 587 U.S. 554 (2019) alters its authority to do so. In so holding, we relied on Ninth Circuit precedent allowing emotional distress damages for violations of the automatic stay. *In re Marino*, 577 B.R. at 787 (citing *Snowden v. Check Into Cash of*

Wash. Inc. (In re Snowden), 769 F.3d 651, 657 (9th Cir. 2014); *Dawson v. Wash. Mut. Bank., F.A. (In re Dawson)*, 390 F.3d 1139, 1149 (9th Cir. 2004)). . . .We are not persuaded that *Taggart* compels us to depart from our precedent in *Marino*." In re Valdellon, ___ B.R. ___, 2024 WL 5182900 (B.A.P. 9th Cir. Dec. 20, 2024).

Federal and State Tax entities did not violate discharge injunction by collection of interest accrued on nondischargeable taxes. Although the debtor had paid substantial portions of taxes in Chapter 13 plan, IRS and Franchise Tax Board were permitted to collect unpaid nondischargeable taxes and interest accruing on those taxes and the collection did not violate discharge injunction. The opinion cited *Bruning v. United States*, 376 U.S. 358, 363, for holding that "post-petition interest on an unpaid tax debt not discharged ... remains, after bankruptcy, a personal liability of the debtor." In re Feltmann, 663 B.R.119 (Bankr. M.D. Fla. 2024), Judge Geyer.

Dismissal and Conversion

Debtor could voluntarily dismiss case, notwithstanding contested debtor eligibility. Under the plain language of section 1307(b), the debtor had absolute right to dismiss the case. A creditor contested the right to dismiss based on allegation that debtor was ineligible to file under section 109(e). The Bankruptcy Court was required to dismiss the case without inquiring into the debtor's original eligibility. In re Powell, 119 F.4th 597 (9th Cir. 2024).

Factors to consider for dismissal under totality of circumstances. Citing Sixth Circuit authority, "there is substantial overlap between the factors used to determine good faith in the context of a dismissal under 11 U.S.C. § 1307(c) and good faith in the context of plan confirmation under 11 U.S.C. § 1325(a). (citing *Alt v. United States (In re Alt)*, 305 F.3d 413, 420 (6th Cir. 2002). These factors, however, are relevant not as an end in themselves as part of a mechanical counting of factors, but rather exist to guide the Court in its analysis of the 'key inquiry' – whether the debtor is seeking to abuse the bankruptcy process. *Alt*, 305 F.3d at 419. Even though it is appropriate for the court to consider the factors, if relevant, in the plan confirmation context when deciding dismissal under 11 U.S.C. § 1307(c), the court should be more reluctant to dismiss a case under § 1307(c).

. . .There is no presumption under 11 U.S.C. § 1307(c) that the case was filed in bad faith, and the burden of proving that the petition was filed in bad faith is on the moving parties. *Alt*, 305 F.3d at 420." In re Anthony, 664 B.R. 418 (Bankr. S.D. Ohio 2024), Judge Nami Khorammi.

Trustee Compensation

Requiring the trustee to refund compensation upon pre-confirmation dismissal does not violate Due Process Clause. The Bankruptcy Appellate Panel rejected the Chapter 13 trustee's argument that denial of compensation in cases dismissed prior to confirmation violated the Due Process Clause. The BAP was bound by *Evans v. McCallister (In re Evans)*, 69 F.4th 1101 (9th Cir. 2023), *cert. denied sub nom. McCallister v. Evans*, —— U.S. ——–, 144 S. Ct. 1004 (2024), in which "the Ninth Circuit held that a Chapter 13 trustee is only entitled to receive the percentage fee if the plan is confirmed; otherwise, if the case is dismissed or converted prior to confirmation, the trustee must return all of the debtor's plan payments to the debtor, and the trustee receives nothing." Trustee payments are governed by 28 U.S.C. § 586(e)(1) and 11 U.S.C. § 1326(b)(2), and the BAP found no constitutional violation by the requirement that compensation is conditioned on plan confirmation. Kerns v. Foss, ___ B.R. ___, 2024 WL 4749497 (B.A.P. 9th Cir. Nov. 12, 2024).

Attorneys

Chapter 13 attorney failed to show permission of debtors to affix their signature to certificate of completion of plan. Debtors' attorney violated Rule 9011 and was sanctioned $500, payable to debtors, for affixing debtors' signature to local form stating completion of Chapter 13 plan and request for discharge, when attorney did not provide documented permission of both debtors to sign the form on their behalf. It appeared that debtors were not eligible for discharge because of prior Chapter 7 discharge in a case filed within four years before order for relief in this case. In re Washington, 663 B.R. 685

(Bankr. D. S.C. 2024), Judge Gasparini. See also In re Lucas, 663 B.R. 301 (Bankr. D. S.C. 2024), Judge Gasparini, for similar violation by debtors' counsel.

Claims

Postpetition domestic support obligation was not included in allowable proof of claim. Although the Chapter 13 debtor was required to maintain payments on postpetition domestic support obligation in order to obtain confirmation of plan and discharge, such postpetition obligations were not to be included in former spouse's proof of claim. The Court construed section 502(b)(5) as permitting allowance of only prepetition domestic support claims. The opinion stresses that disallowance of the claim does not mean that the postpetition obligation is dischargeable under section 523(a)(5). Note that the definition of domestic support obligation in section 101(14A) includes a debt that accrues before or after the date of the order for relief, presenting something of a conflict with section 502(b)(5). In re Andrade, 662 B.R. 898 (Bankr. S.D. N.Y. 2024), Judge Paek.