Bankruptcy Circuit Update

Featuring cases from February 2016

First Circuit

Puerto Rico Highway and Transportation Authority v. Redondo Construction Corp., (In re Redondo Construction Corp.),
__ F. 3rd __, 2016 WL 521188 (1st Circuit, Feb. 10, 2016)

Court of Appeals for the First Circuit ("First Circuit") vacated and remanded: Appellant challenged the district court's affirmance of the bankruptcy court's award of interest to the debtor. The First Circuit held that while the debtor did not forfeit its claim to *pre*-judgment interest under state law Article 1061, 28 U.S.C. Section 1961 exclusively controls the award of *post*-judgment interest in federal court. As such, the case was vacated and remanded for a calculation of pre and post-judgment interest.

Fustolo v. 50 Thomas Patton Drive, LLC; The Patriot Group LLC; Richard Mayer,
__ F. 3rd __, 2016 WL 732207 (1st Circuit, Feb. 24, 2016)

Court of Appeals for the First Circuit held that the creditor's claim at issue was not contingent or disputed; and as such, affirmed the bankruptcy court's decision that found the creditor qualified to join with two other creditors also holding non-contingent, undisputed claims to force the debtor into an involuntary bankruptcy proceeding.

O'Rorke v. Porcaro, (In re Porcaro),
__ B.R. __, 2016 WL 453385 (1st Circuit B.A.P., Feb. 3, 2016)

Bankruptcy Appellate Panel for the First Circuit affirmed the bankruptcy court's grant of summary judgment in favor of the home-owner creditors' based on their complaint to determine their debt was not discharged under 11 U.S.C. Section 523(a)(6). The bankruptcy court correctly determined that a state court judgment, which was upheld on appeal, had issue preclusive effect (doctrine of collateral estoppel) in the current adversary proceeding, i.e., the state court's factual findings satisfied the elements of Section 523(a)(6). The state court found that the debtor had willfully and intentionally violated a contract to install windows, in that the debtor caused incorrectly sized windows to be installed and intentionally failed to obtain the required permits for the work, and when the size issue was brought to the debtor's attention by his subcontractor, the debtor instructed the subcontractor to hide the window defects with over-sized casings and wood filler.

Castellanos Group Law Firm, L.L.C. v. F.D.I.C., as receiver for Westernbank Puerto Rico, et al., (In re MJS Los Croabas Properties, Inc.),
__ B.R. __, 2016 WL 690859 (1st Circuit B.A.P., Feb. 17, 2016)

Bankruptcy Appellate Panel for the First Circuit affirmed the bankruptcy court's two orders sanctioning an attorney and a law firm. The attorney at issue filed a motion

for relief from the automatic stay, and this attorney subsequently refused to answer repeated written and oral communications from the other parties to discuss the matter - even though local rule required that the parties confer in contested stay relief motions. The other parties filed motions for an extension of time to file opposition papers so that they could attempt to reach the attorney at issue to address or resolve the pending motion. Again, the attorney at issue refused to answer further and multiple phone calls and emails from the other parties - ultimately attempting to excuse such behavior with an assertion that her office was moving, although admitting she had an answering machine. The other parties, when faced with no communications from movant's counsel, each filed opposition papers. Movant's counsel then inexplicably withdrew the stay relief motion, leading the F.D.I.C. and the Chapter 7 Trustee to seek reimbursement of their respective legal costs and fees in responding to the now-withdrawn motion. Under the authority of Fed. R. Civ. P. 11, made applicable by Fed. R. Bankr. P. 9011, and the bankruptcy court's inherent authority to sanction, and 28 U.S.C. Section 1927, the attorney and the law firm with which she was affiliated (she was an "independent contractor" doing work for the law firm at issue) were held jointly and severally responsible for the F.D.I.C. and Trustee's legal costs and fees.

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Second Circuit

Silverman v. Cullin, 2016 WL 423800 (2nd Circuit, Feb. 4, 2016)

The Second Circuit affirmed the district court's judgment affirming the bankruptcy court's order awarding $11,744.76 to the bankruptcy trustee on a fraudulent conveyance claim which sought return of interest payments made to Karen Cullin ("Cullin") as part of a Ponzi scheme.

Under Bankruptcy Code Section 544(b)(1), the trustee of an estate in bankruptcy "may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law." Pursuant to the applicable New York state law, N.Y. Debt. & Cred Law § 273, "Every conveyance made and every obligation incurred by a person who is or will be thereby rendered insolvent is fraudulent as to creditors without regard to his actual intent if the conveyance is made or the obligation is incurred without a fair consideration." Though the Second Circuit had not previously addressed the issue of fair consideration in the context of interest payments made in a Ponzi scheme, here the Court agreed with several other courts of appeals (in addition to New York district and bankruptcy courts) in holding that payments of "interest" to Ponzi scheme investors should be treated as fraudulent transfers, because "fair consideration" is not present in the context of such schemes.

The Second Circuit was not persuaded by Cullin's reliance on cases holding that guaranteed interest payments at a commercially reasonable rate made in satisfaction of an antecedent debt constituted fair consideration, because the interest on Cullin's investment was not guaranteed and was in excess of commercially reasonable rates.

***Friedberg v. Neier*, 2016 WL 731238 (2nd Circuit, Feb. 24, 2016)**

The Second Circuit denied the appeal of debtor Richard Friedberg ("Friedberg") and affirmed the district court's judgment affirming the bankruptcy court's order that Friedberg lacked standing to oppose the approval of the settlement of all claims against his estate because he had no pecuniary interest directly and adversely affected by the court's order adopting the settlement.

In order to have standing to appeal from a bankruptcy court ruling, an appellant must be directly and adversely affected by the challenged bankruptcy court order. Here, the settlement in question provided for the distribution of the proceeds from the sale of certain real property to Friedberg's creditors. The property was sold for $2.3 million, and after accounting for administrative expenses, just over $1.9 million remained for distribution to creditors pursuant to the proposed settlement. This amount was far less than the allowed creditor claims against the estate; the priority claim of a single creditor was for $2.725 million. The bankruptcy court therefore found that a surplus after payment of the creditors' claims was a mathematical impossibility.

The Second Circuit held that this finding was not made in error. As such, Friedberg could not have received a distribution from the estate regardless of the terms of the settlement. His only other interest in the settlement proceedings was an exemption he had claimed, which was provided for in the settlement agreement. Absent an adversely affected pecuniary interest, the Second Circuit affirmed that Friedberg lacked standing to oppose the settlement.

The Second Circuit was not persuaded by Friedberg's argument that he had standing to challenge the settlement based on the surplus that he imagined would have remained had the real property been sold for what he believed was its true value. The Second Circuit deemed this argument to be without merit, finding that Friedberg's assertions regarding the "true" value of the property were conclusory and speculative. They Court also found such arguments irrelevant to Friedberg's appeal, because they did not concern the reasonableness of the bankruptcy court's approval of the settlement, but rather the validity of the auction sale that produced the proceeds distributed by the agreement. However, Friedberg had already unsuccessfully appealed the bankruptcy court's order authorizing the sale, and the district court dismissed that appeal under 11 U.S.C. § 363(m), which creates a rule of "statutory mootness" barring appellate review of any sale authorized by 11 U.S.C. § 363(b) or (c), as long as the sale was made to a good-faith purchaser and was not stayed pending appeal. Here, the sale was not stayed pending appeal, and there was no basis upon which to conclude that the buyer was not a purchaser in good faith. As such, the sale was immune to Friedberg's challenge, and the Second Circuit held that he could not rely on its alleged deficiencies to cure his lack of standing.

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Third Circuit

***In re Rock Airport of Pittsburgh, LLC.*,**
2016 WL 697793 (3rd Circuit, Feb. 22, 2016)

The Third Circuit affirmed the Western District of Pennsylvania's decision dismissing an appeal as moot. In 2009, Rock Airport filed for chapter 11 protection. The sole equity holder of the airport objected to the trustee's motion to sell the airport on the grounds that the airport was owned by a non-debtor. After an evidentiary hearing, the Bankruptcy Court concluded that the airport was in fact estate property and approved the sale to a third party. The Bankruptcy Court denied the equity holder's motion for a stay pending appeal and the sale subsequently closed. The equity holder appealed, but the District Court dismissed the appeal as moot under section 363(m). The Third Circuit affirmed on the grounds that the equity holder unsuccessfully sought a stay of the proceedings and because there was no evidence proving that the third-party purchaser was not a good-faith purchaser.

***In re Macri*,**
2016 WL 760201 (3rd Circuit, Feb. 25, 2016)

The Third Circuit affirmed the District of New Jersey's order affirming the dischargeability of a debt incurred by a chapter 7 debtor. In 2007, the appellant sued her neighbor for injuries suffered from multiple dog bites. The parties settled the action, and before the settlement sum was fully paid, the neighbor filed for chapter 7 bankruptcy protection. The appellant sought an order pursuant to section 523(a)(6) that the debt was non-dischargeable as a willful and malicious injury. The Bankruptcy Court concluded after an evidentiary hearing that the appellant had failed to meet her burden of proof. The District Court affirmed and the Third Circuit summarily approved that affirmance.

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Fourth Circuit

JANUARY:

***Stubbs & Perdue, P.A. v. Angell* (*In re Anderson*), 811 F. 3d 166 (4th Cir. 2016)**

On January 26, 2016, the Fourth Circuit held that, under 11 U.S.C. § 724(b)(2), chapter 11 administrative expenses are subordinate to secured tax claims in a case that is later converted to chapter 7. During the pendency of the chapter 11 proceeding, debtor's counsel's fees in the approximate amount of $200,000 were allowed as administrative expenses under §§ 330(a) and 503(b). The IRS asserted a secured claim of approximately $987,000. Upon conversion, the chapter 7 trustee estimated that, after chapter 7 administrative expenses were distributed, the estate would have approximately $420,000 available. Thus, the estate would not be able to satisfy both the IRS secured claim and the fees of debtor's counsel incurred during the chapter 11. The chapter 7 trustee filed a motion seeking guidance, and the lower courts held that the IRS's secured claim had priority over the chapter 11 legal fees.

Pre-BAPCPA, chapter 11 expenses held priority over secured tax creditors in a chapter 7. BAPCPA attempted to change this provision, but due to an erroneous cross-reference, it excluded certain administrative expenses from § 724(b)(2). In 2010, Congress corrected the erroneous cross-reference. After that correction, the debtor's case was converted to chapter 7. The corrected version made clear that the IRS's secured claim had priority of chapter 11 administrative expenses. The chapter 7 trustee argued that this corrected version controlled and, thus, the legal fees incurred during the chapter 11 were subordinate to the IRS's secured claim. Debtor's counsel objected, asserting that its legal fees were senior to the IRS's secured claim. The bankruptcy court and the district court agreed with the trustee's argument.

The Fourth Circuit affirmed after evaluating the legislative history behind § 724(b)(2), noting the ambiguity created by BAPCPA and Congress' 2010 correction. The Fourth Circuit also applied the principle that a court shall apply the law in effect at the time it renders its decision. The Fourth Circuit held that the lower courts applied the proper version of the law and that Debtor's counsel's fees were subordinate to the IRS's secured claim.

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Fifth Circuit

***In re Clean Fuel Technologies II, LLC*, 554 B.R. 591 (Bankr. W.D. Tex. 2016)**

After successfully defending against an involuntary bankruptcy proceeding, the alleged debtor sought attorney's fees and costs against the unsuccessful petitioning creditors under § 303(i). The court noted that such attorney's fees could be recovered from unsuccessful petitioning creditors only if: (1) the court has dismissed the involuntary petition; (2) the dismissal was not with the consent of the alleged debtor and the petitioning creditors; and (3) the alleged debtor did not waive its right to recovery. Even when those prerequisites are met, § 303(i) still contains a discretionary aspect, which as the bankruptcy court pointed out, is approached differently amongst courts.

While the Fifth Circuit has not directly addressed the approach to be used, the bankruptcy court adopted the "majority 'presumption' approach—i.e., that a presumption exists that an award of attorneys' fees and costs will be made against unsuccessful petitioning creditors, but that the presumption may be rebutted based on the totality of the circumstances." In applying this presumption approach, the bankruptcy court considered: (1) the merits of the involuntary petition; (2) role of any improper conduct by the alleged debtor; (3) reasonableness of actions taken by petitioning creditors; (4) the motivation and objectives behind involuntary bankruptcy filing; and (5) other material factors and considerations including the practical operation of any award. Ultimately, here, the bankruptcy court found that although the prerequisites under § 303(i) are met, given the above noted considerations, the court should exercise its discretion by not awarding attorney's fees and costs.

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Sixth Circuit

In re McVicker,
--- B.R. ---, 2016 WL 660102 (Bankr. N.D. Ohio Feb. 17, 2016)

The Bankruptcy Court for the Northern District of Ohio denied a creditor's motion to dismiss a chapter 7 for bad faith. The debtors in the case filed a chapter 7 to discharge two debts: (i) a guaranty of a commercial real estate loan totaling $125,000; and (ii) a general unsecured debt totaling little more than $2,000. The commercial loan was borrowed nearly eight years earlier to refinance existing obligations pertaining to the debtors' rental properties in Toledo. The creditor asserted that the debtors' use of chapter 7 to essentially discharge one debt, in spite of their ability to pay given exempt retirement benefits and homestead property, constituted bad faith. The Bankruptcy Court disagreed, holding that Congress and the states make "policy choices which elevate the protection of [a] debtor's exempt property over the

interests of creditors in being paid." Therefore, asserting exemption rights is not itself conduct that can be characterized as egregious or in bad faith.

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Seventh Circuit

***In re Anna F. Robinson*, 811 F.3d 267 (7th Cir. Feb. 4, 2016)**

On February 4, 2016, the Seventh Circuit affirmed the decision of the district court, holding that under Illinois law, a debtor was entitled to exempt a bible of his or her choosing, not just one of negligible value. Specifically, the debtor owned a valuable copy of the Book of Mormon from the 1830, as well as various modern and digital copies of the book. The debtor wanted to exempt the 1830 Book of Mormon under Illinois statute 735 ILCS 5/12-1001, which designates various items of exempt personal property, including a "bible." The parties agreed that the 1830 Book of Mormon qualified as a bible, but the trustee argued that because it was valuable and the debtor had other copies, she should be made to sell the 1830 Book of Mormon for the benefit of creditors. The Seventh Circuit rejected that argument, holding that (a) exemption laws in Illinois must be construed in favor of the debtor, who has a right to choose his or her exempt property, and (b) the trustee's position would effectively limit the debtor's exemption to a "bible of negligible value," while no such restrictive language was actually present in the statute. As such, the debtor was permitted to exempt the 1830 Book of Mormon.

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Eighth Circuit

JANUARY

***In re O'Sullivan*, 544 B.R. 407 (8th Cir. BAP January 19, 2016)**

In this matter a judgment creditor appealed from the bankruptcy court's order granting the debtor's motion to avoid its judgment lien. The debtor moved to avoid the judgment lien

against a residence owned by the debtor and his wife as tenants by the entirety. The judgment giving rise to the lien was against the debtor and a related business, but not the debtor's wife.

In the bankruptcy proceedings, the debtor claimed a $15,000 exemption in his homestead interest under Missouri law. Under Section 522(f)(1)(A) a debtor may avoid a judgment lien on exempt property if the debtor possessed the property interest at some point before the lien "fixed" on the property. There was no dispute that the debtor possessed his interest in the property prior to the judgment lien. Rather, the creditor argued on appeal that its judgment lien did not attach to the residence because, under Missouri law, tenant by the entirety property is not liable for the judgment debt of one spouse. The creditor argued that the lien must have attached in a technical, enforceable sense for the debtor to avoid it.

The BAP disagreed. Recognizing that Missouri law is restrictive with respect to what constitutes an enforceable lien, the BAP determined that the meaning of the term "fix" as used in Section 522 is less restrictive for lien avoidance purposes, and includes even unenforceable and inchoate liens. The BAP held that even if the residence was not subject to the judgment lien, an unenforceable judgment lien arose that was avoidable under Section 522. It further held that permitting lien avoidance would also avoid any cloud on the title of the residence.

***Jones v. Bob Evans Farms, Inc*., 811 F.3d 1030 (8th Cir. January 26, 2016)**

The Eighth Circuit determined that a plaintiff's failure to disclose employment discrimination claims in his Chapter 13 bankruptcy proceedings judicially estopped him from pursing those claims, upholding the District Court's grant of summary judgment in favor of the defendants.

In the years prior to bringing the employment discrimination claims, the plaintiff and his wife filed for Chapter 13 bankruptcy. The order confirming the Chapter 13 plan required the plaintiff and his wife to notify the trustee of any lawsuits that were "received or receivable" during the term of the plan as a result of their failure to initially disclose a pending worker's compensation claim. Three years into the plan the Plaintiff instituted the employment discrimination in the district court but failed to notify the Chapter 13 trustee. While the district court action was pending, the bankruptcy court terminated the bankruptcy, granting a discharge as to the remaining unsecured debt. The defendants in the district court action then moved for summary judgment, arguing that the Plaintiff was judicially estopped from pursuing the claims. The district court granted the motion, concluding that the failure to disclose was tantamount to a representation to the bankruptcy court that the claims did not exist.

The Eighth Circuit upheld the district court's order finding that the three factors considered by the court in determining whether judicial estoppel applies weighed against the plaintiff. These three factors are: (1) a party taking a position clearly inconsistent with a prior position; (2) whether the party persuaded the court to accept the prior position; and (3) if the party would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped.

The Eighth Circuit determined that given the explicit requirement to disclose any lawsuits in the confirmation order, the failure to do so constituted a representation to the bankruptcy court that they did not exist which was clearly inconsistent with asserting those claims in the district court. The Court further found that the bankruptcy court adopted the plaintiff's position that the claims didn't exist by granting the discharge. The Court then found that the plaintiff obtained an unfair advantage in the bankruptcy proceedings because the trustee could have sought an order to make proceeds from any potential settlement available to unsecured creditors.

***In re O&S Trucking, Inc*., 811 F.3d 1020 (8th Cir. January 22, 2016)**

This matter involves a dispute between the debtor, a company that owned and operated a fleet of trunks and related equipment, and a creditor that lessor of several trucks operated by the debtor and held security interests in a number of other trucks owned by the debtor. Following the confirmation of the debtor's Third Amended Plan of Reorganization, the debtor brought an appeal challenging the confirmation order, as well as two of the bankruptcy court prior orders. These orders concerned the valuation of the trucks to which the creditor held security interests and the amount paid by the debtor in adequate assurance payments.

The BAP, sitting in review of the bankruptcy court, dismissed the appeal for lack of jurisdiction, holding that the debtor lacked standing because the debtor was not a "person aggrieved" by the confirmation of a plan proposed by the debtor itself. The debtor then appealed to the Eighth Circuit. The Eighth Circuit explained that in a prior ruling the Court had determined that a Chapter 13 debtor, in order to appeal a non-final interlocutory ruling, may propose a plan incorporating those interlocutory ruling and object to the confirmation of the plan to acquire "aggrieved" status in order to appeal the confirmation order. Here, the Eighth Circuit adopted this same method for Chapter 11 debtors to seek to appeal interlocutory rulings. However, the Court upheld the BAP's dismissal because the debtor had not objected to the plan it proposed.

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FEBRUARY:

Starion Financial v. McCormick (In re McCormick)
812 F.3d 659 (8th Cir. February 1, 2016)

The Eighth Circuit dismissed for lack of jurisdiction the appeal of the McCormicks from an order of the 8th Circuit BAP.

A provision in the McCormick's confirmed individual chapter 11 plan provided that at least "ten days prior to the Effective Date of the Plan" Starion, a secured creditor with a judgment against the debtors, was to file an itemized statement of its claim for fees and expenses against the debtors. Twelve days prior to the effective date, Starion submitted a statement setting out costs including interest, late fees, taxes, and appraisal and engineering fees, but no attorneys' fees. Eight days prior to the effective date, Starion submitted an updated statement that included $125,000 of attorneys' fees.

The bankruptcy court denied Starion's request for fees based upon a lack of agreement for fees based upon the underlying consent judgments, but did not rule on the timeliness of the submission of the request. Starion appealed to the BAP, which reversed and remanded finding an agreement for fees based upon the notes, mortgages, workout agreements and other documents upon which the judgments were based. The BAP remanded the case to the bankruptcy court to determine the reasonableness and timeliness of the fee request. The McCormicks appealed the BAP's determination on the right to fees to the 8th Circuit. Finding that the resolution of the timeliness and reasonableness of the fee application affects the merits of the dispute on the underlying dispute on the fee request and the underlying remand left the bankruptcy court with more than just a purely mechanical or ministerial task, the 8th Circuit found it lacked jurisdiction over the appeal.

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Ninth Circuit

Gladstone v. U.S. Bancorp (In re Green), 811 F.3d 1133 (9th Cir. 2016)

In *Gladstone v. U.S. Bancorp (In re Green),* the Ninth Circuit affirmed a district court order which reversed a bankruptcy court's grant of summary judgment for defendants and denial of the trustee's motion for leave to file a second amended complaint seeking to recover the value of so-called life settlements by which the debtor's un-matured term life insurance policies which were sold to the defendants.

Prior to the filing of his chapter 7 case, the debtor transferred ownership of three term life insurance policies, none of which were disclosed in his Statement of Financial Affairs or his 341 meeting of creditors. Together, defendants paid approximately $507,000 for the life settlements and received $9 Million in death benefits following the debtor's death. The debtor made other transfers prior to filing his chapter 7 case and, like the life settlements, none were disclosed in connection with the bankruptcy filing. Subsequently, despite non-disclosures, the chapter 7 trustee learned of the life settlement transfers and filed an adversary complaint and motion to extend the statute of limitations, which motion was granted. The trustee filed a first amended complaint after obtaining further information, then sought, but was denied, leave to file a second

amended complaint based on additional information regarding one of the life settlements. The bankruptcy court granted defendants' motion for summary judgment, which ruling was reversed on intermediate appeal by the district court as well as the order denying the trustee's motion for leave to amend. The central issue was whether the debtor's interests in the term life insurance policies, including the secondary market value of the policies and resulting settlements, constituted an "interest of the debtor in property" that was recoverable under Code section 548(a).

The Ninth Circuit agreed with the district court that the debtor's interests in the policies and life settlements constituted recoverable property of the estate, and were not excluded from the estate by operation of Code sections 541(b) (because neither life insurance policies or viatical settlements were listed as excluded from the scope of Code section 541(b)) or 522 (because the debtor did not claim the policies or settlements as exempt, the debtor waived any exemption when he transferred the policies to the defendants, by his wife, and neither contention was raised before the bankruptcy court). The Ninth Circuit agreed with the district court that (i) due to non-disclosures, the trustee's suit was not time-barred, via the doctrine of equitable tolling, and (ii) leave to amend should have been granted due to discovery of new evidence.

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***Zachary v. California Bank & Trust (In re Zachary)*, 811 F.3d 1191 (9th Cir. 2016)**

In *Zachary v. California Bank & Trust,* the Ninth Circuit affirmed the bankruptcy court's order sustaining an objection to a chapter 11 plan of organization and held that the absolute priority rule in 11 U.S.C. § 1129(b)(2)(B)(ii) continues to apply following the amendments to the Bankruptcy Code. As a general matter, an individual debtor filing under chapter 11 can obtain confirmation by satisfying the bankruptcy court, that notwithstanding any creditor's objections, the plan is 'fair and equitable' to each creditor class. 11 U.S.C. § 1129(b)(1), (2). A debtor can "cram down" a plan only if it complies with the absolute priority rule in 11 11 U.S.C. § 1129(b)(2)(B)(ii). This critical rule provides that a dissenting class of unsecured creditors must be provided for in full before any junior class can receive or retain any priority under a reorganization plan.

Section (B)(ii)'s new clause plainly created an exception to the absolute priority rule that only applies to an individual under chapter 11. In particular, the absolute priority rule largely remains "except that in a case in which the debtor is an individual, the debtor may retain property included in the estate under section 1115[.]" The Circuits are split as to what property an individual debtor can retain without violating the absolute priority rule.

Overruling *In re Friedman*, the Ninth Circuit adopted the narrow view of the amendment. Under this reading, what section 1115 takes into the estate is property that the debtor acquires after the commencement of the case and it is only that property that the debtor may retain when his or her unsecured creditors are not fully paid. As a result, the Ninth Circuit's interpretation of the amendment is in sync with the long standing absolute priority rule.

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***U.S. Bank N.A. v. The Village at Lakeridge, LLC (In re The Village at Lakeridge, LLC),* 2016 WL 494592 (9th Cir. Feb. 8, 2016)**

In *US Bank v. The Village at Lakeridge*, the Ninth Circuit affirmed the decision of the 9th Cir. BAP and held that creditor Dr. Robert Rabkin ("Rabkin") was neither a statutory insider nor a non-statutory insider and therefore his vote could be considered for confirmation purposes.

Essentially, debtor had two creditors: US Bank, which held a fully secured claim of approximately $10 million, and debtor's sole member, MBP Equity Partners 1, LLC ("MBP"), which held an unsecured claim of $2.76 million. After filing, MBP board member Kathie Bartlett ("Bartlett") approached Rabkin with an offer to buy MBP's insider claim for $5,000. Under the plan the claim would be paid $30,000. Rabkin testified that although he had a close business and personal relationship with Bartlett, he did not have a relationship with either the debtor or MBP prior to purchasing the claim, and he was unaware of debtor's chapter 11 plan or the proposed distribution on the claim.

The BAP reversed the bankruptcy court's finding that Rabkin had become a statutory insider as a matter of law and affirmed the finding that Rabkin was not a non-statutory insider. The Ninth Circuit affirmed the BAP and held that a claimant does not become an insider merely by acquiring a claim from a statutory insider because insider status pertains to the claimant, not the claim, and because a person's status as an insider is a factual question which must be determined after the claim is acquired. The Ninth Circuit held that the bankruptcy court did not clearly err in determining that Rabkin was not a non-statutory insider because Rabkin's relationships with Bartlett, the debtor, and MBP were not comparable to the classifications enumerated in §101(31), and there was no evidence that the transaction was at less than arm's length.

Judge Clifton dissented from the holding that Rabkin was not a non-statutory insider and found ample evidence in the record that the transaction was not at arm's length, specifically that MBP and Bartlett were clearly motivated to place the unsecured claim in the hands of a friendly creditor who would provide the necessary vote for confirmation, and Rabkin was not motivated solely by the economic proposition.

Moreover, Judge Clifton argued that the majority holding has the effect of rendering §1129(a)(10) meaningless by allowing a savvy insider to develop a plan that would provide a payout on an insider claim and then sell that claim to a friendly third party for a price lower than the payout. This would effectively ensure a vote accepting the plan.

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11th Circuit

Slater v. U.S. Steel Corp.
---Fed.3d---, 2016 WL 723012 (11th Cir. Feb. 24, 2016)

In affirming the district court, the Eleventh Circuit held that the doctrine of judicial estoppel barred Slater's employment discrimination claims against U.S. Steel after she failed to disclose those claims in her Chapter 7 bankruptcy.

Twenty-one months after bringing a lawsuit against her former employer, the debtor filed her Chapter 7 bankruptcy. However, she failed to disclose employment discrimination claims she was planning to pursue against U.S. Steel. The Chapter 7 trustee treated the bankruptcy case as a no asset case. When U.S. Steel learned of the bankruptcy case, they moved the district court to dismiss the case or for summary judgment. U.S. Steel argued that the case should be dismissed because Slater lacked standing to prosecute the claims or for summary judgment under the doctrine of judicial estoppel. Upon receiving U.S. Steel's motion, the debtor immediately amended her bankruptcy petition to identify her law suit against U.S. Steel. Slater claimed that the omissions were unintentional and had her bankruptcy attorney immediately amended her Schedules and Statement of Financial Affairs to reflect the litigation. Shortly thereafter, the Debtor converted her case to Chapter 13 and the Bankruptcy Court confirmed her Chapter 13 plan.

The Court concluded that *New Hampshire v. Maine*, 532 U.S. 742 (2001) did not govern the district court's application of judicial estoppel in this case. Therefore, the court rejected plaintiff's argument that the district court erred in failing to give the New Hampshire factors appropriate weight in barring her employment discrimination claims on the basis of judicial estoppel. The Court concluded that the district court properly applied Eleventh Circuit precedent— in *Burnes v. Pemco Aeroplex, Inc.* 291 F.3d 1282 (11th Cir. 2002) and *Robinson v. Tyson Foods, Inc.* 595 F.3d 1269 (11th Cir. 2010). Each decision sets out the purpose of judicial estoppel. *Burnes* requires (1) it must be shown that the allegedly inconsistent positions were made under oath in a prior proceeding; and (2) such inconsistencies must be shown to have been

calculated to make a mockery of the judicial system. In *Robinson* the court observed that"[w]hen considering a party's intent (under the second prong of our test)… the debtor's failure to satisfy its statutory disclosure duty is inadvertent only when, in general, the debtor either lacks knowledge of the undisclosed claims or has no motive for their concealment." In this present case, the district court concluded that "allowing her to do so without a penalty would encourage rather than discourage debtors like her to conceal their assets unless or until they are caught."

While concurring, Judge Tjoflat thinks that *Burnes* and *Barger* were wrongly decided and the only solution is the en banc court. In the Slater case the only real losers were the debtor's creditors.

> The *Burnes–Barger* doctrine is not an equitable doctrine because its application produces at-least-inequitable results, if not manifestly unjust ones. A debtor deprives his bankruptcy estate of an asset by concealing it. Then the District Court, acting as a court of equity, furthers the deprivation by giving the asset to the defendant, who owes the claim's value to the bankruptcy estate, as a pure windfall. The estate's creditors, who are totally innocent, provide the windfall. The explicit rationale for doing this is that the deprivation deters future debtors from concealing assets of the bankruptcy estate. The implicit rationale is that the bankruptcy courts are either unwilling or incapable of providing such deterrence.

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