The Cramdown

The Newsletter of the Tampa Bay Bankruptcy Bar Association

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PRESIDENT'S MESSAGE

by Elena Paras Ketchum
Stichter Riedel Blain
& Prosser, P.A.

The Good Works of TBBBA!

As we near the end of the 2010 – 2011 bar year and look in the rearview mirror of this past year, the wonderful accomplishments of the Association come into clear focus. While there is not enough room in this article to describe them all, here are two programs which demonstrate the good works of TBBBA in our community.

Credit Abuse Resistance Education ("C.A.R.E.") Program

As you may know, the Association presented its first C.A.R.E. program in 2007. Since then, the Association has reached approximately 6,100 students in Hillsborough County and has received a mayoral proclamation recognizing the Association's efforts. This year alone, TBBBA's C.A.R.E. volunteers have reached approximately 1,100 high school and college students in Hillsborough County. C.A.R.E. volunteers this year presented the program to a number of schools in the area, including: Alonso High School, Durant High School, Erwin Vocational Technical Center, King High School, Middleton High School, Simmons Career Center, South County Career Center, Spoto High School, Strawberry Crest High School, University of Tampa. Many thanks to Barbara Hart, Esq. for serving as this year's Chair of the C.A.R.E. Committee! Her tireless efforts and countless hours of dedication ensured the continuation of this valuable program in our community.

"A Day at Bankruptcy Court" Program

The Association scheduled two (2) programs for the students of Stetson University College of Law to visit the Tampa Division of the United States Bankruptcy Court for the Middle District of Florida. The first program was held on November 17, 2010 and the second on February 24, 2011. At both of these programs, the students spent the day visiting the various bankruptcy courtrooms to watch hearings scheduled on those days. In addition, lunch was provided at which speakers, including bankruptcy judges, spoke about the federal judicial system and bankruptcy related matters. Bankruptcy practitioners volunteered their time at both programs and spent the day with the students answering questions. Thank you to our judges for taking time to participate in these programs. The students greatly appreciated the opportunity to hear from bankruptcy judges and to interact with bankruptcy practitioners!

These are just two of the programs undertaken by the Association's members this past year, which have had a positive impact in our community! Thank you to everyone who has volunteered their time and energy to the Association and its programs.

I look forward to seeing everyone at the Annual Dinner on June 2, 2011!

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Knocking Out Valuation Issues in Bankruptcy from the Debtor's Perspective[1]

by David S. Jennis[2]

One of the most crucial (and overlooked) concepts that a debtors' counsel must consider is valuation. Valuation is the cornerstone that shapes the strategy and often dictates the outcome of many cases. While valuation issues often arise in connection with plan confirmation, valuation can play a key role in almost every phase of a chapter 11 or chapter 13 case. Valuation issues typically emerge in the context of stay relief, adequate protection, and plan treatment.

Round I: An Introduction to Valuation Standards

Section 506(a) of the Bankruptcy Code provides that a bankruptcy court may establish the values of property in a bankruptcy case, including in connection with the determination of the secured and unsecured portions of a claim secured by a lien on property of the debtor, or the estate, and for purposes relating to the confirmation of a plan. Valuation "shall be determined in light of the purpose of the valuation and the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or *on a plan affecting such creditor's interest."*[3] Section 506(a) does not provide a specific valuation method or standard of value to be used by a bankruptcy court when valuing property subject to a lien. Instead, bankruptcy courts are to "determine value on a case-by-case basis taking into account the facts of each case and the competing interests in the case."[4] The valuation of assets is considered "an integral part of the confirmation process under Chapter 11."[5]

In determining the value of property, courts essentially apply one of three valuation standards: liquidation value, market value, or fair value.[6] Liquidation value is the low end of the valuation spectrum and is sometimes described as foreclosure value or wholesale value.[7] Market value is defined as the most probable price a property brings in a competitive and open market with willing buyer and seller.[8] A "fair value" standard applies market valuation and then discounts to present value to reflect the amount of time the creditor will hold and/or market property in anticipation of sale.[9] Market value, replacement value, and fair market value are at the high end of the value spectrum.[10] Accordingly, the full valuation spectrum (from low to high) is as follows: fire sale, orderly liquidation, fair value, fair market value.[11]

Round II: Valuation in the Context of Stay Relief

Typically, valuation issues arise early in a bankruptcy case when a secured creditor seeks relief from stay or adequate protection. Value becomes relevant at that point, as adequate protection analysis looks to what the creditor could have obtained under its state law remedies had bankruptcy not intervened.[12] In the context of stay relief and determination of adequate protection, secured creditors will often advocate for the lowest value of collateral possible (and continued decline) to demonstrate a lack of equity and inflate an unsecured claim, while a debtor will typically argue for a higher value of the property in order to demonstrate adequate protection in the form of an equity cushion and minimize the impact of any diminution in value.[13] One of the primary valuation issues raised in connection

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1 This article attempts to summarize some of the issues addressed at the November 2010 TBBBA Luncheon Seminar in which the author was a panelist. Accordingly, the author reluctantly adopts the theme of that presentation which was an (over) hyped "Battle of the Barristers."

2 David S. Jennis is one of the founding and managing members of Jennis & Bowen, P.L. Dave has over twenty years of experience representing debtors, creditors, trustees, and creditor committees in complex corporate bankruptcies. Dave is AV Peer Review Rated by Martindale-Hubbell and Board Certified in Business Bankruptcy Law by the American Board of Certification. He wishes to thank his associate, Kathleen L. DiSanto for her editorial assistance in the preparation of this article.

3 11 U.S.C. § 506(a)(1).

4 *See In re Arnold and Baker Farms*, 177 B.R. 648, 655 (9th Cir. BAP 1994) (*citing* H.R. Rep. 595, 95th Cong, 1st Sess. 356 (1977)).

5 *In re Sandy Ridge Development Corp.*, 881 F.2d. 1346, 1354 (5th Cir. 1989).

6 *U.S. v. Arnold & Baker Farms (In re Arnold & Baker Farms)*, 177 B.R. 648, 656 (B.A.P. 9th Cir. 1994).

7 *Id.* Judge Williamson's decision in the case of *In re Perez*, 318 B.R. 742, 743, n.1 (Bankr. M.D. Fla. 2005) contains a complete description of the valuation spectrum.

8 *Arnold & BakerFarms*, 177 B.R. at 657.

9 *Id.*

10 *Perez*, 318 B.R. at 743.

11 *Id.*

Knocking Out Valuation

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with adequate protection is determining whether the liquidation or market value of collateral must be protected.[14]

Regardless of whether an attorney is representing a debtor or creditor, counsel needs to carefully consider the implications of advocating for a certain value of property early in a bankruptcy case, as a party may be committed to a valuation made early in the case, unless the bankruptcy court has a reason to establish a different value. Value can change during the pendency of a case for two reasons: (1) different valuation standard is applicable or (2) circumstances change.[15] From the debtor's perspective, the best approach is to determine a realistic value for the collateral and be careful to choose the valuation standard appropriate to the issues and context involved.

For example, in determining the appropriate valuation standard in the context of stay relief or adequate protection, courts engage in a fact specific analysis, customized to each case.[16] Some courts have determined that liquidation value is appropriate in the context of stay relief or adequate protection, as the purpose of adequate protection is to try to compensate the creditor for any diminution in value due to the automatic stay.[17] Liquidation value may be particularly appropriate where the chance of reorganization is slight.[18] Absent the automatic stay, the creditor could seek state court remedies to liquidate the collateral, making liquidation value appropriate in this context. Other courts have found that going concern or fair market value are more appropriate valuation standards, particularly where the prospects of reorganization are reasonably optimistic and the debtor intends to continue to use the collateral to generate income.[19]

The other main valuation issue that frequently arises in the context of stay relief and adequate protection is whether and when did any diminution of value occur. To the extent a decline in value occurs prior to the date a creditor seeks relief from the stay based on a diminution in value, a creditor may not be entitled to adequate protection for a decline in value that already occurred – the creditor is only entitled to adequate protection for prospective decreases in value that occur after the automatic stay is in place.[20]

Knockout Round : The Treatment of Secured Claims and Applicability of Rash

Valuation struggles often emerge during the plan formulation and confirmation process as a result of a debtor's proposed treatment of a secured claim. Some confusion concerning the treatment of secured claims in chapter 11 cases has resulted from the Supreme Court's holding in the case of *Associates Commercial Corporation v. Rash.*[21] Rash made it clear that in a chapter 13 case, where a debtor seeks to retain property, "replacement value" is the appropriate standard. Less clear is whether *Rash* does (or should) govern valuation issues in connection with "dirt for debt" or "eat dirt" plans in which a debtor proposes to surrender real property to a secured creditor as the indubitable equivalent of the creditor's secured claim.[22] In the current real estate climate, these issues may be particularly relevant, especially in instances where lenders strategically elect to forego their collateral in order to pursue personal liability of borrowers or guarantors.

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12 *See In re Deico Elecs., Inc.*, 139 B.R. 945, 947 (B.A.P. 9th Cir. 1992).

13 Interestingly, this dynamic will typically flip in the context of confirmation if the debtor intends to retain the collateral and must pay the secured claim.

14 Courts have applied various standards of valuation, ranging from going concern or fair market value to liquidation value. *See In re Phoenix Steel Corp.*, 39 B.R. 218, 224 (D. Del. 1984).

15 *Schreiber v. U.S. (In re Schreiber)*, 163 B.R. 327, 332 (Bankr. N.D. Ill. 1994).

16 Such practice is consistent with Congress' intent not to specifically include a valuation standard in section 361, as the Senate Report states, "Neither is it expected that the courts will construe the term value to mean, in every case, forced sale liquidation value or full going concern value. There is wide latitude between those two extremes…." *Heritage Savs. & Loan Assoc. v. Rogers Dev. Corp. (In re Rogers Dev. Corp.)*, 2 B.R. 679, 683-84 (Bankr. E.D. Va. 1980) (*quoting* Senate Report No 95-989, 95th Cong., 2d Session (1978), U.S. Code Cong. & Admin News 1978, pp. 5787, 5840).

17 *Deico Elecs., Inc.*, 139 B.R. at 947. *See also American Bank & Trust co. v. RAM Mfg., Inc. (In re RAM Mfg., Inc.)*, 32 B.R. 969, 973 (Bankr. E.D. Pa. 1983).

18 *In re C.F. Simonin's Sons, Inc.*, 28 B.R. 707, 713 (Bankr. E.D.N.C. 1983).

19 *First Nat'l Bank of McDonough v. Shockley Forest Indus., Inc. (In re Shockley Forest Indus., Inc.)*, 5 B.R. 160, 163 (Bankr. N.D. Ga. 1980).

20 *Elmira*, 174 B.R. at 903.

21 520 U.S. 953, 957; 117 S.Ct. 1879; 138 L.Ed.2d 148 (1997).

22 *In re Perez*, 318 B.R. 742, 744 (Bankr. M.D. Fla. 2005) ("Nowhere in *Rash* does the Supreme Court hold that all valuations under section 506 must be based on a replacement value standard. Rather, *Rash* was decided entirely in the contest of a debtor's exercise of the 'cram down' option available in a chapter 13 case….")

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The inapplicability of *Rash* to "dirt for debt" plans can be illustrated by the context of the case. *Rash* involved chapter 13 debtors who proposed to retained a tractor truck used in freight hauling business and attempted to value the truck.[23] The Rashes argued that the truck was valued at $31,875 based upon what the creditor would receive at a foreclosure sale, while the creditor asserted that replacement value was the appropriate standard, and that the truck should be valued at $41,000.[24] The Supreme Court held that replacement value applies where a chapter 13 debtor seeks to retain collateral over the objection of a secured creditor, but specifically noted the limited application of its holding to retention cases, stating "(f)rom the creditor's perspective as well as the debtor's, surrender and retention are not equivalent acts. When a debtor surrenders the property, a creditor obtains it immediately, and is free to sell it and reinvest the proceeds."[25] Therefore, while *Rash* stands for the proposition that replacement value applies if collateral is being retained, *Rash* does not state and should not be interpreted to mean that liquidation value is applicable if the collateral is being surrendered.[26]

Dirt for Debt: Property as the Indubitable Equivalent?

Many of the early "dirt for debt" cases addressed whether a debtor could retain property and surrender less than all collateral in full satisfaction of a creditor's secured claim.[27] In "partial surrender" cases, modern case law has demonstrated that it is virtually undisputed that the bankruptcy court must value the portion of the collateral that is proposed to be transferred for the purpose of ensuring that the secured creditor receives collateral of sufficient value to constitute the "indubitable equivalent"

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23 *Id.*

24 *Id.*

25 *Id.* at 961.

26 *Rash's* application in a chapter 11 case where the debtor seeks to retain collateral is not really disputed. *In re Nat'l Book Warehouse, Inc.*, 2007 WL 5595524 at *5 (Bankr. M.D. Tenn. May 23, 2007) (citing *Fin. Sec. Assurance Inc. v. T-H New Orleans Ltd. P'ship (Matter of T-H New Orlean Ltd. P'ship)*, 116 F.3d 790 (5th Cir. 1997); *In re Preventive Maint. Servs., Inc.*, 359 B.R. 607 (Bankr. W.D. La. 2007); *In re TennOhio Transp. Co.*, 269 B.R. 775 (Bankr. S.D. Ohio 2001)).

27 *See U.S. v. Arnold & Baker Farms (In re Arnold Baker Farms)*, 177 B.R. 648 (B.A.P. 9th Cir. 1994); *In re Atlanta S. Bus. Park, Ltd.*, 173 B.R. 444 (Bankr. N.D. Ga. 1994); *In re May*, 174 B.R. 832 (Bankr. S.D. Ga. 1994); *In the Matter of Martindale*, 125 B.R. 32 (Bankr. D. Idaho 1991); *In re W.B. Simons*, 113 B.R. 942 (Bankr. W.D. Tex. 1990); *In re Walat Farms, Inc.*, 70 B.R. 330 (Bankr. E.D. Mich. 1987); *In re Fursman Ranch*, 38 B.R. 907 (Bankr. W.D. Mo. 1984).

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of the secured claims under the standards of 11 U.S.C. § 1129(b)(2)(A)(iii) is satisfied.[28] It is well settled that "[a] creditor receives the indubitable equivalent of its secured claim when it receives all of the property to which its lien attaches, because 'common sense tells us that the property is the indubitable equivalent of itself.'"[29]

But some issues remain unresolved – what is the appropriate standard of valuation to be applied in dirt for debt cases? If *Rash* dictates that liquidation applies when real property is surrendered to the secured creditor, which of the different standards of liquidation value applies? Is the determination of a liquidation value subject to a reasonableness standard? Should a secured creditor be permitted a "fire sale" valuation in order to increase its unsecured deficiency claim to the detriment of other creditors and parties in interest?

What is the appropriate standard for valuation?

Pre-*Rash* case law suggests that liquidation value would not be the appropriate standard in the "dirt for debt" context.[30] Instead, in evaluating "dirt-for-debt" plans contemplating the surrender of collateral to a secured creditor, courts predominantly utilized a "fair market value" or "fair value" standard.[31] "Conservative valuation" cases are distinguishable from plans contemplating full surrenders and generally involve an entirely different purpose for valuation, as "conservative valuation" cases often involve partial surrenders.[32] For example, *Atlanta Southern* and *Park Forest* were "partial surrender" cases where the Debtor was proposing to surrender only a portion of the secured creditor's collateral in full satisfaction of the secured claim (and eliminating any lien in the remaining collateral).[33] In those situations, courts have held that a valuation on the transferred collateral should be conservative to avoid "shifting the risk" to the secured creditor who would no longer have recourse to the remaining collateral.[34]

Is the determination of a liquidation value subject to a reasonableness standard?

If *Rash* is properly limited to plans contemplating the retention of collateral, policy reasons dictate that bankruptcy courts apply a market or fair value standard in valuing the collateral to be surrendered as the "indubitable equivalent." The *Stockbridge* court further recognized that while the bank could dispose of the property by whatever method it chose, the bank "elects this method at its own risk and may not elect a lesser use than highest and best, realize less on the disposition and impose on the debtor and its estate an artificially low price on forced diminishment in the value of the collateral."[35] Creditors should not be permitted to fire sale the property and then saddle the debtor and any guarantors with an inflated deficiency simply because it wants to "dump" the property at its earliest opportunity.[36]

Bonus Round: ABCs and Wetherington Decision

As evidenced by the increasing emergence of "dirt for debt" plans, it is clear that valuation issues are increasingly important as a result of the present economy and its devastating effect on values of real property. In all likelihood, bankruptcy courts will be facing these issues with increasing frequency based on recent state court developments in the context of assignments for the benefit of creditors. On its face, section 727.108(11) of the Florida Statutes allows an assignee to abandon collateral to a secured creditor, perhaps avoiding the challenges presented by chapter 11 and inconsistent valuation standards created by the misapplication of *Rash* in the "dirt for debt" context.[37] However, a trial court in the Twelfth Judicial Circuit may

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28 *See In re PNC, Nat'l Assoc. v. Park Forest Dev. Corp. (In re Park Forest Dev. Corp.),* 197 B.R. 388, 396 (Bankr. N.D. Ga. 1996).

29 *Park Forest*, 197 B.R. 388 (emphasis added), *citing Sandy Ridge*, 881 F.2d. at 1350 (5th Cir. 1989).

30 *See In re Wermelskirchen*, 170 B.R. 118 (Bankr. N.D. Ohio 1994); *In re Stockbridge Props. I, Ltd.*, 141 B.R. 469 (Bankr. N.D. Ga. 1992); *Sandy Ridge Dev. Corp. v. La. Nat'l Bank (In re Sandy Ridge Dev. Corp.)*, 881 F.2d 1346 (5th Cir. 1989); *Fursman Ranch*, 38 B.R at 910.

31 *Id.*

32 *May*, 174 B.R. 832 (Bankr. S.D. Ga. 1994).

33 *Id. See also Atlanta S. Bus. Park, Ltd.*, 173 B.R. 444; *Park Forest*, 197 B.R. 388 (Bankr. N.D. Ga. 1996).

34 *In re May*, 174 B.R. 832 (Bankr. S.D. Ga. 1994)

35 141 B.R. at 472.

36 *See In re Arnold Baker Farms*, 177 B.R. 648, 659 (approving valuation which contemplated the creditor holding the surrendered property for two to three years); *Stockbridge*, 141 B.R. 467, 471-472 (choosing valuation which provided for creditor holding collateral for up to three years).

37 Section 727.108(11) of the Florida Statutes authorizes an assignee to abandon assets to secured creditors if he or she determines the assets are burdensome to the estate or are of inconsequential value or benefit to the estate (operates like section 554 of the Bankruptcy Code).

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have curtailed this option in its *Wetherington* decision, which is presently on appeal to the Second District Court of Appeals.[38] In *Wetherington*, the trial court found that a creditor is not required to accept title to real property abandoned in accordance section 727.108(11) of the Florida Statutes.[39] If the *Wetherington* decision is upheld by the Second District Court of Appeals, debtors and guarantors may have no other option but to file chapter 11 and propose "dirt for debt" plans in order to deal with recalcitrant creditors who are otherwise unwilling to work with the debtors and/or guarantors to otherwise maximize the value of their collateral.[40]

Down and Out: A Conclusion

Understanding valuation standards and their application in various factual scenarios during the pendency of a bankruptcy case are key to a successful debtor's practice, as valuation is integral to the Bankruptcy Code. A fundamental knowledge of why a certain valuation standards are appropriate and an appreciation of the implications of advocating for a particular valuation of collateral is invaluable to debtor's counsel attempting to develop a strategy to successfully dodge the blows of creditors in a chapter 11 case, as valuation issues arise constantly throughout the life of a chapter 11 case.

38 *In re Assignment for the Benefit of Creditors of Lee Wetherington Dev., LLC to Hyman*, Case No. 2009 CA 0323 NC (Fla. Cir. Ct. 2010).

39 *Id.*

40 However, it is worth noting that the Supreme Court has yet to rule on the issue, and none of the other district court of appeals have issued published decisions on the issue.

The Absolute Priority Rule–In a State of Uncertainty

by Derrick Clarke - J.D. Candidate 2011, Stetson University College of Law; Moot Court Board Member and Participant in 19th Annual Conrad Duberstein Bankruptcy Moot Court Competition

Jerry was a sole proprietor who ran a small shipping business in Tampa, Florida. He wished to take advantage of a bull market by purchasing additional shipping equipment and real property, in order to expand his business. Jerry began by purchasing used shipping trucks with cash deposits, and then he took out a mortgage to purchase the real property. As a result, Jerry's shipping business flourished, bringing market growth and development in the greater Tampa Bay area. Jerry's success continued, when suddenly a financial recession plagued the State of Florida, hitting the Tampa Bay economy particularly hard. Unfortunately, Jerry's business began to dwindle and eventually he defaulted on his debts including his mortgage.

Jerry filed for Chapter 11 bankruptcy protection. He then submitted his proposed plan of reorganization in which he sought to operate his business and retain ownership of his pre-petition business assets. His plan did not pay unsecured creditors in full and instead proposed deferred cash payments to be funded out of future business operations. However, unsecured creditors voted against the plan because they were not paid in full and Jerry was proposing to retain some property of the estate. Trying to retain his business, Jerry attempted to confirm his plan in cram down, arguing that his shipping business would fail unless he is allowed to retain his business assets. However, with bankruptcy courts undecided as to whether the absolute priority rule applies to individuals, the status of Jerry's plan was suspended with uncertainty.

Jerry's situation illustrates the importance of resolving the issue as to whether the absolute priority rule applies to individual Chapter 11 debtors. The absolute priority rule requires unsecured creditors to be paid in full under the plan before any junior class may retain an interest in the estate property.[1] Prior to the Bankruptcy Abuse Protection and Consumer Protection Act of 2005 ("BAPCPA"), the absolute priority rule has served as the "bedrock" principle to balance debtor relief and unsecured creditor protection in cram down.[2] The absolute priority rule had been applied uniformly to all Chapter 11 cases with only rare exceptions.[3] But whether the absolute priority rule still applies to individual Chapter 11 debtors will dictate how Jerry and other individuals in situations similar to Jerry's will be afforded relief and to what extent creditors will be protected in cram down.

This Article will address the importance of resolving whether the absolute priority rule still applies to individual Chapter 11 debtors. Beginning with a brief overview of the BAPCPA changes to the absolute priority rule, this Article will survey the bankruptcy court decisions addressing this issue. A discussion elaborating on the application and possible ramifications of the current state of the law follows. This Article concludes by briefly addressing the possible ramifications if this issue is not resolved.

I. THE ABSOLUTE PRIORITY RULE—BANKRUPTCY COURT SPLIT

Bankruptcy courts nationwide are split as to whether the absolute priority rule applies to individual debtors after BAPCPA. To briefly summarize: BAPCPA added § 1115 to the Bankruptcy Code, and § 1115 expanded the definition of property of the estate for individual debtors to include post-petition property and earnings.[4] BAPCPA also amended § 1129(b)(2)(B) to allow individual Chapter 11 debtors to retain at least some property through an exception to the absolute priority rule, but this section also references § 1129(a)(15) requiring the debtor to commit five years of projected disposable income to the plan (per the disposable income requirement).[5] However, the amendment is not entirely clear as to what property Congress intended for individuals to retain in § 1115 in spite of the absolute priority rule, or whether the absolute priority was abrogated with regard to individuals.

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1 11 U.S.C. § 1129(b)(2)(B)(ii) (2006).
2 *See* G. Eric Brunstad, Jr. & Mike Sigal, *Competitive Choice Theory and the Broader Implications of the Supreme Court's Analysis in* Bank of America v. 203 North Lasalle Street Partnership, 54 Bus. Law. 1475, 1494–95 (1999).
3 The long standing exception to the absolute priority rule was refined and set forth in *Norwest Bank Worthington v. Ahlers*. 485 U.S. 197 (1988). In *Norwest*, the United States Supreme Court held that individuals could retain pre-petition property in exchange for contributions of "new value," which needed to be in "money's worth" of tangible assets and payments from post-petition earnings did not satisfy this requirement. *Id.* at 205–206.
4 11 U.S.C. § 1115 (2006).
5 BAPCPA changed the language adding the phrase "except that in a case in which the debtor is an individual, the debtor may retain property included in the estate under section 1115, subject to the requirements of subsection (a)(14) of this section." 11 U.S.C. § 1129(a)(15); 11 U.S.C. § 1129(b)(2)(B)(ii).

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As a result of these amendments, the bankruptcy courts have adopted two different and polarizing interpretations of the added language to the absolute priority rule. First, some bankruptcy courts have read the BAPCPA changes to abrogate the absolute priority rule for individual Chapter 11 debtors. These courts allow debtors to retain both pre-petition and post-petition property even if creditors are not paid in full while requiring the debtor to commit five years of projected disposable income (hereinafter "broad interpretation").[6] Alternatively, other bankruptcy courts have read BAPCPA changes to allow individual Chapter 11 debtors to retain only post-petition property under the absolute priority rule if they do not pay unsecured creditors in full, requiring the debtor to commit all pre-petition non-exempt property and five years of projected disposable income to the plan (hereinafter "narrow interpretation").[7]

A. Broad Interpretation

At first glance, it seemed that bankruptcy courts unanimously agreed that BAPCPA abrogated the absolute priority rule for individual debtors as reflected by the broad interpretation. In fact, bankruptcy courts held for this interpretation in the first three decisions after BAPCPA. Courts seemed to have this issue well-in-hand even after the BAPCPA changes to the absolute priority rule.

In 2007, the Bankruptcy Court for the District of Nebraska issued the first opinion addressing whether BAPCPA abrogated the absolute priority rule for individual debtors. *In In re Tegeder*, the individual debtors filed for Chapter 11 bankruptcy protection and proposed to retain pre-petition business assets under the plan without paying unsecured claims in full.[8] Once establishing both an accepting and objecting impaired class, the debtors attempted to cram down the plan. The court adopted

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6 *See In re Roedemeier*, 374 B.R. 264, 273–74 (Bankr. D. Kan. 2007); *In re Shat*, 424 B.R. 854, 862–63 (Bankr. D. Nev. 2010); *In re Tegeder*, 369 B.R. 477, 480 (Bankr. D. Neb. 2007).

7 *See In re Maharaj*, No. 09–15777–SSM, 2011 WL 1753795, at *7 (Bankr. E.D.Va. May 9, 2011); *In re Draiman*, No. 09 B 17582, 2011 WL 1486128, at *37 (Bankr. N.D. Ill. April 19, 2011); *In re Welsh*, No. 09-16031-WCH, 2011 WL 867046, at **2–3 (Bankr. .D. Mass. Mar. 9, 2011); *In re Stephens*, No. 10–31263–H3-11, 2010 WL 719485, at *4 (Bankr. S.D. Tex. Feb. 22, 2011); *In re Karlovich*, No. 10–10860–PB11, 2010 WL 5418872, at **3–4 (Bankr. S.D. Cal. Nov. 16, 2010); *In re Gbadebo*, 431 B.R. 222, 229 (Bankr. N.D. Cal. 2010); *In re Gelin*, 437 B.R. 435, 439 (Bankr. M.D. Fla. 2010); *In re Steedley*, No. 09–50654, 2010 WL 3528599, at **3–4 (Bankr. S.D. Ga. Aug. 27, 2010); *In re Mullins*, 435 B.R. 352, 360–61 (Bankr. W.D. Va. 2010).

8 369 B.R. at 479–80.

the broad interpretation and held that the debtors were permitted to retain both pre-petition and post-petition property under the plan. The court relied heavily on legal commentary and reasoned that individual debtors no longer were required to satisfy the absolute priority rule primarily because the absolute priority rule cross-referenced § 1115, which refers to both post-petition property and pre-petition property of the estate under § 541.[9]

Approximately three months later, the Bankruptcy Court for the District of Kansas addressed the same issue. *In In re Roedemeier*, the individual owned two dental practices when he filed for Chapter 11 bankruptcy protection, proposing to retain equity ownership of his dental practice without paying unsecured claims in full.[10] In response to the objecting unsecured class, the debtor attempted to cram down the plan and retain pre-petition property sufficient to stay in business. The court adopted the broad interpretation and held that the debtor was permitted to retain both pre-petition and post-petition property.[11] The court reasoned that the broad interpretation must be adopted to preserve Chapter 11 plans as a viable option of reorganization for individual debtors because the majority of individual debtors cannot satisfy the "new value" exception to retain pre-petition property.[12] The debtor could not meet the "new value" exception because his primary source of new value in exchange for pre-petition property would be derived from post-petition earnings. Accordingly, the broad interpretation was necessary to ensure that sole proprietors would be able to remain in business under Chapter 11.

The Bankruptcy Court for the District of Nevada was the third court to address whether BAPCPA abrogated the absolute priority rule for individual Chapter 11 debtors. *In In re Shat*, the debtors owned and operated a dry cleaning business as a sole proprietorship and proposed to retain business assets under their Chapter 11 plan without paying unsecured claims in full.[13] The court adopted the broad interpretation and held that the debtors could retain pre-petition business assets and cram down the plan. The court primarily relied upon the decisions issued in *In re Tegeder* and *In re Roedemeier* and reasoned that the BAPCPA changes to the absolute priority rule in individual Chapter 11 cases were part of a design to make individual Chapter 11 plans more like Chapter 13 plans, emphasizing that Chapter 13 plans have the disposable income requirement and do not have the absolute priority rule.[14]

Almost five years removed from BAPCPA, bankruptcy courts had demonstrated a strong consensus that individual debtors no longer have to satisfy the absolute priority rule as reflected by the broad interpretation. Additionally, in 2009, the decision in *In re Johnson* recognized, in dicta, that the broad interpretation was correct.[15] However, this national consensus would hit a wall, causing uncertainty about the current status of the absolute priority rule.

B. Narrow Interpretation

The majority of bankruptcy courts have held for the narrow interpretation, finding that Congress intended for individual Chapter 11 debtors to satisfy the absolute priority rule, at least in regard to retaining pre-petition property of the estate. However, it was not until mid-2010 when bankruptcy courts began adopting the narrow interpretation.

On April 16, 2010, the Bankruptcy Court for the Northern District of California decided *In re Gbadebo*—the first decision to adopt the narrow interpretation.[16] *In In re Gbadebo*, the debtor was a licensed professional engineer and owned the property on which his business was located.[17] The debtor proposed to retain his pre-petition equity interest in his business without paying unsecured claims in full.[18] The court held that the debtor could not retain his pre-petition property and rejected the argument that Congress intended to make individual Chapter 11 cases more like Chapter 13 cases under the broad interpretation because it found that each BAPCPA change to the absolute priority rule appeared to be designed to ensure a greater payout to creditors. Specifically, the court stated that "no one who reads

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9 *Id.* at 480.
10 373 B.R. at 267–68.
11 *Id.* at 275–76.
12 *Id.* at 275.
13 424 B.R. at 862–63.
14 *Id.* at 867–68.
15 402 B.R. 851, 852–53 (Bankr. N.D. Ind. 2009).
16 431 B.R. at 229–30.
17 *Id.* at 224–25.
18 *Id.* at 228–29.

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BAPCPA as a whole can reasonably conclude that it was designed to enhance the individual debtor's fresh start."[19]

Shortly after, the Bankruptcy Court for the Western District of Virginia decided *In re Mullins* and also adopted the narrow interpretation.[20] *In In re Mullins*, the debtor was a dentist who filed Chapter 11 bankruptcy protection proposing to retain equity ownership of his practice without paying unsecured claims in full.[21] The court held that the debtor could not retain his pre-petition interest in cram down.[22] The court reasoned that the narrow interpretation was correct because Congress was primarily concerned with preventing individuals from retaining post-petition earnings and not allowing them to retain pre-petition property. Prior to BAPCPA, post-petition property and earnings were not property of the estate. The narrow interpretation addressed this situation by interpreting § 1115 to bring post-petition earnings into the estate for individual debtors and by adding language to § 1129(b)(II)(B)(ii) subjecting post-petition earnings to the disposable income requirement. Building on this reasoning, the court stated that if Congress wished to go further and intended for such debtors to retain pre-petition property it would have been clearer under BAPCPA.

By late 2010, the narrow interpretation garnered further support in *In re Steedley*, *In re Gelin*, and *In re Karlovich*, where all three courts agreed that the debtor could not retain non-exempt pre-petition property.[23] *In In re Steedley*, the debtor was a sole proprietor who owned a law maintenance business and properties.[24] The debtor proposed to retain all property of the estate under the plan without paying unsecured claims in full. The court adopted the narrow interpretation and held that the debtor could not retain pre-petition property. While the court's reasoning is not explicitly clear, the court seemed to rely heavily on the decision in *In re Gbadebo*.

Soon thereafter, Judge Jennemann wrote the decision in *In re Gelin* for the Bankruptcy Court for the Middle District of Florida.[25] *In In re Gelin*, the debtors were real estate investors proposing to retain real property without paying unsecured claims in full.[26] The court adopted the narrow interpretation and held that the debtors could not retain pre-petition property under the plan, reasoning that if Congress wished to abrogate the absolute priority rule for individual debtors, then it would have stated that individuals could retain property of the estate under § 541 instead of the language it chose referencing § 1115.[27] The court explained that because § 1115 brings post-petition property into the estate for individual Chapter 11 debtors and BAPCPA did not change the general definition of property of the estate under § 541, it made no sense to read § 1115 as superseding § 541. Rather, the court stated that the most sensible reading of § 1129(b)(2)(B)(ii) was to allow individuals to retain property "added" in the estate under § 1115, which is only post-petition property.

By late 2010, the Bankruptcy Court for the Southern District of California joined the courts favoring the narrow interpretation. *In In re Karlovach*, the debtor requested that the court decide whether she was required to satisfy the absolute priority rule so that she could determine how to proceed under her plan.[28] The court adopted the narrow interpretation and held that the debtor's plan would violate the absolute priority rule.[29] The court offered a unique perspective by reasoning that the BAPCPA changes to the absolute priority rule were designed to keep the cram down requirements for individual debtors unaltered by BAPCPA as it relates to post-petition property. Since BAPCPA added § 1115 to bring post-petition property and earnings into the estate for individual debtors, an additional exception was needed to under the absolute priority rule to allow individual debtors the discretion to retain post-petition property as was permitted prior to BAPCPA.

In February 2011, the Bankruptcy Court for the Southern District of Texas issued the next decision requiring individual Chapter 11 debtors to satisfy the absolute priority rule. *In In re Stephens*, the court held that the debtor was required to satisfy the absolute priority rule and could not retain his pre-petition assets without paying

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19 *Id.* at 229–30.
20 435 B.R. at 360–61.
21 *Id.* at 355–56.
22 *Id.* at 360–61.
23 2010 WL 3528599, at **2–3; 437 B.R. at 439; 2010 WL 5418872, at **3–4.
24 2010 WL 3528599, at **2–3.
25 It should be noted that the debtor failed to establish that an impaired class accepted the plan as required by § 1129(a)(8). 437 B.R. 435 at 438, n. 11.
26 *Id.* at 437–38.
27 *Id.* at 441–42.
28 2010 WL 5418872, at *1.
29 *Id.* at **3–4.

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unsecured claims in full.[30] The court reasoned that if the phrase "in addition to the property specified in section 541" in § 1115(a) were read to include all of property of the estate, then such reading would render the phrase "all property of the kind specified in section 541" in § 1115(a)(1) superfluous.[31] The court then explained that the reference to § 1115 in § 1129(b)(2)(B)(ii) does not encompass all property of the estate, but rather only the post-petition property listed in § 1115.

Shortly after the decision in *In re Stephens*, the narrow interpretation garnered further support from two recent decisions. In March 2011, the Bankruptcy Court for the District of Massachusetts decided In re Walsh, where the court adopted the narrow interpretation and held that individual Chapter 11 debtors must satisfy the absolute rule.[32] The court relied heavily on Judge Tchaikovsky's opinion in *In re Gbadebo*, and further reasoned that because § 1115 only references post-petition property, individual Chapter 11 debtors may only retain such property under § 1129(b)(2)(B)(ii). On April 19, 2011 the Bankruptcy Court for the Northern District of Illinois joined the party and adopted the narrow interpretation.[33] Just like the court in *In re Walsh*, the court *In re Draiman* also held that individual debtors must satisfy the absolute priority rule. The court primarily reasoned that when looking to the plain language of § 1115, property of the estate under § 1115 does not absorb § 541but rather refers only to the property "added" in the estate which is post-petition property under subsections (1) and (2).

On May 9, 2011, the Bankruptcy Court for the Eastern District of Virginia issued the most recent decision ruling that the absolute priority rule still applies to individual Chapter debtors.[34] *In In re Maharaj*, the court held that the individual debtor could not retain non-exempt pre-petition property without paying unsecured claims in full. The court primarily reasoned that if Congress intended to make individual Chapter 11 cases more like Chapter 13 cases as argued under the broad interpretation, then it would have amended the statutory debt ceilings for Chapter 13 cases as set forth under §109(e). However, the court stated that because Congress did not either increase or eliminate the debt ceilings, the narrow interpretation reflects the correct statutory reading.

Since May 2011, the score sheet indicates that twelve bankruptcy courts have addressed whether BAPCPA abrogates the absolute priority rule. Initially, there seemed to be a consensus amongst bankruptcy courts in favor of the broad interpretation as reflected by the three earliest decisions. However, since the 2010 decision in *In re Shat*, nine bankruptcy courts held in favor of the narrow interpretation. As a result, this issue remains unsettled and with consequences for many hanging in the balance. A resolution to this issue is needed.

II. UNPREDICTABLE RESULTS: ADDRESSING THE RAMIFICATIONS OF EACH APPROACH

Jerry's fate, along with individuals and sole proprietors in situations similar to Jerry's, rests solely with the bankruptcy court's interpretation of the BAPCPA changes to the absolute priority rule. While this notion may seem comforting, the split amongst bankruptcy courts demonstrates uncertainty regarding this issue. As a result, practitioners do not have a clear indication on how courts will decide this issue, and practitioners could be leading the debtors down a path of uncertainty to a fork in the road—the broad interpretation or the narrow interpretation.

A. The Broad Interpretation: The Debtor Preference

The broad interpretation puts Jerry and individual debtors like him on a path to recovery. The broad interpretation would only require Jerry to commit five years of his projected disposable income to the plan under the disposable income requirement so long as that disposable income was sufficient to fund a feasible plan. He would not have to satisfy the absolute priority rule and would be able to retain the pre-petition property necessary to stay in business. In the above example, Jerry would be able to keep his business assets along with other pre-petition property, which would help him ship to various venues and locales. This in turn could possibly create employment and stimulate economic development. However, this vehicle still is not a perfect model.

The broad interpretation may create problems, as unsecured creditors will likely recover less. In this case, unsecured creditors lose out as Jerry would be able to retain his business assets, which would have been committed to the plan. While Jerry is required to satisfy

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30 2011 WL 719485, at **1-2.
31 *Id.* at *4.
32 2011 WL 867046, at *3.
33 2011 WL 1486128, at **36–37.
34 2011 WL 1753795, at *7.

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the disposable income requirement, this may not be sufficient as there is nothing stopping debtors such as Jerry from modifying business operations in a way that would yield lower income while retaining pre-petition property.[35] Regardless of possible motivations for doing this, the disposable income requirement becomes less attractive in this hypothetical. Additionally, the unsecured creditors are often business entities, and if they are recovering mere cents on the dollars owed to them, then this could lead to an increase in business failures. It should be emphasized that this concern is not limited to only unsecured business creditors, but also non-business unsecured creditors because they are subject to the same risk of debt recovery.

B. The Narrow Interpretation: The Creditor Preference

Jerry is worse off under the narrow interpretation. Unfortunately for Jerry, he will be unable to retain his pre-petition property—his business assets—and he is still required to commit five years of his projected disposable income to the plan. Jerry may not be able to retain sufficient pre-petition property under his plan because the majority of his contributions of "new value" in exchange for pre-petition property are in the form of promised payments from post-petition earnings. This potentially leaves Jerry with insufficient assets to keep his business. However, Jerry may still retain exempt property in the light of the absolute priority rule. Exempt property becomes important, as such assets could satisfy the "new value" exception.[37]

On the other hand, unsecured creditors are better off under the narrow interpretation. All pre-petition non-exempt property is committed to the plan, allowing unsecured creditors to recover greater amounts of the debt owed. This reduces the unsecured creditors' risk because the narrow interpretation ensures a higher rate of debt recovery. Additionally, a larger recovery for unsecured creditors will allow such entities to retain business autonomy and financial health due to the corresponding reduced debt loss.

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35 It must be emphasized that Jerry's earnings must still be sufficient to satisfy the plan.
36 *See Van Buren Indus. Investors v. Henderson (In re Henderson)*, 341 B.R. 783, 790–91 (M.D. Fla. 2006); *In re Bullar*d, 358 B.R. 541, 544–45 (Bankr. D. Conn. 2007).
37 In general, exempt property is characterized as diminimus. However, in Florida exempt property such as Homestead property and pension plans for example are not diminimus and could satisfy the "new value" exception.

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As demonstrated above, the fate of individual debtors and unsecured creditors will be guided by two completely different interpretations "fates." Under the broad interpretation, sole proprietors and individual debtors alike are better off, but unsecured creditors will not. Alternatively, the narrow interpretation may be the end for sole proprietors, but unsecured creditors will be able to recover a greater amount of debt owed. While bankruptcy courts grapple over these interpretations, the extent of debtor relief and unsecure creditor protection remains uncertain.

III. A NEED FOR RESOLUTION—THERE IS NO CONTROLLING PRECEDENT

There has never been a greater need to resolve the issue as to whether the BAPCPA abrogated the absolute priority rule for individual Chapter 11 debtors. With the two different interpretations, the fate of many sole proprietors is unpredictable and uncertain. However, it must be emphasized that the Bankruptcy Court in the Middle District of Florida (which would hear Jerry's case) is not left completely without guidance on this issue.

A guiding light was ignited in the wake of Judge Jennemann's decision in *In re Gelin*. As mentioned above, Judge Jennemann held in favor of the narrow interpretation, requiring sole proprietors and individuals to satisfy the absolute priority rule.[38] While Judge Jennemann's decision should be applauded for its detailed and exhaustive analysis, it should be noted that this opinion is not controlling precedent.

A controlling precedent does not exist to guide the future of individual Chapter 11 debtors. In fact, not one appellate court has addressed the issue. As a result, individual debtors and bankruptcy practitioners are struggling to prepare plans and anticipate the court's ruling. Sole proprietors and individuals such as Jerry will likely be able to survive in the market place under the broad interpretation. However, the narrow interpretation is not as promising for individual debtors. Without a controlling precedent, and with the majority of bankruptcy courts undecided on this issue, the future of many sole proprietors and individual Chapter 11 filings are unpredictable. Bankruptcy should be a road to recover and not a suspended nightmare. As such, the need for resolution has never been more important.

38 *In re Gelin*, 437 B.R. at 441–42.

The "Wildcard" Personal Property Exemption in Bankruptcy

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On February 3rd 2011, the Florida Supreme Court issued an opinion on "[w]hether for the purpose of the statutory personal property exemption in section 222.25 (4), a debtor in bankruptcy receives the benefits of Florida's article X, section 4, constitutional homestead exemption where the debtor owns homestead property but does not claim the homestead exemption in bankruptcy and the trustee's administration of the property is not otherwise impeded by the existence of the homestead exemption." Osborne v. Dumoulin, 55 So.3d 577, 580, 2011 WL 320986, 1 (Fla. 2011).

The issue arises in the context of Bankruptcy because Florida Statute 222.25(4) allows an individual that does not claim or receive the benefits of the homestead exemption to claim an additional $4,000 of personal property as exempt ("personal property exemption"). Fla. Stat. §222.25(4) (2007). Id. at 584. Before the Supreme Court issued this opinion, Florida bankruptcy courts had split on whether a debtor must surrender their homestead property in order to not "receive the benefits" of the homestead exemption under Section 4, Article X of the State Constitution ("homestead exemption"). The two cases that illustrated the underlying issues are In re Bennett, 395 B.R. 781, 785 (Bkrtcy. M.D. Fla. 2008) and In re Magelitz, 386 B.R. 879, 881 (Bkrtcy. N.D. Fla. 2008).

In Magelitz, the court held that the debtor received the benefit of the homestead exemption by remaining in the home. The debtor did not claim the homestead exemption in Schedule C, and explicitly claimed the "wildcard" personal property exemption under section 222.259(4). In re Magelitz, 386 B.R. 879, 881 (Bkrtcy. N.D. Fla. 2008). In a nutshell, to claim the "wildcard" exemption, under Magelitz the debtor would have to "(1) not claim the property as exempt, and (2) timely and properly show a clear and unambiguous intent to abandon the property." Id. at 884. The Court noted "Under the reasoning in Magelitz, the debtor's election not to claim the homestead as exempt from administration by the bankruptcy trustee had no effect on the debtor's eligibility to claim the statutory personal property exemption." Osborne v. Dumoulin, 55 So.3d 577, 585, 2011 WL 320986, 6 (Fla. 2011).

On the other hand, the court in Bennett focused on the impact of not claiming the homestead exemption (i.e. the ability of the trustee to administer the homestead property), and found that the ability of the Chapter 7 trustee to dispose of the homestead property for the benefit of the estate was sufficient to destroy the benefits that flowed from the homestead exemption. The court in Bennett held that a debtor in bankruptcy can end the benefits received from the homestead exemption without abandoning the property. The Court noted "... [i]t is this Court's conclusion that debtors who do not affirmatively exempt their homestead under § 522(b)(1) and the Homestead Exemption, but instead leave it available for administration by the Chapter 7 trustee, neither have claimed nor received the benefits of the Homestead Exemption found in Article X of the Florida Constitution. It is important to note that the Chapter 7 trustee need not actually administer the homestead for it to lose the protection of the Article X Homestead Exemption. That the homestead would not be protected were the trustee to decide to administer it is sufficient, because this means that the protection afforded by the Homestead Exemption has ceased." In re Bennett, 395 B.R. at 789–90.

The Supreme Court found the holding in Bennett persuasive. The fact that the homestead, if not claimed as exempt, would be vulnerable to administration by the Trustee was the cornerstone of the Court's reasoning in the Osborne case. Therefore, according to the Florida Supreme Court, the key to obtaining the personal property exemption is not abandonment of the homestead, or moving out of the homestead, but rather not claiming the property as exempt on schedule "C".

The benefit of the homestead exemption under Article X of the Florida constitution only provides one benefit. It protects the homestead property from creditors.

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Osborne v. Dumoulin, 55 So.3d 577, 587, 2011 WL 320986, 8 (Fla. 2011) ("the protection of the homestead from creditors constitutes the only "benefits" of the article X homestead exemption."). Once the Supreme Court identified the benefit of the homestead exemption, the Court explained what it means to "receive the benefits" of the homestead exemption. If the homestead property becomes subject to the Trustee's administration, the debtor has lost the benefit of the homestead exemption (i.e. homestead no longer has any legal effect). Id. at 587-588. As long as the debtor does nothing to interfere with the administration of the homestead by the Chapter 7 trustee, any benefit that flows from the trustee's decision to not administer the estate is not a benefit of the homestead exemption. Id. at 588.

In this economic climate, it is likely that the trustee will be less inclined to pursue homestead property, which often lacks equity. It is important to note that there are other parties involved in this scenario. While the trustee may not pursue the homestead property because of lack of equity, it stands to reason that the secured creditor will seek to enforce its rights with respect to the homestead if they are not being paid; however, a secured creditor for the homestead property being paid will not attempt to foreclose on the homestead. Where the property lacks equity, the trustee generally will not pursue administration of the property. It seems that there may be a windfall to a debtor that does not claim an undersecured homestead property as exempt, but continues to pay the mortgage. This debtor will be allowed to remain in the home if the trustee does not administer the undersecured property, and this debtor will also receive the $4,000 personal property exemption. This windfall is not a result of the homestead exemption, but instead is a function of the economic climate.

In Osborne, the Supreme Court held "… whether a debtor in bankruptcy could claim the homestead exemption, previously received the benefits of the homestead exemption, or may receive such protection after discharge from bankruptcy does not constitute receiving the benefits of the article X homestead exemption within the meaning of the personal property exemption". Osborne v. Dumoulin, 55 So.3d 577, 588-589, 2011 WL 320986, 10 (Fla. (Fla. 2011). This holding eliminates the possibility of the debtor in my hypothetical above being challenged on the grounds of "could" or "received" or "may receive such protection after discharge" benefits of the homestead exemption and such should not be allowed to receive the personal exemption. The hypothetical above, and the issue that the courts struggled with before Osborne, are a result of the ability of the debtor to remain in the homestead property and still receive the personal property exemption. The Supreme Court held that the debtor need not abandon the homestead to receive the benefit of the enhanced "wildcard" personal property exemption. 55 So.3d at 586. ("…a debtor with a homestead is eligible to claim the section 222.25(4) personal property exemption without abandoning the homestead property.").

The "receives the benefit" analysis does not end with non-exemption of the homestead property. The Court must examine the facts of each case to ensure that the debtor is not receiving an indirect benefit or "benefits of the homestead exemption through another avenue". In re Orozco, 2011 WL 462789, 4 (Bkrtcy. S.D. Fla. 2011), citing the case of Osborne, 2011 WL 320986 at 10. This issue is most likely to occur when there is a non-filing spouse. For example, a married debtor files for bankruptcy, does not claim the homestead exemption, receives the enhanced "wildcard" personal property exemption but is living in the home with the non-filing spouse. In this situation, the trustee is unable to administer the homestead because it is protected by the wife's homestead rights. See, e.g., In re Watford, 427 B.R. 552 (Bankr. S.D. Fla. 2010) (the court held that the debtor received an indirect benefit because the debtor was indirectly receiving the benefit of the homestead exemption through her spouse. The property was held as tenants by the entireties by the debtor and non-filing spouse. The court disallowed the § 222.25(4) personal property exemption.). See In re Orozco, 2011 WL 462789 at 4, citing In re Shoopman, 2008 WL 817109, at 5–6 ("stating that since the debtor did not have a wife to claim the homestead exemption there was no circumstance that indirectly bestowed the benefits of the homestead exemption upon him"). In the case of In re Hernandez, 2008 WL 1711528, 1 (Bankr. S.D.Fla. 2008), the debtor

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New Form Required by Tampa and Fort Myers Judges
Certification of Necessity of Request for Emergency Hearing

The Tampa and Fort Myers Judges have approved a new form for use when requesting an emergency hearing. The new Certification of Necessity of Request for Emergency Hearing requires that you provide more detailed information regarding the request for an emergency hearing, including the following:

o Identity of the moving party (i.e., debtor or name of moving party)

o Brief statement of relief requested (one or two sentences should suffice)

o Date by which the hearing is requested to be scheduled

o Brief statement of the reason why the matter must be heard on an emergency basis by the requested date (i.e., debtor's employees are due to be paid on a specific date requiring emergency hearing on motion for order authorizing use of cash collateral)

The use of the new form will facilitate the court's scheduling hearings in time to meet true emergency deadlines. The form is now available at flmb.uscourts.gov under "Procedures/Miscellaneous Forms" and is under consideration for use District wide. Please note that the old form (still in use in Orlando and Jacksonville) is located under "Procedures/Emergency Filings."

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF FLORIDA
_____ DIVISION

IN RE: CHAPTER _____ CASE
CASE NO.: _____

Debtor(s)
_____/

CERTIFICATION OF NECESSITY OF REQUEST FOR EMERGENCY HEARING

I HEREBY CERTIFY, as a member of the Bar of the Court, that I have carefully examined the matter under consideration and to the best of my knowledge, information and belief formed after reasonable inquiry, all allegations are well grounded in fact and all contentions are warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law can be made, that the matter under consideration is not interposed for any improper purpose, such as to harass, to cause delay, or to increase the cost of litigation, and there is just cause to request a consideration of the following pleading on an emergency basis:

[Title of pleading]

I CERTIFY FURTHER that there is a true necessity for an emergency hearing, specifically, because **[the moving party, i.e, "the Debtor"]** seeks **[brief statement of relief requested]** and requires a hearing prior to **[date]** for the following reason: **[brief statement of reason why the matter must be heard on an emergency basis]** _____
_____
_____
_____

I CERTIFY FURTHER that the necessity of this emergency hearing has not been caused by a lack of due diligence on my part, but has been brought about only by circumstances beyond my control or that of my client. I further certify that this motion is filed with full understanding of F.R.B.P. 9011 and the consequences of noncompliance with same.

DATED this _____ day of _____, _____.

SIGNATURE BLOCK

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listed real property as an exempt tenancy by the entirety and also claimed the personal property exemption. The court in Hernandez held that the non-debtor spouse would have to affirmatively waive the right to claim the homestead exemption in order for the debtor to claim the personal property exemption. Id. at 6. Therefore, the debtor cannot circumvent the Bankruptcy Code by having a non-filing spouse who is able to assert the protection of the homestead exemption, remain in the homestead property, and claim the "wildcard" personal property exemption.

The next issue that likely will arise occurs when a debtor seeks to obtain the enhanced "wildcard" personal property exemption after initially seeking to claim the homestead exemption on Schedule C. The debtor has the right to amend schedules at any time during a case. In re Bennett, 395 B.R. 781, 791 (Bkrtcy. M.D. Fla. 2008), citing In re Doan, 672 F.2d 831, 833 (11th Cir.1982) ("… the Eleventh Circuit has made clear that bankruptcy courts have no discretion to deny a debtor's right to amend schedules and statements at any time during a case."). In Doan, however, the Eleventh Circuit held that a court may deny the creditor the right to amend if the court finds that the amendment was in bad faith or would cause prejudice to creditors. 672 F.2d at 833. Recently, a court held that the debtor could not amend his exemption schedule to claim the personal property exemption because of prejudice to creditors caused by the timing of the amendment and the res judicata effect of the court's order sustaining the trustee's objection to initially claimed exemptions. In re Wilson, 2011 WL 666514, 4 (Bkrtcy. M.D. Fla. 2011) ("In this case, the Trustee argues that the Debtor's belated responses sound in bad faith and laches, and that the delayed amendment has unnecessarily created additional expenses in prosecuting the Initial Motion for Turnover and Motion to Compel. These additional administrative expenses will prejudice creditors in that it will reduce any ultimate distribution to them. The Court finds that while this prejudice is not great, it does constitute some prejudice because the Trustee continued forward in prosecuting the turnover of the Debtor's non-exempt property based on the assumption that the wildcard exemption had never been claimed, either at the beginning of the case or in connection with the Trustee's Initial Motion for Turnover."). The debtor may end up losing the benefit of the personal property exemption and their homestead if they wait too long to decide whether they want to keep their homestead or receive the enhanced "wildcard" personal property exemption. In the case of a debtor that is in default on the homestead mortgage, this could be devastating. The debtor will more than likely lose their home to foreclosure, and would have forfeited their rights to the personal property exemption. See In re Wilson, 2011 WL 666514 at 4 ("An endless cycle of amendments and litigation thereon would certainly frustrate the bankruptcy system's goal to swiftly and efficiently resolve disputed claims. In this respect, the Eleventh Circuit's precedent in Doan, gives the Court discretion to "deny leave to amend on a showing of a debtor's bad faith or of prejudice to creditors.").

In conclusion, we have learned the following from Osborne. The debtor does not need to surrender the homestead property to receive the enhanced "wildcard" personal property exemption. The only benefit that flows from the homestead exemption is that the Trustee is prevented from administering the homestead property as part of the bankruptcy estate. In addition, while timeliness is not a prerequisite of the personal property exemption, a debtor's amendment of Schedule C may not be allowed if it is prejudicial to creditors or filed in bad faith. If the debtor is allowed to amend Schedule C to decline the exemption of the homestead property, this alone changes the debtor's entitlement to the homestead exemption (absent a finding that the debtor is benefitting indirectly from the homestead exemption).

Tampa Bay Bankruptcy Bar Association
Presents

RAYS NIGHT

Save the Date

Friday, August 5th, 2011

Tampa Bay Rays vs. Oakland Athletics
Game starts at 7:10 p.m.
Tropicana Field

Come enjoy a night of fun at the ballpark with fellow colleagues, family & friends while supporting your association!

For more information on this event contact:
Robert Wahl at 289-0700 or rwahl@forizs-dogali.com, Luis Martinez-Monfort at 579-4010 or lmmonfort@bpmmlaw.com, or Keith Appleby at 579-4010 or kappleby@fowlerwhite.com.

Chapter 7 Debtors Inability to Strip Unsecured Liens Affirmed

by Rubina K. Shaldjian, Esq.
Florida Default Law Group, PL

In July 2010, Judge Jennemann held Chapter 7 debtors cannot "strip off" their wholly unsecured junior liens under § 506(d) of the Bankruptcy Code.[1] The Chapter 7 Debtors appealed and sought to have the court declare the junior lien on their residence as wholly unsecured, because the value of the property was insufficient to protect the junior lien holder.

United States District Judge Gregory A. Presnell affirmed the Bankruptcy Court's decision.[2] The District Court's position is in line with the Fourth and Sixth Circuits, as well as the Bankruptcy Appellate Panel for the Ninth Circuit.[3]

Like the Bankruptcy Court, the District Court followed the reasoning in *Dewsnup v. Timm*.[4] Although *Dewsnup* dealt with a single under-secured creditor who could not strip off the unsecured portion, the court explained that the Debtors failed to provide a persuasive argument as to why the Supreme Court's reasoning shouldn't extend to wholly unsecured junior lienors. Judge Presnell also reiterated that relying on § 506(a) to interpret § 506(d) is inconsistent with *Dewsnup*.

Finally the court rejected the Debtors' policy argument with respect to maintaining equity among creditors, because Congress has not enacted any legislation overturning *Dewsnup* in 20 years since the Supreme Court handed down the decision.

1 In re Hoffman, 09-18839 (Bankr. M.D. Fla. Filed Dec. 10, 2009) (Memorandum Opinion Denying Debtors' Motions to Avoid Junior Liens).
2 Armstrong v. Regions Bank, 10-1316 (M.D. Fla. Filed Sept 1, 2010) (Order).
3 *Id.* (citing Talbert v. City Mortgage Servs, 334 F.3d 555 (6th Cir. 2003); Ryan v. Homecomings Fin. Network, 253 F.3d 778 (4th Cir. 2001); In re Laskin, 222 B.R. 872 (B.A.P. 9th Cir. 1998)).
4 502 U.S. 410 (1992).

People on the Move

Karan S. Nayee has joined Donica Law Firm, PA., in Tampa as an associate. Mr. Nayee graduated from Thomas M. Cooley Law School, Auburn Hills, Michigan and will be concentrating his practice in insolvency law with a focus on representing bankruptcy trustees and fiduciaries.

Movers & Shakers

Holland & Knight is pleased to announce that Tampa Partner, **Leonard H. Gilbert**, is the 2011 recipient of the Distinguished Service Award (DSA), the highest honor awarded by the American College of Bankruptcy (the College). The DSA is given annually for significant accomplishments in improving the administration of justice in the insolvency and bankruptcy field, primarily arising from volunteer activities (rather than services to a client or as a judge or other professional). Gilbert was selected for this award for his continuous and dedicated contributions to the College and to the field of bankruptcy law.

The 2010 DSA recipient, Neal Batson, said during his presentation of Gilbert's award on March 18 in the Great Hall of the U.S. Supreme Court, "I am honored to present the Distinguished Service Award to my friend Leonard Gilbert. His distinguished service has continued for more than half a century."

Gilbert has served with distinction as a Fellow, Regent, Director and the Chair of the Judicial Nominating Committee for the College and as a Director and Treasurer of the College's Foundation. His volunteer activities include professional, charitable and cultural organizations on the local, state, national and international levels which include: President of The Florida Bar, President of the American College of Commercial Finance Lawyers, Chairman of the Tampa Bay Bankruptcy Bar Association, President of the Tampa Museum of Art, Chairman of the Arts Council of Tampa and Hillsborough County, President of the Harvard Law School Association of Florida, President of the Midtown Kiwanis Club, Chairman of the General Practice Section and a Member of the House of Delegates of the American Bar Association, Co-Chair of the International Bar Association Section on Insolvency Law, a member of the Judicial Legal Delegation to the People's Republic of China, and many more.

Gilbert, who was recently recognized by The Bankruptcy Bar Association Southern District of Florida for practicing bankruptcy law for more than 45 years, currently practices at Holland & Knight in the areas of banking, commercial finance, creditors' rights, insolvency, and commercial litigation. In his bankruptcy practice, Gilbert has represented numerous state, national and international banks and other financial institutions and public bodies, secured and unsecured creditors' committees and equity.

Ronald Bidwell was an Honoree at the Thirteenth Judicial Circuit's Annual Pro Bono Awards Ceremony on April 13, 2011. The Committee presented an award to Mr. Bidwell for the extraordinary number of hours and services he devoted to Bay Area Volunteers Program.

March, 2011

This open letter to attorneys who represent parties at Section 341 meetings, whether as counsel of record or special appearance counsel, is written with the consensus of the Office of the United States Trustee, Tampa, Florida Office, and the Tampa Division Judges of the Middle District of Florida.

Attorneys frequently discuss the issue of professionalism in the legal practice and the public's perception of the legal profession. In Chapter 7 and Chapter 13 bankruptcy cases, the 341 meeting of creditors is frequently your clients' only experience with the federal court system. Many debtors are unfamiliar with the process and find it to be very stressful. The behavior of the attorneys and trustees at the 341 meeting should convey the seriousness of the proceeding to all persons in attendance. Lack of proper dress, disrespectful attitudes or language, tardiness, lack of preparation and excessive background noise diminish the significance of 341 meetings, cause delays and convey a negative image of the legal system and judicial process. The following suggestions are designed to promote an atmosphere of professionalism and to increase the public's confidence in our bankruptcy courts and the bankruptcy process.

1. Timeliness. The increases in filings over the past several years have resulted in heavier calendars for each of the trustees. The trustees endeavor to conduct the meetings in a prompt fashion, but delays in waiting for attorneys can add several minutes to each case. Your being present on time and when your case is called will greatly facilitate the process.

2. Attire. We all know that standards of business attire have relaxed over the years and that many attorneys dress in "business casual" while working at their offices. Most attorneys take care to dress appropriately for appearances in court. But some have observed that the standard of dress at the 341 meetings has been relaxed to a point that it no longer appears professional. Some attorneys may feel that their clients are more relaxed when the attorney is casually dressed. While clients should always be made to feel at ease, the 341 meeting is a quasi-judicial proceeding with serious legal repercussions. A level of formality in dress (appropriate business attire for men and women) reinforces everyone's awareness of the significance of the meeting.

3. General Decorum. The 341 meetings are recorded. The quality of the recording is greatly affected by background noise in the meeting room. To the extent possible, attorneys waiting for their cases to be called should consult with their clients outside of the meeting room. In light of the legal significance of the 341 meeting, jokes, laughter and casual asides (particularly with the trustee) are not appropriate.

New Bankruptcy Rules Take Effect Dec. 1, 2011

This is a reprint of information provided by the CLLA (Commercial Law League of America.) Additional information about these new rules can be found on the website for the United States Courts at www.uscourts.gov/RulesAndPolicies/FederalRulemaking/Overview.aspx

On April 26, the U.S. Supreme Court approved and forwarded to Congress amendments to the Federal Rules of Bankruptcy Procedure, Federal Rules of Appellate Procedure, and Federal Rules of Evidence. A proposed amendment, which has proved to be controversial, would be made to Fed. R. Bankr. P. 2019 to make creditors disclose the price they paid for claims.

The amendments take effect Dec.1, unless Congress, in the interim, rejects, modifies, or defers them.

Proposed amendments to Bankruptcy Rule 2019, which applies to Chapter 9 and Chapter 11 proceedings, would require committees, groups, or entities that consist of or represent creditors or equity security holders who are acting in concert to identify their "disclosable economic interests" relating to the debtor. The proposed amendments would broadly define the term to include economic rights and interests that are affected by the value, acquisition, or disposition of a claim or interest.

The conference's Rules Committee, in a report discussing proposed rule amendments of significant interest, describing arguments in favor of the amendment to Bankruptcy Rule 2019 said that the proposed disclosure requirement is important in order to reveal potential conflicts of interest and to permit evaluation of positions taken by such groups, committees, and entities.

Proposed new Bankruptcy Rule 1004.2 would require that a petition for recognition of a foreign proceeding under new Chapter 15, applicable to ancillary and other cross-border cases, identify the countries where a foreign proceeding is pending against the same debtor and the country where the debtor has its "center of main interests."

A proposed amendment to Bankruptcy Rule 2003 would require the presiding official to file a statement upon adjourning a meeting of creditors or equity security holders. The requirement aims to ensure that the record reflects whether the meeting of creditors was concluded or extended to another day and if extended, when it will resume.

A proposed amendment to Rule 3001 would require creditors to provide additional information supporting certain proofs of claim and impose penalties if creditors fail to comply with the new disclosure requirements. The sanctions provision would allow a court to prohibit the creditor from presenting omitted information as evidence in a contested matter or adversary proceeding in the case, but only if the failure to provide the required information was not "substantially justified or...harmless."

Proposed new Bankruptcy Rule 3002.1 would implement Section 1322(b) (5) of the Bankruptcy Code, which permits a Chapter 13 debtor to cure a default and maintain payments of a home mortgage.

A proposed amendment to Bankruptcy Rule 4004 would provide that a party may seek an extension of time, based on newly discovered information, to object to a debtor's discharge after the time for objecting expires

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New Rules

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but before a discharge is granted.

A proposed amendment to Bankruptcy Rule 6003 would clarify that the 21-day waiting period before a court can enter certain orders at the beginning of a case, including an order approving employment of counsel, does not prevent the court from specifying an effective date for the order that is earlier than the date that the order is entered.

Appellate Rules 4 and 40 would be amended to clarify that additional time is provided to the government to appeal or to seek rehearing in a case in which the United States, a federal agency, or a federal employee is a party to the litigation.

Existing Rule 4 provides a 60-day appeal period in a case in which the "United States or its officer or agency is a party." The same provision is included in 28 U.S.C. § 2107. A proposed amendment to Rule 4(a)(1)(B) would clarify that the 60-day appeal period applies in cases in which an officer or employee of the United States is sued in an individual capacity for acts or omissions occurring in connection with duties performed on behalf of the United States.

The proposed amendment is consistent with Civil Rule 12(a) (3), which recognizes that the government requires additional time to determine whether to provide representation to the defendant officer or employee. The same reasons justify providing additional time to the solicitor general to decide whether to file an appeal, according to notes prepared by the Judicial Conference of the United States's Advisory Committee on Appellate Rules, which prepared the proposed rule amendments.

The same reasons also apply to a petition for panel rehearing in such cases, according to the advisory committee. Thus, the proposed amendment to Rule 40 (a) (1) would make clear that the period to file the petition is 45 days. To avoid any potential jurisdictional issue, the Judicial Conference has requested that Congress amend Section 2107, coordinated to have the same provisions and to take effect on the same day as the amendments to Rule 4.

The rule amendments are posted on the Federal Judiciary website.

What is the best way to connect with your fellow insolvency professionals both in and away from your office?

Via ABI's Social Networking Groups – whether you use LinkedIn, Facebook or Twitter, ABI keeps you connected with all of the latest bankruptcy news.

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