Bankruptcy misc. research

The Cram-Down

VOL. 3 NO. 3 | Tampa Bay Bankruptcy Bar Association Newsletter | Spring 1993

SUPREME COURT RULING PROHIBITS CHAPTER 13 RESIDENTIAL MORTGAGE LIEN STRIPPING

In recent years, Chapter 13 debtors have experienced increasing success in their attempts to bifurcate the allowed claims of their undersecured home mortgage lenders pursuant to Bankruptcy Code § 506 (a). Lenders have argued that § 1322 (b) (2) implicitly prohibits Chapter 13 debtors from modifying residential mortgage lenders' rights in this manner. Four Circuit Courts of Appeal have permitted this so-called practice of "home mortgage cram-down" or "residential lien stripping." See In re Bellamy, 962 F.2d 176 (2nd Cir. 1992); In re Hart, 923 F.2d 1410 (10th Cir. 1991); Wilson v. Commonwealth Mortgage Corp., 859 F.2d 123 (3rd Cir. 1990); In re Hougland, 886 F.2d 1182 (9th Cir. 1989); however, on June 1, 1993, the United States Supreme Court overruled these Circuits in an opinion that will prohibit Chapter 13 residential lien stripping. The opinion, in Nobelman v. American Savings Bank, 1993 U.S. LEXIS 3745 (U.S. 1993), has resolved a conflict among the Courts of Appeal that was created upon the Fifth Circuit's issuance of its opinion in In re Nobelman, 968 F.2d 483 (5th Cir. 1992).

Nobelman involved a confirmation dispute between Chapter 13 debtors and a lender holding a deed of trust on the debtors' principal residence, a Dallas, Texas, condominium. The debtors had purchased the condominium in 1984 for $68,250. In 1990, when the debtors filed their Chapter 13 petition, the residence was valued at only $23,500. The debtors' Chapter 13 plan proposed to treat the secured portion of the lender's claim as fully secured, but proposed to treat the remainder of the lender's $71,335 claim as a general unsecured claim. The debtors' plan provided no recovery for general unsecured creditors.

In support of confirmation, the Nobelman debtors relied upon § 506(a), which provides in part as follows:

> (A)n allowed claim of a creditor secured by a lien on property in which the estate has an interest . . .is secured claim to the extent of the value of such creditor's interest . . . and is an unsecured claim to the extent that the value of such creditor's interest . . . is less than the amount of such allowed claim . . . .

In opposition to confirmation of the debtors' plan, the Nobelman lender invoked Bankruptcy Code § 1322(b)(2), which provides that a Chapter 13 plan may

> modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence . . .

The Chapter 13 trustee concurred. In response, the Nobelman debtors further argued that § 1322(b)(2) only protects that portion of a residential mortgage lender's claim that is a "secured claim" as contemplated pursuant to Bankruptcy Code § 506(a). Accordingly, they contended that the Nobelman lender's unsecured deficiency claim would not be protected by § 1322(b)(2).

Sustaining the objections of the lender and the Chapter 13 trustee, the Bankruptcy Court denied confirmation of the Nobelman Chapter 13 plan. Upon appeal, the District Court affirmed, In re Nobelman, 129 B.R. 98 (Bankr. N.D. Tex. 1991), as did the Fifth Circuit, 968 F.2d 483 (5th Cir. 1992). Unanimously affirming the rulings of the lower Nobelman courts, Justice Thomas' opinion distinguished between § 506(a)'s application to creditors' "claims" and § 1322(b)(2)'s broader application to creditors' "rights." The Nobelman opinion observed that § 506(a) permits bifurcation of "an allowed claim" into secured and unsecured claims. By contrast, § 1322(b)(2) broadly prohibits any modification of a residential mortgage lender's "rights." Accordingly, the protections of § 1322(b)(2) are not limited to the secured portion of a residential mortgage lender's claim, but rather to all rights created pursuant to a residential mortgage or deed of trust. Notwithstanding the results of any valuation of collateral pursuant to § 506(a), the Nobelman Chapter 13 plan would have substantially modified the lender's rights. The Nobelman opinion therefore affirmed the ruling that this plan was unconfirmable as a matter of law.

As noted in Justice Stevens' concurring opinion, the Nobelman result is consistent with the legislative history of Chapter 13. The legislative history reflects a congressional intent to preserve the residential lending industry. Hearings Before the Subcommittee on Improvements of the Judicial Machinery of the Senate Committee on the Judiciary, 95th Cong., 1st Sess. (1977) (pp. 652-53 (Wiese), 703, 707, 714-15 (discouragement of savings and loan associations making home loans), 719-21 (Kulik, National Association of Real Estate Investment Trusts)). Additionally, the Nobelman opinion is consistent with the related Supreme Court opinion in Dewsnup v. Timm, 116 L.Ed.2d 903 (1992) (Blackmun). In its Dewsnup opinion, the Supreme Court prohibited Chapter 7 debtors from using § 506(a) to engage in lien stripping of undersecured mortgage claims to enable them to redeem inexpensively. Judge Thomas did not participate in the consideration or decision of Dewsnup.

(Continued on page 5)

INSIDE

· Exemption Legislation
· Pioneer Investment Services

PRESIDENT'S COLUMN

It has been a pleasure to have served as your President - all 275 of you - during this past year. Thanks to much hard work by many people, we have accomplished a great deal. I am especially grateful to Roberta Colton and Sharyn Zuch, the co-chairs of the Meetings, Programs, and Continuing Legal Education Committee and to all of you who have worked to provide us with top quality CLE programs this past year, including Russell M. Blain, Steven Berman, Randolph Fabal, Camille Iurillo, John Lamoureux, Randall Lord, Kathleen McLeroy, Catherine McEwen, Kevin O'Brien, and Lynn Ramey.

Michael Horan and his Publications and Newsletter Committee have done a superb job in putting out three issues of The Cram-Down. Lynne England has served double duty as the Treasurer for the Association as well as chair of the special committee concerning the computer access program to the bankruptcy court clerk's office and deserves special recognition for handling both jobs so competently. I am grateful to Harley Riedel as chair of the Membership and the Elections Committee and Stephen Meininger, the chair of the Court, United States Trustee and Clerk Liaison Committee. I am very appreciative of the work of Robert Glenn and Leonard Gilbert for their work on a special committee on long range planning for the Association.

Bob Glenn, John Yanchunis, and Chip Morse have worked diligently and are leaving the Board of Directors. We will miss them as board members, but look forward to their continuing to work on behalf of the Association. I am particularly grateful to Bob Glenn who has served on the Board since the organization of the Association and has been a mentor to me this past year.

As one athletic coach was quoted upon winning a championship, "I could not have won without the players." We would not have had this great year without the work of all of you.

The Association will conclude the year with our Fifth Annual Dinner and Dance at the University Club of Tampa, 3800 Tampa City Center, on Friday, June 11, 1993. I hope each of you will join us for this festive occasion.

Tom Mimms

NO NEW JUDGES YET

Chief Judge Paskay, Judge Baynes and Chief Deputy Clerk Kilcoyne graciously offered to meet with the officers and directors of this association on May 20 to discuss the status of the new bankruptcy judges, and other related matters. Judge Paskay stated he doubted that Congress would appropriate funding for the new bankruptcy judges in this fiscal year, which ends on September 30. Renovation of existing space to accommodate two new courtrooms also will not be completed this fiscal year.

The move of Judge Briskman from Mobile to Orlando has been placed on hold. Recent reports in the press suggest that some congressmen, citing the drop in bankruptcy filings nationally, question whether the authorization of new bankruptcy judges should be reconsidered. Accordingly, Judge Paskay believes that we should not expect the two new bankruptcy judges to arrive in Tampa before November 1, 1993.

Nevertheless, the Judges and Mr. Kilcoyne have devised a procedure for dividing existing case loads and assigning new cases when (and if) the new judges arrive. Existing cases will be reassigned to new judges, although Judges Paskay and Baynes will exercise discretion to keep cases where substantial activity has already occurred. For example, a Chapter 7 case involving an adversary proceeding which has proceeded to pretrial conference or has been set for final evidentiary hearing, or a Chapter 11 case that has been noticed for a disclosure statement hearing, normally would not be reassigned. After the arrival of the new judges, Judge Paskay will be assigned all cases filed in the Ft. Myers Division. In the Tampa Division, Judge Baynes and the two new judges would share equally in the random draw for Chapter 7 and Chapter 13 cases. Each of the four judges would share equally in the random draw for Chapter 11 cases.

The Judges and Mr. Kilcoyne recognize that four judges simultaneously running hearing calendars will cause attorney conflicts. This is a difficult problem to resolve. Judge Baynes suggests that to the extent possible, the judges should schedule certain case types on different days; for example, each judge could have a different "Chapter 13 Day." The clerk's office is also attempting to develop a data base that will flag attorney conflicts for case managers before hearings are scheduled.

The Judges are also sensitive to the problem of procedural uniformity. Judges Paskay and Baynes are aware of the concern of attorneys and the clerk's office that the existence of four different procedures for four different judges could prove unwieldy. The group discussed a proposal that procedures be largely standardized, and that changes only be made by majority vote of the Judges.

Mike Horan

1993 LEGISLATIVE CHANGES REGARDING EXEMPTIONS

The Florida Legislature recently passed a bill which makes substantive changes to Chapter 222 of the Florida Statutes. These changes restrict the extent of statutory exemptions from creditor claims. The changes will effect garnishment of wages, personal property exemptions and fraudulent conversion. The effective date of these changes is October 1, 1993.

A summary of the statutory changes:

Garnishment of Wages

- clarifies that sovereign immunity does not preclude a creditor's right to garnish the wages of government employees. Therefore, city, county and state employees will be subject to wage garnishment;
- provides that to a limited extent, the head of household will now be subject to wage garnishment. The first $500.00 per week of head of household disposable earnings remain exempt;
- limits to six months the exemption from attachment of traceable earnings deposited in any financial institution (the so-called "wage account"). Presently, such traceable head of family earnings deposited in banks are completely exempt from attachment.

Personal Property

- provides for a $1,000.00 exemption in a single motor vehicle;
- exempts professionally prescribed health aids for the debtor, or a dependant of the debtor.

Fraudulent Conversion

- prohibits allowance of an exemption to the extent it results from a fraudulent transfer or conveyance;
- defines fraudulent asset conversions, to wit: any conversion which results in the proceeds of the asset becoming exempt from creditor claims (whether the creditor's claim arose before or after the conversion of the asset) if the debtor made the conversion with the intent to hinder, delay or defraud the creditor;
- provides a four year statute of limitations on creditor actions for fraudulent asset conversion;

These statutory changes certainly are great news for creditors. However, creditor euphoria should be tempered somewhat, since these significant changes in the law will be applicable only to financial transactions, and to any fraudulent asset conversion, which occur on or after the law's effective date — October 1, 1993.

Dennis LeVine

CONSTRUCTION / DESTRUCTION OF DEBTORS' BUDGETS USING DATA FROM 1990 CENSUS

As a federal taxpayer who itemizes deductions on Schedule A of Form 1040, every year I note with interest the chart of average itemized deductions published in the U.S. Master Tax Guide by Commerce Clearing House, Inc. (for example, see ¶88, 1993 U.S. Master Tax Guide (76th Ed., Commerce Clearing House, Inc. 1992, pp. 76)). Now, our friendly bureaucrats in Washington, D.C. have provided similar information which is useful in the bankruptcy context.

For Debtors who itemize their expenses on Schedule J and all others who assess the reasonableness of Debtors' budgets, charts in the U.S. Bureau of the Census, Statistical Abstract of the United States: 1992 (112th Ed. Washington, D.C. 1992) on pages 442 and 443 should be of special interest.

These charts state the average annual expenditures of consumers in 1990 for such categories as food, housing, clothing, transportation, health care, insurance, taxes and personal expenses. The charts refer to people as "consumer units" and include single person consumer units, husband and wife consumer units, and consumer units of two or more persons. Some categories seem to overlap, so the charts are not very "user-friendly" or easy to understand. For example, the annual food expenditure for a single person shows up in the charts in three places with three different amounts:

One Person Consumer unit	$2,302
Single Consumer: No earner	$1,774
Single Consumer: One earner	$2,592

Throwing out the low figure gives a range between $2300 and $2,600 for annual food expenditures for a single consumer in 1990.

For an illustration of the utility of such information, see In Re Smurthwaite, 149 B.R. 409 (Bankr. N.D. W.Va. 1992), where the Bankruptcy Court for the Northern District of West Virginia used census data as one basis for ruling that the Debtor's proposed budget was excessive or unreasonable. The Chapter 7 Debtor's original budget included $250 per month for food. Subsequent to the U.S. Trustee's Motion to Dismiss for Substantial Abuse under Bankruptcy Code 707(b), the Debtor amended his petition, increasing his food expenditures by 20% (from $250 to $300 per month).

Referring to the census data in the Statistical Abstract, the Court noted that the average annual food expenditure for a single consumer in 1990 ranged between $2,300 and $2,600 (or roughly $200 per month), and that the Debtor purported to spend approximately 50% more on food than the average single consumer. These facts resulted in a finding by the Court that the Debtor's proposed budget was excessive or unreasonable.

If you want a copy of the Statistical Abstract of the United States, 1992, order it from the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402-9325. To order or verify prices call 202-783-3238. To FAX orders or inquiries, dial 202-512-2250.

Philip E. Perrey

SUPREME COURT CLARIFIES & LIBERALIZES EXCUSABLE NEGLECT STANDARD

In Pioneer Investment Servs. Co. vs. New Brunswick Assoc. Ltd. Partnership. 113 S. Ct. 1489; 1993 U.S. Lexis 2402 (1993), the United States Supreme Court clarified and liberalized the excusable neglect standard in connection with the allowance of late filed Proofs of Claim under Federal Rule of Bankruptcy Procedure 9006(b)(1). Pioneer is instructive in that the Supreme Court rejected the 11th Circuit's narrower view of excusable neglect. See In re Analytical Systems, Inc., 933 F.2d 939-942 (11th Cir. 1991). Under the 11th Circuit view, excusable neglect under Rule 9006(b)(1) required a showing that the delay was caused by circumstance beyond the movant's control. Justice White, writing for the majority, rejected the Debtor's contention that a showing of excusable neglect required circumstances beyond the reasonable control of the party seeking to file a late Proof of Claim. The Pioneer Court went on to find that requiring the showing that circumstances were beyond the reasonable control of the party was not consistent with either the language of Rule 9006 (b)(1) or the purposes underlying the rule.

Factual and Procedural Background

Pioneer Investments Servs. Co. ("Pioneer Investments" or "Debtor") filed a Voluntary Petition under Chapter 11 of the Bankruptcy Code on April 12, 1989. New Brunswick Assoc. Ltd. Partnership ("Brunswick" or "Creditor") was listed as a contingent, unliquidated or disputed claimant on the Debtor's Schedules. On April 13, 1989, the Bankruptcy Court mailed a Notice of Meeting of Creditors to Pioneer Investment's creditors which contained an August 3, 1989 bar date. The notice also indicated that creditors must file a Proof of Claim if the claim was scheduled as "disputed, contingent or unliquidated." The record revealed that the President of the corporate general partner of Brunswick received the notice, attended the creditors' meeting and retained an experienced bankruptcy attorney. Brunswick's attorney was provided with a copy of the notice to creditors.

In due course, on August 23, 1989, Brunswick filed their Proofs of Claim and a motion to permit the late filing of those claims under Bankruptcy Rule 9006(b)(1). The motion recited that Brunswick's counsel was unaware of the bar date and that it came at a time when he was experiencing a major disruption in his professional life caused by his withdrawal from his former law firm. As a result of the disruption, counsel did not have access to the copy of the case file until mid-August.

The Bankruptcy Court, adopting the 11th Circuit view, refused the late filing, holding that a party can claim excusable neglect only if its failure to timely perform a duty was due to circumstances which were beyond its reasonable control. On appeal, the District Court affirmed, in part, and reversed, in part, and instructed the Bankruptcy Court to adopt a more liberal approach to the excusable neglect standard similar to the standard set forth in In re Dix, 95 B.R. 134, 138 (B.A.P. 9th Cir. 1988). On remand, the Bankruptcy Court applied the factors set forth in Dix, and once again, denied Brunswick's motion to file its late Proofs of Claim. The creditor once again appealed the Bankruptcy Court's decision. Thereafter, the District Court affirmed the Bankruptcy Court's ruling.

The Court of Appeals for the 6th Circuit reversed the District Court and held that excusable neglect was not limited to cases where the failure to act was due to circumstances beyond the movant's control. Moreover, the 6th Circuit's analysis compared the Notice to Creditors in the Pioneer case with the model notice set out in the Official Bankruptcy Forms and found that a "dramatic ambiguity" in the notice to creditors would have confused even persons experienced in bankruptcy law. The 6th Circuit went on to discuss counsel's role and ultimately concluded that the Bankruptcy Court had inappropriately penalized Brunswick for the errors of its counsel. The 6th Circuit found that the record demonstrated excusable neglect. The Court found that an equitable inquiry was required in analyzing excusable neglect under Rule 9006(b)(1).

Supreme Court Analysis

The Supreme Court began its analysis by finding that the dictionary definition of neglect included both simple, faultless omissions to act and, more commonly, omissions caused by carelessness. According to Justice White, applying the ordinary, contemporary meaning to the word neglect, Congress contemplated that Courts would be permitted to accept late filings caused by inadvertence, mistake, or carelessness, as well as intervening circumstances beyond the party's control.

The Pioneer Court then discussed the Dix factors and found that Brunswick's neglect was, in fact, excusable. As set forth by the Court, the four (4) Dix factors are:

1. Whether granting the delay will prejudice the Debtor.
2. The length of the delay and its impact on efficient Court administration.
3. Whether the delay was beyond the reasonable control of the person whose duty it was to perform.
4. Whether the creditor acted in good faith.

Although the Supreme Court affirmed the 6th Circuit's decision, it did disagree with the 6th Circuit's analysis regarding the omissions of Brunswick's attorney. Citing agency law, the Court pointed out that clients must be held accountable for the acts and omissions of their attorneys. The client, who has selected an attorney, is bound by the acts of the lawyer agent and is considered to have notice of all facts.

Accordingly, the Court gave little weight to the disruption in counsel's practice; however, the Court did consider it significant that the notice of bar date provided by the Bankruptcy Court was not adequate notice under the circumstances. The Court indicated that the bar date in a bankruptcy case should be prominently announced and accompanied by an explanation of its significance. Applying the Dix factors, the Court held that the dramatic ambiguity, when coupled with the absence of prejudice to the Debtor or judicial administration, and a lack of bad faith established that the neglect was excusable. The 6th Circuit's decision was affirmed by the Supreme Court 5-4, and the late filed claims were allowed.

Justice O'Conner, writing for the dissent, argued that the majority engrafted a balancing test upon Rule 9006(b)(1) instead of following the two (2) part analysis set forth in the Rule.

(Continued on page 5)

(continued from page 1 Lien Stripping)

The Nobelman ruling is also consistent with the previous opinions of our judges in the Tampa Division. On February 12, 1992, Judge Baynes issued an opinion in In re Davidoff, 136 B.R. 567 (Bankr. M.D. Fla. 1992), on an order denying Chapter 13 debtors' second amended motion to value the collateral of a residential mortgage lender. Two days later, Judge Paskay issued an opinion in In re Ireland, 137 B.R. 65 (Bankr. M.D. Fla. 1992), also on the denial of Chapter 13 debtors' motion to value collateral of a residential mortgage lender. Both cases involved facts very similar to those at issue in Nobelman.

John Anthony

Amendment to Local Rule 1.04

Local Rule 1.04 "Assignment of cases initially and on Recusal or Disqualification", was recently amended by Order of the Bankruptcy Judges in the Middle District. The amended rule sets out in more detail the procedures to be followed in the event cases and proceedings are reassigned due to disqualification for recusal.

Dennis LeVine

(continued from page 4 Excusable Neglect)

According to Justice O'Conner, the Court refused to follow the plain meaning of Rule 9006(b)(1). As explained by the dissent, under a plain meaning interpretation, a two (2) step analysis was required. First, no relief is available unless the failure to comply with the deadline is actually the result of excusable neglect. In short, the failure to timely file must be "excusable." Second, the Court may then consider the equities. The dissent argued that Rule 9006(b)(1) does not require the Court to forgive every omission caused by excusable neglect, but states that the Court "may" grant relief "in its discretion." According to Justice O' Conner, the majority's interpretation effectively read the word excusable out of the Rule because any neglect could be forgiven.

Al Gomez

MOVERS AND SHAKERS

Movers:

Lynn Ramey recently joined Rumberger, Kirk & Caldwell, P.A. from Bush, Ross, Gardner, Warren & Rudy, P.A. She will continue her practice in the bankruptcy area.

Camille Iurillo left Rumberger, Kirk & Caldwell, P.A. to join the Clearwater firm of Carson & Bobenhausen. She is practicing bankruptcy and commercial litigation.

Michael Brundage left Holland & Knight to continue in the bankruptcy area at Honigman, Miller, Schwartz and Cohn.

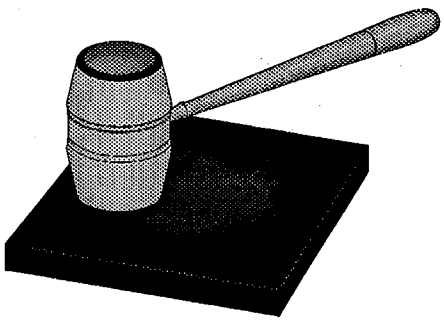
Gray Gibbs left Foley & Lardner and has established his own bankruptcy and tax practice in St. Petersburg, Florida.

Laura Prather is now with the Tampa office of Icard, Merrill, Cullis, Timm, Furen & Ginsburg, P.A. She formerly practiced with Rydberg, Goldstein & Bolves, P.A.

Wanda Hagan Anthony recently left Trenam, Simmons, Kemker, Scharf, Barkin, Frye & O'Neill to join the firm of Stichter, Riedel, Blain & Prosser, P.A.

Shakers:

Terry Smith, our new Chapter 13 Trustee, can be reached at Chris Larimore's old office on Wednesdays and Fridays at phone number 813-758-4635.



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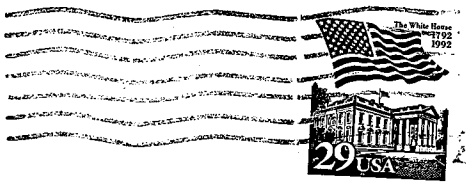

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