Reflections of a Retiring Judge
By Douglas O. Tice Jr. 1

My decision to retire is one of the most difficult I have made this past 25 years. My reluctance is not difficult to explain. Service as a bankruptcy judge has been highly gratifying in itself, and I cannot leave such a post without misgivings. However, what I will miss most are the people who make up the court—the judges, my personal staff including law clerks, past and present, other court employees, practicing attorneys, and, yes, I will even miss (most of) the debtors. I will elaborate on these thoughts later in this article.

The Early Years.
I followed a circuitous route to the bench. I grew up in Greensboro, North Carolina, and attended the University of North Carolina for both undergraduate and law school. In 1961, I moved to Richmond from a real estate law practice in Raleigh and became an Internal Revenue Service attorney. After nine years, I left IRS in 1970 to become corporate counsel to a real estate developer in Richmond. This employment ended in 1975 after my employer filed a Chapter XII real property arrangement under the Bankruptcy Act. At the time, it was said to be the largest bankruptcy filing in Virginia history. So, in August 1975, I was cast on the street at the tender age of 42, looking for a job as a Virginia lawyer. Unable to find employment, I found a couple of lawyers with offices on East Main Street who took me in to help pay the rent.

I wanted to build a law practice that did not include domestic relations or criminal law and thought to try my hand as a trustee in bankruptcy. Then, as now, the Eastern District of Virginia had four judicial divisions. Spread among the divisions were three referees in bankruptcy, Henry D. Evans in Richmond, Martin V.B. Bostetter in Alexandria, and Hal J. Bonney in Norfolk-Newport News. After opening my new office, I sought out the Richmond referee, Henry Evans, who was an old friend from government service. When I knew him previously, Henry had been a federal probation officer. At that time he was a law school graduate but had never taken a Bar exam. It is fairly common knowledge that as Henry neared retirement age, District Judge Robert R. Merhige Jr. told him that if he would pass the Virginia Bar Exam, Judge Merhige would appoint him referee in bankruptcy, a position that would improve his retirement annuity.

Catching Henry on the street at...
lunch one day, I asked him if Richmond could use a new bankruptcy trustee. Demonstrating the casual approach of bankruptcy practice in those days, Referee Evans approved me on the spot and instructed me to train for the job by attending one or two first meetings of creditors. In particular, he told me to observe a meeting when Richmond lawyer Blackwell N. Shelley was to be trustee of the day.

So it was that soon after beginning my law practice in Richmond, I was being assigned cases as trustee in bankruptcy under the Bankruptcy Act of 1938. At that time, first meetings of creditors were held in the bankruptcy courtroom, a small room on the third floor of Richmond’s Federal Courthouse on East Main Street. Creditor meetings then were essentially court sessions, presided over by the judge, and the debtors (or bankrupts as they were then known) were called in turn, sworn, and examined in a witness box. After questions from the judge, the trustee examined the debtor, asking questions primarily about assets that may have been omitted from the schedules. One characteristic of those early creditor meetings was the presence of creditors’ lawyers who were actively seeking to have the trustee endorse relief from stay orders, usually for delinquent auto loans. It was not unusual

Continued from page 1

Continued on page 5
Message from the Editor

I have edited the Bankruptcy Law News for about three years now. Before serving as Editor-in-Chief, I edited the Case Summaries for over two years. An editor’s job, in essence, is to evaluate and critique. Editing taught me how easy it is to find fault in another’s work. The editor’s challenge is to convey criticism in a way that encourages the writer.

Like many lawyer, I also write. When I write, I feel a sense of ownership of my work product, as if I’ve poured in healthy measures of my own blood, sweat, and tears. For this reason, I confess that I sometimes have struggled not to take criticism of my writing personally. The writer’s challenges lies in separating the sacrifice of blood, sweat, and tears from the resulting work, and in embracing criticism in a way that fosters growth.

This is my last issue as editor of the Bankruptcy Law News. Upon reflecting, I think this experience has made me both a better writer and a better editor. Editing the Law News was made easy by the excellent writers – the practitioners, members of the bench, and court staff - who have donated their time and talents to the Law News. My red editor’s pen rarely needed a heavy hand for Law News articles, and I like to think my own writing has improved by studying what these talented colleagues submitted for publication.

This final issue for me is bittersweet. We feature a truly wonderful article by Judge Douglas O. Tice, Jr., but the occasion giving rise to the article is his retirement. In terms of my legal career, I was raised in Judge Tice’s courtroom, where he taught attorneys how to practice with civility and comity. Judge Tice welcomed everyone who entered his courtroom both well-prepared and ready to play fair. He recognized and rewarded those lawyers who made efforts to raise the level of practice, and who demonstrated respect for the court, its staff, and other members of the bar. We will greatly miss you, Judge Tice.

Judge Tice has also contributed pictures for this issue of his past and present clerks as well as a picture recently taken of the Bankruptcy Court Judges of the Eastern and Western District of Virginia. The second article contained in this issue is on means testing issues presented when a married debtor files bankruptcy but his or her spouse does not join in the case. It is written by Charlottesville practitioner Marshall Slayton and is bursting at the seams with valuable tips and references to key cases. W.L. “Chip” Craig, II, Bankruptcy Court Clerk for the Western District, reports on the state of the Clerk’s Office in the Western District, and includes an update on challenges the federal budget presents. Finally, Sarah Boehm prepared her final section as Case Summaries editor. Sarah’s tenure as the Case Summaries Editor was short-lived, though, as she graciously agreed to be my successor as Editor of the Bankruptcy Law News. Replacing Sarah as editor of the Case Summaries section will be Kelly M. Barnhart of the firm of Roussous, Lassiter, Glanzer, and Barnhart, in Norfolk.

I trust you will enjoy this issue of the Bankruptcy Law News. I am truly honored to have served the Bankruptcy Section of the Virginia State Bar through this valuable publication.

Mark Leffler
Message from the Chair of the Section  Douglas Foley

“We Virginians do not go to the storied shrines of the past to do worship but rather to gain inspiration.”

~ Douglas Southall Freeman

As my term comes to a close on the Board of Governors I want to take this opportunity to extend my heartfelt thanks to Lynn Tavenner, my immediate predecessor, and Steve Ramsdell, my successor. They are not only excellent bankruptcy attorneys and consummate professionals, but also reliable and trusted colleagues who already have made substantial contributions to the Bankruptcy Section of the Virginia State Bar for many years. It has been my privilege to serve with them on the Board and I look forward to working with them in the future as part of this organization and beyond. I also would be remiss if I did not take this opportunity in my final message to comment on the impending retirement of Judge Tice.

Most people who have practiced before Judge Tice know he is an excellent jurist with impeccable temperament. Many also know that he is a student of history – and a supremely knowledgeable one at that. His reflections in this newsletter are a prime example of that and a great history lesson for us all. Several of us had the honor of clerking for Judge Tice. I was fortunate enough to have done so when he was still the junior Judge in the District “riding circuit” throughout the Eastern District of Virginia. It made my clerkship all the more enriching and allowed my mentorship with Judge Tice to prosper. I have always said, and maintain to this day, that my year clerking for Judge Tice was the best job I have ever had – notwithstanding the modest financial compensation. I have tried to employ what I learned that year throughout my years of practicing bankruptcy law. One of the many lessons Judge Tice teaches all of his clerks – and exemplifies to all practitioners that appear before him – is professionalism and integrity. Judge Tice is truly “a lawyer’s judge” in that he expects much from those who practice before him, but also exerts the same effort and energy in his role as mentor and jurist. In short, he has personified leadership throughout his tenure on the bench in the Eastern District of Virginia and has been an inspiration to all the lawyers that clerked for him as well as the many practitioners that have appeared before him – including attorneys from other jurisdictions. We are all fortunate to have had the benefit of his wisdom, patience and experience over the past twenty-seven years as a Judge, colleague, mentor, and friend. He will be greatly missed from the bench when he retires. We all owe him a tremendous debt of gratitude for his long, faithful and diligent service to the public and the bar, and I wish him Godspeed in his future endeavors.
during a debtor’s examination for a lawyer to tug on the trustee’s sleeve and ask for his endorsement of an order. Momentarily distracted, the trustee, returning to his examination of the debtor, might unknowingly be facing a different debtor than the one he had just been examining.

In early 1976, within several weeks after I joined the trustee ranks, Referee Evans retired, and the district judges appointed Blackwell N. Shelley as the new Richmond referee, effective February 2, 1976. Judge Merhige liked to tell the story that it was only when he was administering the oath to Referee Shelley that he learned Blackwell Shelley’s middle name was Nixon. When this was revealed, Judge Merhige, who had been appointed by a Democratic President, said, jokingly, “Nixon you didn’t tell me your name is Nixon I may have to reconsider this.” Due to a rule change, within a year or so after Blackwell Shelley took office, referees in bankruptcy became bankruptcy judges, a change made official in the 1978 Bankruptcy Code.

The 1978 Bankruptcy Code.

In 1970, Congress formed a commission to review the bankruptcy laws of the United States. Extensive Congressional hearings were held to consider all aspects of then existing bankruptcy law. Collier On Bankruptcy reports that Congress found significant problems with the law in that the bankruptcy referees’ appointment and supervision of trustees presented an appearance of favoritism, the referees were performing nonjudicial administrative functions, and, by presiding over creditors meetings, referees were able to hear evidence that in court might be inadmissible.3

The commission’s work during the 1970s resulted in the enactment of the 1978 Bankruptcy Code on November 6, 1978, to be effective on October 1, 1979. The 1978 Act sought to modernize American bankruptcy law, and it remains the basis for our current bankruptcy laws. At the time of enactment, it was written that the 1978 Code was modeled after the Internal Revenue Code (obviously a model of clarity). The new code established the bankruptcy courts as adjuncts of the district court with expanded powers to enter final orders. Judges were to perform judicial functions only and were no longer involved in the appointment or supervision of trustees. The new code sought to lift the field of bankruptcy law in other, more subtle ways, such as in matters of professional compensation. Under the Act, compensation had been held down due to a supposed lack of resources in cases of insolvency. Under the Code, professional compensation was to be comparable to that in other areas of the law. (It might be argued that the Code went too far in this regard, given the routinely huge fees in modern chapter 11 cases.)

Of course, there have been significant amendments to the Code since 1978, notably in 1984 when Congress attempted to remedy the jurisdictional problems addressed by the Supreme Court in the Marathon Pipe Line Co. case (holding that bankruptcy judges could not constitutionally exercise the expanded powers provided by the Code) and the 2005 amendments affectionately known as BAPCPA. One of the ironies of 1978 Code history is the fact that Chief Justice Warren Burger urged President Carter to veto the legislation; however, in the Marathon case, the Chief Justice voted to uphold the expanded authority given bankruptcy judges in the 1978 Code as enacted.

The 1978 Code incorporated a pilot program for a United States Trustee system within the Department of Justice for general oversight of bankruptcy cases. Congress designated the Eastern District of Virginia among the first pilot districts to incorporate the program, which later became permanent nationwide except in two states. In my opinion, the presence of the Office of U.S. Trustee was a welcome addition to the bankruptcy system and particularly to consumer bankruptcy trustees because of the guidance and support the office could provide. Under the prior law a trustee often had to rely largely on the practice advice of other trustees, and I can recall cases where it was difficult to get a good answer on how to handle a particular transaction.

It is beyond my purpose to review the history of the 1978 Code except to observe in a general way how it has impacted bankruptcy law practice. With the advent of the new Code beginning in October 1979, the practice of consumer bankruptcy law under new chapters 7 and 13 opened up and became more fluid both for trustees and attorneys. Most of us who were trustees under the Bankruptcy Act continued as chapter 7 trustees, although some soon dropped out.
Initially we worked under the supervision of Francis P. Dicello, who was the first U.S. Trustee appointed for the region that included the Eastern District. The individual chapter 7 trustees replaced the judge in conducting meetings of creditors for cases assigned to them. (Code section 341 dropped the term, “first meeting of creditors.”) Chapter 7 trustees could pretty much operate on their own in liquidating small asset cases. Under the Code’s notice provisions, a trustee could sell or abandon assets without prior approval by the judge, a liberal procedure still not fully utilized by trustees. Of course it took some time for the professionals to get used to the new system.

An early and persistent criticism of the 1978 Code was that it removed the stigma of bankruptcy and made it too easy for debtors to discharge debt. There is probably some truth in this. There was another significant change in the practice of bankruptcy law from the Act. It was fairly common under the Act for lawyers who were general practitioners handling all types of cases, criminal, domestic, collections, etc., to also represent debtors in bankruptcy filings. This soon changed. In Richmond, Judge Shelley held lawyers strictly accountable for compliance with the Bankruptcy Code and Rules. He was also known for his close scrutiny of attorney fee requests. The truth was that the new Code had raised the difficulty level of bankruptcy practice, which in turn made it difficult for an attorney to be a part-time practitioner in the field. In my opinion, Judge Shelley’s strictness under the Code transformed the Bankruptcy Bar. He instilled a much higher level of professionalism in bankruptcy practice that remains with us today. I believe the same can be said of Judge Bostetter in Alexandria and the late Judge Bonney in Tidewater.

For whatever reasons, the number of bankruptcy case filings began to rise after enactment of the 1978 Code, and the bankruptcy trustees were kept busy in the consumer cases. In the early 1980s in the Richmond division there were probably a half dozen chapter 7 trustees and one standing chapter 13 trustee. I enjoyed serving as a chapter 7 trustee, and in 1985 I was also appointed chapter 13 trustee for Richmond. There was always something different in trustee work, and generally, it was casual work in that you could do it whenever there was nothing else much going on.

My most memorable case as a chapter 7 trustee was the involuntary case of Clyde Pitchford, a Richmond stock broker who had embezzled client funds and later served a prison term. When his misdeeds were uncovered, he disappeared from Richmond for several weeks to intense media attention. Mr. Pitchford eventually gave himself up to the FBI and returned. His section 341 meeting was my only one that was initially scheduled to be held in Richmond city jail. The auction of Pitchford’s personal property, held in a basketball arena, received national media attention, and Motley’s Auctions raised nearly $100,000.

**Becoming a Bankruptcy Judge.**

The increased filings of bankruptcy cases placed a strain on the courts, which Congress addressed in 1986 by passing legislation to significantly increase the number of authorized bankruptcy judgeships. Included in the legislation was a fourth judge for the Eastern District of Virginia. As provided in the 1984 Code amendments, bankruptcy judges were to be appointed by the courts of appeals to serve terms of 14 years. This led, in December 1986, to my submitting an application to the Fourth Circuit for appointment to the new position. The process, then as now, was for the court of appeals to appoint a merit selection panel of attorneys and judges to interview applicants and make a recommendation for the position to the court. I went through this process and was fortunate enough to be appointed a bankruptcy judge of the Eastern District of Virginia, effective September 2, 1987.

It was understood by the applicants for this position that the new judge would “swing,” that is, travel and hold court in all four divisions of the Eastern District. The judges agreed that I should be assigned 25 percent of the case filings in each division. Accordingly, for a period of approximately ten years following my appointment, and in addition to my Richmond docket, I traveled to hold court almost every other week in either Alexandria or Norfolk and once a month in Newport News.

During my early years, I traveled with my law clerks to Alexandria by train, leaving Richmond at around 6:30 a.m. on court days. During this period I was late for that court only once. Arriving just before court, we had little time to review the matters on the dockets. In fact, my first ever experience on the bench was in Alexandria, presiding over one of Judge Bostetter’s “monster dockets” of well over one
hundred miscellaneous motions, none of which I had reviewed beforehand. For several hours I faced a full courtroom of stern-faced lawyers who were unknown to me or me to them. I have just one vivid recollection of that experience, aside from the terror of it. On one motion I heard the movant’s argument, and finding his position reasonable, I immediately gave a ruling that the motion was granted. Imagine my surprise and embarrassment when the opposing counsel spoke up and said, “Judge, I wanted to argue my opposition to the motion.” I allowed counsel to make his argument but in the end stood by my original ruling.

I consider my district travel to have been my great good fortune. It was from my experiences in the different courts that I gained confidence in what I was doing and, of course, I became familiar with the regular practitioners in each division. The Bars of each court have their own personalities; collectively they pounded me into a seasoned, and usually fearless, veteran. My travels also gave me the opportunity to interact with all the district’s judges and clerk’s staff. All in all those years were the most educational of my life.

My circuit riding days eventually came to an end in late 1996 after additional judges had been designated for the district. The Norfolk Division was authorized a second judgeship, which Judge David H. Adams filled in 1993. Judge Shelley retired from full-time service in 1994, but he continued to sit in Richmond, taking 25 percent of the docket. In December 1994, Judge Stephen S. Mitchell took over Judge Shelley’s slot, which was moved to Alexandria.

Whether traveling or not, my time on the bench has been busy, challenging, and stimulating - also exciting. Bankruptcy law is an ideal subject for scholarly legal writing, and another satisfying aspect of my work has been the opportunity to write judicial opinions. In general, a judge is able to devote as much time as necessary to an opinion without undue regard for the amount of money involved. West’s Bankruptcy Reporter, now approaching 500 volumes, demonstrates that there has been a proliferation of bankruptcy opinions since enactment of the 1978 Code.

Bankruptcy was a growth industry in the late 20th and early 21st centuries. However, since 2010, there has been a significant reduction of case filings, particularly chapter 7’s. Although it seems likely that we will see a growth of filings in the future, it is possible that BAPCPA has achieved its intended purpose, leading to a permanent lower level of consumer bankruptcies. As a result of the filing slowdown and serious budgetary problems in the Federal government, the bankruptcy courts face an unpredictable future in terms of the services that can be provided to the public.

The docket of the Eastern District bankruptcy court raises countless issues, most of which the judges must address immediately. Cases run the gamut, from asset and no asset chapter 7s, to chapter 13 plans of debtors trying to save their homes or autos, to family farmers (just a few filings in Virginia), to attempted reorganizations of large and small businesses. I have found that most lawyers who practice bankruptcy in the Eastern District are quite professional in their demeanor and skilled at their jobs. Our Bar is also commendably collegial. Most disputes are resolved by agreement, and, if not, litigation is usually not a painful experience.

Of course, there are trials on an endless variety of issues both on complaints in adversary proceedings and in motions practice. Perhaps most common in chapter 7 cases are adversary proceedings brought by creditors against debtors to determine the dischargeability of debt. While some debtors are truly undeserving of discharge, many cases elicit sympathy on both sides of the issue. Education loan debt can be particularly troublesome. Although debtors who owe education loans usually present deserving circumstances, Congress has imposed harsh rules that rarely allow for their discharge. Other common trials are on objections to proofs of claim, objections to confirmation of chapter 13 or 11 plans, and motions for relief from the automatic stay.

Chapter 11 reorganization cases are altogether different from consumer bankruptcies. Actually, a large reorganization case can be less problematic for the judge than other cases because of the skills of lawyers who specialize in reorganizations. My first such case of any size was that of Miller & Rhoads, the venerable Richmond department store chain, founded in 1885, that had been a favorite shopping place of Virginians. The company filed chapter 11 in 1989, and after reorganization failed it became my sad duty to watch it liquidated. Included in the sale of Miller & Rhoads’s assets was the concept of the company’s legendary “real” Santa Claus, who had been visited at Christmas time by generations of Richmond and Virginia chil-

Continued on next page
dren. The “real” Santa Claus was purchased out of bankruptcy by Thalhimer’s Department Store, and he still receives children each holiday season at the Richmond’s Children’s Museum.

Other of my chapter 11 cases included Ryan Homes (N.V.R. L.P.), an Alexandria case that reorganized in the early 1990s and that introduced me to the “sticker shock” of New York lawyer’s fees; another Richmond institution, Best Products Co., which filed in 1996, sold substantially all of its assets the same year and eventually paid its creditors nearly 100 per cent of their claims; and the 2000 case of Heilig-Meyers Company and its subsidiaries, which at one time operated a chain of more than 1,200 furniture stores. In Heilig, I conducted my longest trial, ten days, in an adversary proceeding brought by the debtors against the firms’ principal lenders, to avoid allegedly fraudulent cash transfers and preferences in connection with a critical refinancing of debt. The issuance of my initial Heilig opinion following this trial also caused one of my most embarrassing moments because the opinion contained a mathematical error in the balance sheet calculation that was intended to support my conclusion that the debtor was not insolvent at the time of the refinancing. The error was quickly called to my attention and also reported in the Richmond Times-Dispatch. Fortunately, there was a simple remedy, and we promptly issued a revised opinion.

I have very fond recollections of holding court in all divisions of the Eastern District. I always strived to be conscious of my courtroom demeanor and to maintain my composure and sense of humor. It has been my goal through my own behavior to set an example for others. My interest in this aspect of being a judge has prompted me on a number of occasions to write or speak about best attorney practices in the bankruptcy court. My pet peeves should be well known to the Bar, and I need not repeat them here. Nevertheless, I believe my admonishments of counsel have been relatively benign. Perhaps my most memorable admonishment took place in chambers and did not involve a lawyer; during a recess I told my wife that she was not to chat with trial witnesses in the building elevator. (A tale for another day.) Did I mention that I was fearless?

Now, Retirement.

Returning to my previously expressed concerns about retirement, I make the following observations.

I leave a bench that has been much changed since 1987. Until Judge Shelley’s death in February 2001, the district had two bankruptcy judges in each division. In Norfolk, Stephen C. St. John, now chief judge, replaced Judge Bonney upon his retirement in 1995. (Judge Bonney died in December 2011.) Judge Bostetter retired in 1999 and was replaced by Judge Robert G. Mayer. From February 2001 until September 2006, I was the only judge in Richmond. The 2005 BAPCPA legislation gave the district an additional judge, a position filled in Richmond by Judge Kevin R. Huennekens in 2006. In 2011, Alexandria Judge Stephen S. Mitchell retired and was replaced by Judge Brian F. Kenney. Finally, in Richmond, Keith L. Phillips, a well-qualified bankruptcy attorney and chapter 7 trustee of long experience, has been named by the court of appeals to fill my position.

I have always found my fellow judges in the Eastern (and Western) Districts to be exceptionally skilled, conscientious, and dedicated. They have been my close friends and mentors, and the camaraderie we have shared is without parallel in my life. I should also mention that during the years I have served, the bankruptcy judges have enjoyed most cordial relations with the judges of the district court, who are essentially our bosses.

For my personal staff and law clerks I have tremendous affection, which I hope they know from the enduring friendships we have shared these past years. Jane Nuttall has served faithfully as my judicial assistant throughout my time with the court and also as my paralegal (and chapter 13 assistant) during the previous eleven years. Laurie Ross, my career judicial law clerk, has kept me straight, effectively serving as assistant judge, and courtroom deputy Peggy Rintye-Gibbs has for years efficiently managed the court docket and served as an exceptional spokesperson for the court. Our chambers has stayed in touch with all my former judicial law clerks, and we get together for a lunch once each year, most recently in December 2012.

As for the clerk’s office, much of my satisfaction from serving in the Eastern District has come from the outstanding and always helpful employees of our clerk of court. Because they can be of such great benefit, it is a foolish lawyer indeed who does not treat every

Continued on next page
member of the clerk’s staff with utmost respect and friendship. Our court has always been fortunate in its choice of clerks, and current clerk Bill Redden and his chief deputy Jim Ingold are to be commended for their skilled guidance, particularly during the financial crisis and budget cuts all courts now face.

There is little to add to what I have already said about the members of the Eastern District Bankruptcy Bar who have practiced before me. In my opinion, our lawyers are without equal, both in competence and in collegiality, and they will show our newest judge, Keith Phillips, the way.

In bankruptcy we have thousands of unfortunate debtors, who are the court’s customers. Not all of my days on the bench have been a pleasure. In explaining my work to friends outside the field of law, I often tell them that a downside of my job has been the frequency with which I encounter people suffering from financial difficulties, many severe. This has become particularly true with the devastation of the mortgage market and other financial problems our country has endured beginning in 2008. One of the principal purposes of modern bankruptcy law is to permit the honest but unfortunate debtor to obtain relief from financial difficulties in an honorable manner. While the current law does permit this, it is sometimes less than user friendly and far from perfect. I will always regret the fact that in enacting BAPCPA Congress was somehow persuaded that many if not most debtors were abusing the system by filing bankruptcy unnecessarily and being assisted in doing so by many unethical lawyers. It was just not so. Yet, Congress is unlikely to attempt improvements or to rectify inconsistencies in the Code anytime soon.

Thus it is vitally important that the Code we have be fairly administered to the benefit of all persons or entities who need financial relief.

I have no doubt that despite looming budgetary problems the bankruptcy court and its professionals will continue as conscientious caretakers of this valuable aspect of American government.

(Endnotes)
1. U.S. Bankruptcy Judge, Eastern District of Virginia. Judge Tice was appointed to the bench effective September 2, 1987. He has announced that he will retire from full time service on June 30, 2013.
2. In those days, many young lawyers served as trustees at the beginning of their careers and then moved on to other areas of practice. It was only after the adoption of the 1978 Bankruptcy Code that we have seen the growth of a semi-permanent cadre of chapter 7 trustees. Today, there are few openings for chapter 7 trustee positions, and each new trustee must undergo an FBI background check. However, one thing has remained relatively constant — trustee compensation. In a no asset case, trustees were paid a minimal $15 or $20. As with today, there were not that many substantial asset cases, and trustees often did much work for little compensation. The referee was able to and often did balance a trustee’s good and bad cases by awarding the trustee more compensation in cases where funds were available. For example, if the trustee had recovered several hundred dollars in a case, the referee might award all of that cash to the trustee as compensation. This method of providing trustee compensation in small asset cases was eliminated under section 326(a) of the 1978 Bankruptcy Code, which provided payment to trustees in asset cases on a sliding percentage basis that limited compensation to 25 percent of the first $5,000 of assets distributed to creditors.
Clerk’s Corner  Leaner Times Ahead at the Bankruptcy Court
John W. L. Craig, II • Clerk of Court • Western District of Virginia

The bankruptcy courts are currently facing a budget crisis. Reductions to our funding from Washington along with sequestration cuts, downsizing of our staffing formula, and the continual downturn in filings are the elements that have come into play to cause this perfect storm of funding woes. These factors will force the courts to make drastic cuts in an effort to reduce cost and expenses. The most notable reductions are in the elimination of positions. At least two involuntary separations will take place in the Western District of Virginia before the end of this fiscal year. During the upcoming fiscal year further belt-tightening will take place with double digit furlough days being imposed upon the entire staff. At present we do not anticipate any diminution in service to the bar and public; but unless these trends change that will inevitably follow.

Budget Cuts and Sequestration: The Bankruptcy Court has dealt with cuts to our previous year budgets for the last several years. This past year was no different, however, in addition to the plan cuts, sequestration hit the bankruptcy court particularly hard. Though sequestration was announced as a 2% across-the-board cut to federal programs, by the time it got to the bankruptcy court it became a 34% reduction in allocation in all non-salary categories. Salary categories were reduced by 12%. For fiscal year 2014 we have been told to expect further cuts from this year’s allotment (including the sequestration reduction) of another 5 to 7% and a similar cut is expected for fiscal year 2015.

Adjustments to the Staffing Formula: This year the Administrative Office of United States Courts is examining the current staffing formula of all courts nationwide. Bankruptcy courts will be evaluated as to their on board staffing cost at the end of June this year and a new staffing formula put into place by resetting the formula to this lower base. A portion of the formula will be an across-the-board reduction for what is called the shared administrative services initiative that will further reduce amounts allocated to the courts. This program is designed to encourage further sharing between district and bankruptcy courts. In the Western District we have always had a strong and active sharing of responsibilities and resources between the two courts.

Downturn in Filings: It will not be a surprise to any bankruptcy practitioner that bankruptcy filings are down. In the Western District of Virginia they have fallen approximately 30% in the last three years. As we have entered 2013 that trend appears to have continued. Since the funding of our courts is based, in large part, on the number of cases filed the continuation of this trend bodes poorly for our court. In calendar year 2012 there were 6900 cases filed in the Western District of Virginia, compared to 9595 in 2009 and 13,579 in 2005.

CM/ECF: It is not all bad news for the future. Our automated filing system, CM/ECF, continues to work very well and has recently added a few new features. Some you may notice are:

(1) Two new menu selections appear under the Utilities menu to allow navigation quickly between CM/ECF and PACER. You won’t have to leave your CM/ECF session to access another court in PACER or to use the PACER Case Locator.

(2) The “Create Appeal” option has been modified so you have more flexibility in customizing a docket report. Now you can select only the entries you want and whether you want the PDF document appended to this customized report. Or, if you just want an abbreviated docket report without attached PDF documents, you can select only the entries you need for the task at hand.

(3) The number of pages for documents associated with a docket entry is a new option. Knowing how big a file is helps PACER users predict the cost of viewing an attachment and also to anticipate the loading time of a document.

(4) Additional dates and deadlines now display on the caption of the docket report.
Ever since the enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), the determination of a debtor's Current Monthly Income (CMI) has become an essential part of any Chapter 7 or Chapter 13 case, at least where the debts are primarily consumer in nature. One problem faced by courts since the inception of BAPCPA is calculating CMI when a debtor is married, but the debtor's spouse does not join in the bankruptcy. This article will explore and summarize the cases dealing with this issue as it pertains to Chapter 13 and Chapter 7 bankruptcies.

Section 101(10A)(A) of the Bankruptcy Code defines “currently monthly income” as “the average monthly income from all sources that the debtor receives . . . without regard to whether such income is taxable income,” in the six months preceding the petition date. Section 101(10A)(B) further provides that “[c]urrent monthly income includes any amount paid by any entity other than the debtor . . . on a regular basis for the household expenses of the debtor or the debtor’s dependents . . . .” A plain reading of these two subsections leads one to conclude that a debtor must include the non-filing spouse's income to the extent it is used to pay household expenses of the debtor or of the debtor's dependents on a regular basis.

The drafters of Official Form B22 determined that the best way to determine CMI is to include the non-filing spouse's average gross income over the six months preceding the bankruptcy filing on line 2, and then for a “marital adjustment” to be deducted later on, on lines 13 or 19 in a Chapter 13 (Official Form B22C) and on line 17 in Chapter 7 (Official Form B22A).
This calculation process has led debtors to ask courts two questions. First, is it proper for the “marital adjustment” to be taken by the debtor on line 13 of Form B22C, thus affecting the required length of a Chapter 13 plan? Second, what types of expenses of the non-filing spouse can be included in the “marital adjustment” in Chapters 7 and 13.

WHEN IS THE MARITAL ADJUSTMENT TAKEN IN CHAPTER 13?

Section 1325(b)(2)(B) of the Bankruptcy Code requires that if a Chapter 13 debtor’s plan does not pay all of the unsecured creditors in full, the debtor must pay all of her projected disposable income received in the “applicable commitment period” for their benefit.

Section 1325(b)(4) of the Code governs the length of the applicable commitment period. It provides, in pertinent part:

For purposes of this subsection, the “applicable commitment period”—(A) subject to subparagraph (B), shall be—(i) 3 years; or (ii) not less than 5 years, if the current monthly income of the debtor and the debtor’s spouse combined, when multiplied by 12 is not less than—. . . (II) in the case of a debtor in a household of 2, 3, or 4 individuals, the highest median family income of the applicable State for a family of the same number….

Thus, in general, if the debtor has below median income, the applicable commitment period is three years. If the debtor has above median income, the applicable commitment period is five years.

The issue then becomes whether all of the non-filing spouse’s gross income must be included to determine the debtor’s applicable commitment period, even in cases where a portion of that income will not be contributed to the debtor’s household expenses and not considered a part of the debtor’s disposable income. In other words, can a debtor take a marital adjustment on line 13 in Part II of Form B22C, in which the debtor’s commitment period is calculated, or is the debtor only allowed to take a marital adjustment on line 19 in Part III of Form B22C, in which the debtor’s disposable income is calculated? The answer turns on the meaning of “current monthly income.”

Section 1325(b)(4)(A)(ii) of the Code states that a court should consider the “current monthly income” of the debtor and the debtor’s spouse to determine the applicable commitment period. “Current monthly income” is defined in Section 101(10A) and includes two amounts. First, per Section 101(10A)(A), “current monthly income” includes “the average monthly income from all sources that the debtor receives . . .” As stated by Judge Huennekens in In re Grubbs, a debtor’s spouse has no current monthly income except in a joint case. In a single case, current monthly income applies solely to that income derived by the debtor. The definition of “current monthly income” includes income received by the debtor’s spouse only when the debtor has filed a joint case with his or her spouse. See In re Barnes, No. 07-03263, 2007 WL 4162822, at * 3 (Bankr. D.S.C. Oct. 26, 2007); In re Quarterman, 342 B.R. 647, 650 (Bankr. M.D. Fla. 2006) (“The parenthetical [in 11 U.S.C. § 101(10A)] stating that, in a joint case, a debtor’s current monthly income shall include the debtor’s spouse’s income suggests that, in a single case, the spouse’s income is not included in the debtor’s current monthly income; otherwise, the parenthetical would be superfluous.”). Because the debtor’s spouse has no current monthly income, the applicable commitment period will be based only on the debtor’s current monthly income. 8 Collier on Bankruptcy ¶ 1325.08[5][d] (Lawrence P. King ed., 15th ed. rev 2007).

Thus, with respect to Section 101(10A)(A), “current monthly income” does not include a non-filing spouse’s gross income.

The second part of “current monthly income” is provided by Section 101(10A)(B). This section provides that, in a Chapter 13 case where the debtor is married but his spouse is not filing, the debtor’s “current monthly income” includes any portion of the non-filing spouse’s income that is “paid . . . on a regular basis for the household expenses of the debtor or the debtor’s dependents.” Again Judge Huennekens explains in Grubbs:

Section 101(10A)(B) states that “current
monthly income” “includes any amount paid by any entity other than the debtor (or in a joint case the debtor and the debtor's spouse), on a regular basis for the household expenses of the debtor or the debtor's dependents (and in a joint case the debtor's spouse if not otherwise a dependent) . . . .” Thus, the income that the debtor's spouse contributes to household expenses is part of the debtor's current monthly income under Section 101(10A)(B). Barnes, 2007 WL 4162822, at *3; Quarterman, 342 B.R. at 651 (“. . . [I]n a single case, a debtor's spouse's income shall be included in the debtor's current monthly income to the extent that it is paid ‘on a regular basis for the household expenses of the debtor or the debtor's dependents.’”) (quoting 11 U.S.C.A. § 101(10A)(B) (Pamph. 1 to Supp. 2007)).

Judge Huennekens explains that his interpretation satisfies the rules of statutory construction because it does not make the phrase “and the debtor's spouse in §1325(b)(4)(A)(ii)” mere surplusage, it comports with the policies of the Bankruptcy Code, and does not conflict with the instructions for Form B22C line 13. Consequently, the Court ruled in In Re Grubbs that it was proper for the Debtor to take the marital adjustment on line 13 of Official Form B22C, and confirmed a plan with a three year commitment period.

This interpretation is the majority opinion of the courts that have ruled on the issue. However, there are also courts that have ruled that a marital adjustment is not allowed on line 13 in determining the debtor's commitment period.

WHAT EXPENSES CAN BE INCLUDED IN THE MARITAL ADJUSTMENT

Per Section 101(10A)(B), “current monthly income” “includes any amount paid by any entity other than the debtor . . . on a regular basis for the household expenses of the debtor or the debtor's dependents . . . .” The term “any entity other than the debtor” refers to the non-filing spouse. Thus, if a debtor is claiming a marital adjustment on Form B22, the debtor is asserting that some portion of the spouse’s income is not being used for these purposes.

Unfortunately, the term “household expenses” is not defined in the Bankruptcy Code. Nevertheless, a household is ordinarily defined as a family living together or a group of people who dwell under the same roof; and an expense is defined as an expenditure of money. As a way of offering guidance, one Court gave a non-exclusive list of factors to be considered when trying to determine the validity of a marital adjustment on Form B22. The list includes:

1. The particular history behind the non-filed spouse's refusal to contribute all income to the household. (i.e., is it based upon legal or financial advice at a time bankruptcy of the debtor was in prospect (which would not be supportive of such deduction)?)
2. What are the specific facts as to the marital relationship and the debts to be discharged under the plan?
3. Were the debts incurred solely by the debtor, and before the marriage?
4. What is the nature of the debts to be discharged and the benefits received in exchange for the debt?
5. Is the non-filing spouse legally obligated to repay debts and thus will benefit by plan payments reducing that co-liability?
6. Were goods or services received in exchange for the indebtedness which receipt benefitted the non-filing spouse?

In reviewing court opinions discussing the marital adjustment, a few things become clear. First, the non-filing spouse's income must be included in Part I (lines 2-9) of Form B22C. Second, a party opposing a marital adjustment cannot circumvent the allowance of the deduction based upon a “totality of the circumstances” argument under Section 707(b)(3). Third, a debtor may not take a marital adjustment for an expense that is included somewhere later in Form B22C. In other words, a debtor cannot “double-dip.” Fourth, a debtor may deduct the non-filing spouse's withholding taxes. Fifth, a debtor may deduct the non-filing spouses prior support obligations.

After consideration of the above list of permissible bases for adjustment, the answers become a bit less clear cut. For example, several courts have faced the issue of whether or not the payments made by a

Continued on next page
non-filing spouse on real estate solely owned and financed in the non-filing spouse’s name are valid marital adjustments. There are two lines of opinions on this question.

The first line of cases has adopted a payment “for the benefit of” the debtor approach. Courts applying this household centric approach hold the mortgage payments must be included in the debtor’s current monthly income (that is, not taken as a marital adjustment) because the payments benefit the debtor. “The second line of cases . . . adopt a debtor centric approach and hold such mortgage payments may be excluded from the debtor’s current monthly income because the debtor does not possess any ownership interest in the home and is not liable on the mortgages which encumber the home.”

Cases involving vehicles driven by, titled in and financed in the name of the non-filing spouse are not as problematic. In these cases, courts generally hold that the payments for such vehicles constitute a valid marital adjustment. The courts’ conclusions do change, however, if there is some benefit to the debtor or debtor’s dependent from the vehicle or the debt tied to the vehicle.

Other expenses that have been ruled to be valid marital adjustments include: (1) non-filing spouse’s gym membership; (2) non-filing spouse’s recreational expenses (e.g., lunches out, movies and health club membership), loan repayment to non-filing spouse’s parents, payments to help support adult child; (3) clothing and personal items for non-filing spouse’s child from a prior marriage; (4) payments of student loans of non-filing spouse’s child from a prior marriage; (5) non-filing spouse’s cigarette expenses; (6) payments by non-filing spouse to keep up appearance of former residence owned by debtor and non-filing spouse in the hopes that it would sell; (7) payments for non-filing spouse’s 401k loan for which the proceeds were used on improvements of home solely owned by non-filing spouse; (8) household expenses paid by non-filing spouse when house and loan not in debtor’s name; (9) 401k deduction and 401k loan from non-filing spouse’s paycheck; (10) hunting cabin owned and used solely by non-filing spouse; (11) college tuition and car payment for adult child since law unclear if adult child can be a dependent; (12) credit card payments where charges were for items not for household use of debtor or debtor’s dependents; and (13) expenses for non-filing spouse’s clothes and personal items.

Expenses deemed by courts not to be valid marital adjustments include: (1) college 529 plan payments by non-filing spouse for the benefit of debtor’s daughter; (2) payment by non-filing spouse for heating the swimming pool used by debtor and her son; (3) payment for food and utilities; (4) non-filing spouses’s payments for hay for debtor’s horse; (5) debtor’s portion (50%) of health insurance premium paid for by non-filing spouse by wage deduction from non-filing spouse’s paycheck; (6) household utilities (e.g. electric, gas, water, sewer, television) were not brought into the marriage by the non-filing spouse and are not valid marital adjustments; (7) college expenses and college student’s car loan payments are household expenses of debtor’s dependent even though college student is over 18 years of age because a dependent is someone sustained by another or someone that relies upon the support of another; (8) Dell personal computer is a household expense absent showing that it is not used for household benefit by debtor or debtor’s dependents; (9) signature loan used by non-filing spouse to pay for car repairs and refinace credit card debt; (10) car title loan used to pay credit card debts for food, apparel and personal incidental expenses; (11) high school and college tuition for debtor’s children that is the sole responsibility of non-filing spouse and paid from his sole bank account; (12) orthodontic care of debtor’s minor child; and (13) expenses for non-filing spouse’s food and for utilities.

As is evident by the above list of items that can be valid marital adjustments and those that cannot, the courts’ rulings turn on the specific facts in each case. Therefore, for a lawyer to prevail in a hearing on this issue she will have to put on evidence and carry the burden of proof. In terms of actual practice, at the outset, it is up to the debtor to claim the marital adjustment with sufficient specificity to satisfy the court. After that, the burden shifts to the party opposing the marital adjustment to put on sufficient evidence to show that the debtor is not applying all of his disposable income to the plan payments. Once that burden is satisfied, the burden of proof shifts back to the debtor to demonstrate compliance with Section 1325(b). Consequently, failure to present sufficient evidence supporting the debtor’s position can be fatal.

Continued on next page
and leave the court with no choice but to rule in favor of the party opposing the marital adjustment.

In conclusion, as with all factual issues in bankruptcy law, it is imperative for the debtor's attorney to look behind the transaction to see what is really going on with the alleged “marital adjustment” in order to determine whether or not it is valid. And, once the attorney is satisfied that the “marital adjustment” is proper, he must be prepared to put on evidence sufficient to convince the court of the same.

(Endnotes)
1. Mr. Slayton is a Member of the firm Boyle Bain Reback & Slayton with offices in Charlottesville, Culpeper, and Harrisonburg.
3. Id.
5. Id. at *3.
6. Id. at *3-4.
7. Id. at *5.
11. Id.
17. See, In re Osmond, Case No. 10-10211 (Bankr. Vt. 5/10/2010).
21. See, in re Schroeder, Case No. 11-32962 (Bankr. D. Minn. 8/1/2012)(debtor was not allowed to take a marital adjustment for the vehicle payments made by her non-filing spouse because she was on the title to the vehicle); In re Vollen, 426 B.R. 359 (Bankr. D. Kan. 2010)(car payments made by non-filing spouse for debtor's daughter at college are not valid marital adjustments, and car title loans taken to pay household expenses like food, apparel and personal incidentals are household expenses and not valid marital adjustments); In re Sances, Case No. 01138 (Bankr. E.D. N.C. 12/15/2009)(vehicle payment by non-filing spouse for vehicle driven by debtor is not a valid marital adjustment); and In re Toxward, 485 B.R. 423 (Bankr. D. Co. 2013)(payments by non-filing spouse for Jeep jointly owned with debtor only allowed for a marital adjustment of 50% of the payment amount).
29. Id.
31. In re Schroeder, Case No. 11-32962 (Bankr. D. Minn. 8/1/2012).
32. Id.
34. In re Schroeder, Case No. 11-32962 (Bankr. D. Minn. 8/1/2012).
39. Id.
40. Id.
42. Id.
43. Id.
44. Id.
46. In re Schroeder, Case No. 11-32962 (Bankr. D. Minn. 8/1/2012).
47. Id.
49. In re Burke, Case No. 07-62311 (Bankr. N.D. Ohio, July 21, 2008).
Case Summaries
By Sarah Boehm

Recent Circuit Court Decisions

Branigan v. Davis (In re Davis), No. 12-1184, 2013 U.S. App. LEXIS 9535 (4th Cir. May 10, 2013)

Residential Junior Lien Stripping in “Chapter 20” Cases

Background: Chapter 7 debtors received discharges and subsequently filed chapter 13 cases (called “chapter 20” cases when they follow chapter 7 cases) in which they sought to strip off valueless liens on their principal residences. Both the Bankruptcy Court and the District Court held that these chapter 20 debtors could strip off completely valueless liens on their principal residences. The Bankruptcy Court and the District Court held that these chapter 20 debtors could strip off completely valueless liens on their principal residences. The Bankruptcy Court and the District Court held that these chapter 20 debtors could strip off completely valueless liens on their principal residences. The Bankruptcy Court and the District Court held that these chapter 20 debtors could strip off completely valueless liens on their principal residences. The Bankruptcy Court and the District Court held that these chapter 20 debtors could strip off completely valueless liens on their principal residences. However, the Fourth Circuit was careful to point out that “bankruptcy courts are bound to carefully scrutinize filings for good faith and dismiss cases where the debtor attempts to use a Chapter 20 procedure solely to strip off a lien. . . . [C]reditors are also protected by section 349(b)(1)(C), which provides that a lien springs back if the case is dismissed.” Id. at * 20.

Holding: On appeal, the Fourth Circuit affirmed the Bankruptcy and District Courts and first explained that lien stripping in a typical chapter 13 case is undoubtedly permissible—“section 506(a), which classifies valueless liens as unsecured claims, operates with section 1322(b)(2) to permit a bankruptcy court, in a Chapter 13 case, to strip off a lien against a primary residence with no value.” 2013 U.S. App. LEXIS 9535, at *11. This general rule is subject to the Supreme Court’s limitation in Nobelman v. Am. Sav. Bank, 508 U.S. 324 (1993), holding that chapter 13 debtors cannot strip down a partially secured claim secured by a debtor’s principal residence under section 1322(b) because such claims are still “secured” claims. Next, the Fourth Circuit pointed to its own prior precedent holding that “[n]otwithstanding the bar on discharges imposed by BAPCPA, we have held that a debtor may still take advantage of the protections offered by Chapter 13 short of a discharge.” Id. at * 12 (citing Branigan v. Bateman (In re Bateman), 515 F.3d 272, 283 (4th Cir. 2008)). Thus, the Fourth Circuit concluded that, because claims secured by valueless liens are considered to be unsecured claims under section 506(a), section 1322(b) permits a chapter 20 debtor to strip off a valueless junior lien on a primary residence. However, the Fourth Circuit was careful to point out that “bankruptcy courts are bound to carefully scrutinize filings for good faith and dismiss cases where the debtor attempts to use a Chapter 20 procedure solely to strip off a lien. . . . [C]reditors are also protected by section 349(b)(1)(C), which provides that a lien springs back if the case is dismissed.” Id. at * 20.


Chapter 7 Trustee Conflicts of Interest

Background: A partnership filed a single-asset real estate chapter 7 case, and a few months later, the chapter 7 trustee filed a motion to sell the debtor’s primary asset—130 acres of land in Charles Town, West Virginia. The debtor’s general partner tried to thwart the sale by first obtaining a six-month extension of time during which the trustee would further market the property and then unsuccessfully seeking dismissal of the bankruptcy case. During the marketing period, the Bankruptcy Court approved the employment of the trustee’s own law firm as special counsel to the trustee. The trustee’s law firm also had been engaged by a bank to collect from the general partner on an unpaid personal loan, unrelated to the chapter 7 case of the general partnership. The general partner did not object to the employment of the law firm as special counsel to the trustee in the bankruptcy case. The property was sold at an auction for $3 million and approved by the Bankruptcy Court, with no objection from the debtor or the general partner. The sale generated an approximately $1.87 million distribution to partners after payment of all claims. Nonetheless, the general partner filed a motion to remove the trustee based on an alleged conflict of interest arising from the trustee’s law firm’s representation of both the trustee and the bank in the unrelated collection action directly against the
general partner. The Bankruptcy Court denied that motion, and the general partner subsequently dismissed his appeal in the district court before a ruling. Next, the general partner filed a motion to invalidate the sale, arguing that the trustee was not disinterested as required by section 372(a) and had violated his fiduciary duties by selling the property for an inadequate price. The Bankruptcy Court also denied this motion, and the District Court affirmed.

**Holding:** On appeal in the Fourth Circuit, the general partner limited his challenge to the Bankruptcy Court's finding of fact that no actual conflict of interest existed. The Fourth Circuit made short shrift of this argument and pointed out that “[a]t the most basic level, the separate debt collection proceeding was against [the general partner] as an individual, while the bankruptcy proceedings dealt with the property of the partnership—an unrelated matter.” 2013 U.S. App. LEXIS 7316, at *17–18. Therefore, the trustee's law firm's representation in the debt collection action was not materially adverse to the partnership’s bankruptcy estate.

**Campbell v. The Hanover Ins. Co. (In re ESA Environmental Specialists, Inc.), 709 F.3d 388 (4th Cir. March 1, 2013)**

**Earmarking Defense to Preference Actions**

**Background:** The debtor was a government contractor in environmental and industrial engineering and as such was required to furnish surety bonds to secure performance and payment of subcontractors. An insurance company issued surety bonds to secure performance on eight government contracts, but prepetition the debtor required additional capital for new government contracts and obtained $12.2 million from a lender and new surety bonds from the insurance company. However, concerned about the debtor’s financial condition, the insurance company required the debtor to obtain a $1.375 million letter of credit from a bank with the insurance company as the beneficiary. In turn, the bank required the debtor to fund a $1.375 million certificate of deposit as security for the letter of credit. Lacking cash for the certificate of deposit, the debtor borrowed the funds from the lender and transferred them to the bank to fund the certificate of deposit. The bank then issued the letter of credit, and the insurance company issued the new bonds. The debtor filed its chapter 11 case shortly thereafter, and the insurance company drew on the letter of credit and the bank liquidated the certificate of deposit. After the debtor’s assets were sold, the case converted to a chapter 7 case and the trustee filed a preference action against the insurance company as an indirect beneficiary of the debtor's transfer of the loan proceeds that funded the $1.375 million certificate of deposit. The insurance company asserted two defenses—earmarking and new value. The Bankruptcy Court granted summary judgment in the insurance company’s favor and concluded that both defenses precluded recovery by the trustee. The District Court affirmed.

**Holding:** On appeal, the Fourth Circuit affirmed the overall holding that the insurance company was entitled to summary judgment, but the Fourth Circuit disagreed that the earmarking defense applied. The Fourth Circuit explained that “the earmarking defense applies when a third person makes a loan to a debtor specifically to enable that debtor to satisfy the claim of a designated creditor.” 709 F.3d at 395 (citation and quotation omitted). In this case, the Fourth Circuit concluded that the earmarking defense did not apply for the simple reason that the funds were not used to pay an antecedent debt. Id. at 396. “Here, [the debtor] borrowed money from [the lender]—incurring new debt—and used those funds to collateralize both existing obligations to [the insurance company] as well as the New Bonds—a new debt not previously owed to any creditor.” Id. at 397. On the new value defense, the Fourth Circuit held that the new government contracts (in and of themselves, not the future revenue to be obtained from such contracts) that the debtor was able to obtain as a result of the $1.375 million transfer constituted new value in excess of the transferred amount. See id. at 399–400.

**Recent District Court Decisions**


**Standing; Judicial Estoppel**

**Background:** Defendant moved to dismiss plaintiff’s employment discrimination suit for lack of standing and failure to state a claim. Plaintiff, the debtor in a
pending chapter 13 bankruptcy case, had failed to schedule the suit—the basis of which arose prepetition—in his bankruptcy schedules. Therefore, defendant argued that only the chapter 13 trustee had standing to bring the action and further argued that plaintiff’s non-disclosure of the suit on his bankruptcy schedules allowed the District Court to apply the doctrine of judicial estoppel.

**Holding:** The District Court found that defendant’s standing argument ignored basic differences between chapter 7 and chapter 13 bankruptcy proceedings because in a chapter 13 case, unlike a chapter 7 case, the debtor remains in possession of the property of the estate. Therefore, the debtor had standing to bring the suit. The District Court further found that plaintiff’s status as a debtor in possession did not hinge on the accuracy of his prior disclosures on his personal property schedule. The District Court also noted that its conclusion was supported by Fed. R. Bankr. P. 6009, which states: “With or without court approval, the trustee or debtor in possession may enter an appearance and defend any pending action or proceeding by or against the debtor, or commence and prosecute any action or proceeding in behalf of the estate before any tribunal.”

The District Court also found that it could not apply judicial estoppel because the Bankruptcy Court had not accepted the position plaintiff took in his bankruptcy schedules (i.e., that he did not have a claim against defendant). In the Fourth Circuit, judicial estoppel can only be applied where four factors are met: (1) the party to be estopped must be advancing an assertion that is inconsistent with a position taken during previous litigation; (2) the position must be one of fact instead of law; (3) the prior position must have been accepted by the court in the first proceeding; and (4) the party to be estopped must have acted intentionally, not inadvertently. See *King v. Herbert J. Thomas Mem’l Hosp.*, 159 F.3d 192, 196 (4th Cir. 1998). While the District Court noted that the first two prongs were easily met, the third prong could not be met because the debtor’s bankruptcy proceeding remained open—”‘acceptance’ in this context means that bankruptcy court has not merely confirmed the debtor’s bankruptcy plan but has also taken the ultimate step of granting the debtor relief (i.e., discharge or repayment).”

**Najafian v. Education Credit Mgmt. Corp.,** 2013 U.S. Dist. LEXIS 50040 (E.D. Va. April 5, 2013) (Judge Trenga)

11 U.S.C. § 523(a)(8) – Discharge of Student Loan Debt

**Background:** The debtor, 65 years old, unmarried, with no dependents, had taken out multiple student loans to finance her education; had acquired multiple degrees, including an M.D. and master’s degree in special education; and worked as an ophthalmologist until 2006. Debtor sought discharge of her student loan debt pursuant to 11 U.S.C. § 523(a)(8). The Bankruptcy Court found that the debtor had not met all three requirements announced in *Brunner v. N.Y. State Higher Education Serv. Corp.*, 831 F.2d 395, 396 (2d Cir. 1987) (the “*Brunner* test”). The debtor appealed the Bankruptcy Court’s decision.

**Holding:** The *Brunner* test requires a court to find: (1) that the debtor cannot maintain, based on current income and expenses, a “minimal” standard of living for herself and her dependents, if forced to repay the loans; (2) that additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and (3) that the debtor has made good faith efforts to repay the loans. The District Court agreed with the Bankruptcy Court’s finding that the first *Brunner* element had been met: the record showed the debtor was “unemployed, homeless, living out of her car, sleeps in public parking lots, and relies on public restroom facilities for her personal needs” and, therefore, unable to maintain a minimal standard of living. *Id.* at *8-9.

The District Court further agreed with the Bankruptcy Court that the debtor could not meet the second element of the *Brunner* test due to her decision to limit her search for employment to the field of ophthalmology. Finally, the District Court agreed with the Bankruptcy Court that debtor’s refusal to participate in one of two loan repayment programs that would have allowed debtor to make payments of $0 per month based on her adjusted gross income or discretionary income demonstrated was “objectively unreasonable.” “This refusal, together with her unwillingness to obtain a job other than as an ophthalmologist, led the Bankruptcy Court to find lack of good faith on her part to repay the loans or consider an alternative.” *Id.* at *15.
Bankruptcy Law News


11 U.S.C. § 524(e) – Nondebtor releases

Background: The debtor appealed the Bankruptcy Court’s decision disallowing certain nondebtor release provisions and severing them from the order confirming the debtor’s plan of reorganization. The case was before the Bankruptcy Court on remand from the Fourth Circuit. The Bankruptcy Court had originally approved the nondebtor release provisions; however, on appeal, the Fourth Circuit found that the Bankruptcy Court’s factual findings were insufficient to determine whether the release provisions should have been approved and “commended” to the Bankruptcy Court the factors outlined in Class Five Nev. Claimants v. Dow Corning (Dow Corning), 280 F.3d 648 (6th Cir. 2002) and In re Railworks Corp, 345 B.R. 529, 536 (Bankr. D. Md. 2006).

On remand, the Bankruptcy Court held a status conference and gave the parties the option of introducing new evidence at a supplemental confirmation hearing; however, the parties declined. After application of the Dow Corning and Railworks factors, the Bankruptcy Court determined that the record did not support including in the reorganization plan the nondebtor release provisions or the corresponding injunction and severed those provisions from the confirmation order.

On appeal to the District Court, the debtor argued that (1) the Bankruptcy Court overstepped the mandate of the Fourth Circuit when it concluded, contrary to its original decision, that the releases were not warranted; (2) that the Bankruptcy Court erroneously concluded that the rejected releases were not essential to the debtor’s reorganizations because—absent the release provisions—the debtor’s indemnification obligations would cause the reorganized debtor to fail and the directors and officers would have refused to serve if the release provisions were severed; and (3) that the Bankruptcy Court had misapplied the Dow Corning and Railworks factors.

Holding: The District Court dismissed each of the debtor’s arguments in turn and affirmed the Bankruptcy Court’s decision. First, the District Court found that the Fourth Circuit’s mandate obligated the Bankruptcy Court “to review the record and articulate, if it could, why the extraordinary and ‘dramatic measure’ of nondebtor release provisions was warranted based on this record.” Id. at *16-20. After review of the record, the Bankruptcy Court “acted in the only way it could . . . —it disallowed those provisions and severed them from the Reorganization Plan.” Id. at *19.

Second, the District Court found “no evidence in the record that [the debtor’s] officers and directors are facing or would, in fact, face claims that would trigger indemnification obligations on the part of [the debtor] so onerous as to threaten the prospects of a successful reorganization.” Id. at *24. Rather, the only evidence was the number of individuals who theoretically might bring claims. The District Court found that more information on the actual amount and nature of potential claims was necessary in order to find the nondebtor release provisions to be “essential” to successful reorganization.

Finally, the District Court found that the Bankruptcy Court had correctly applied the Dow Corning and Railworks factors. Specifically, the Bankruptcy Court found that an unenforceable promise for future services by the directors and officers did not qualify as a “significant contribution” to the reorganization; that, while the only “impaired” class under the plan voted to approve the plan, the impacted class—the Donor class—did not vote in favor of the plan; that the plan did not provide any mechanism for the payment of the Donor claims, which were the claims affected by the release provisions; and that the plan did not provide any opportunity for the Donors to recover. The Bankruptcy Court found that the only factor in favor of the release provisions—the potential for an obligation to indemnify the officers and directors—could not by itself justify the release provisions.

Recent Bankruptcy Court Decisions

In re Chong, 2013 Bankr. LEXIS 1772 (Bankr. E.D. Va. May 1, 2013) (Judge Kenney)

11 U.S.C. § 521(a)(4) – Abandonment of assets; Automatic stay

Background: Before filing a voluntary chapter 7 petition, the debtor had purchased a dry cleaning
business. The previous owner assigned the commercial property lease and sold the business assets to the debtor for a security interest in said property. The debtor thereafter filed an individual petition and indicated that he intended to surrender the property securing the debt to the original owner. The debtor stopped making rent payments once he filed the chapter 7 petition. The lessor, as owner of the commercial property, moved for relief from the stay, which was granted. The lessor entered the premises on the same day the order was entered and ordered the debtor to vacate the premises. The remaining clothing was distributed to the customers without charge. The debtor filed a motion for contempt seeking damages arising from the lessor’s actions, arguing that the property owner did not wait the requisite days as required by Fed. R. Bankr. P. 4001(a)(3).

Holding: The Court held that the debtor lacked standing because under 11 U.S.C. § 524(a)(4) he was required to turn over possession of the premises as leaseholder upon filing his petition. The Court looked to a number of cases involving frozen bank accounts to ascertain whether the debtor had standing to argue a violation of the automatic stay. The Court determined that he did not because ownership of the property had vested in the chapter 7 trustee and the debtor could not be an “injured individual.” In addition, the debtor indicated an intent to surrender his right to remain on the premises, and the trustee retained the possessory interest in the leased premises since the lease had not yet been rejected.

Plan Injunction; Barton Doctrine

Background: A single chapter 11 plan was approved for LandAmerica Financial Group (“LFG”) and multiple affiliates, including LandAmerica Credit Services, Inc. (“LACS”). The plan resolved intercompany claims and established trusts into which the debtors’ assets were placed for liquidation. A single trustee was appointed to administer the plan for both LFG and LACS (the “Trustee”). The plan contained a provision giving the Bankruptcy Court jurisdiction over implementation of the plan as well as an injunction against claimholders from interfering with consummation of the plan. Finally, the plan acknowledged and resolved intercompany claims by treating them as general unsecured claims.

Experian Information Solutions, Inc. (“Experian”) filed a claim in the bankruptcy case, but also filed an action in the U.S. District Court for the Northern District of Illinois against the Trustee based on alleged conflicts of interest for the dual representation of LFG and LACS and breaches of fiduciary duty for not seeking to subordinate affiliate claims. The Trustee responded by requesting the Court to enforce the injunction and jurisdictional provisions of the plan and to impose sanctions.

Holding: The Court held that the Illinois action was barred due to the Barton doctrine and the provisions of the chapter 11 plan. The Barton doctrine bars a party from bringing suit against a court-appointed receiver without first obtaining leave of the appointing court. See Barton v. Barbour, 104 U.S. 126, 128 (1881). Failure to obtain leave of the appointing court deprives the other forum of subject-matter jurisdiction. The Court noted that the Barton doctrine is properly enforced by the appointing court as well. Finally, Experian’s argument that the Trustee’s improper acts were outside the scope of his duties, and thus beyond the protection of the Barton doctrine, was not well-founded, since the duties undertaken by the trustee were directed by the plan itself.

The Court also barred the Illinois action under the provisions of the chapter 11 plan. The Court’s retention of jurisdiction was proper and it had the authority to interpret its own orders. Moreover, the plan contained an express injunction against claimholders, which included Experian, from interfering with the implementation of the plan. Finally, the actions Experian alleged that the trustee failed to take—equitable subordination of affiliate claims and pursuit of these affiliate claims—were already covered by the plan terms. Because Experian failed to make these objections during plan confirmation, it was barred from doing so thereafter.

Non-dischargeability of student loan debt; Motion for Reconsideration; Motion to Amend; Motion for New Trial

Background: A pro se chapter 7 debtor sought to discharge her student loan debt under 11 U.S.C. § 523(a)(8) arguing that it would impose an undue hardship. The debtor was making payments of zero dollars a month towards repayment of the student loan debt under a federal program that calculated reduced payments based on income. The Bankruptcy Court dismissed the debtor’s complaint for dischargeability, prompting her to file motions for reconsideration, to amend the findings, and for a new trial. In her motion for reconsideration, the debtor challenged the Bankruptcy Court’s application of the Brunner test for determining dischargeability of student debt as violations of equal protection and due process. The debtor also argued against the Bankruptcy Court’s application of the Brunner test by alleging that it conflicted with applicable case law. In the motion to amend under Fed. R. Bankr. P. 7052, the debtor sought to modify certain factual findings in the Bankruptcy Court’s earlier opinion. Finally, in her motion for a new trial, the debtor sought to introduce medical and mental health evidence.

Holding: The Bankruptcy Court denied all of the debtor’s motions. The Court upheld its earlier application of the Brunner test (from Brunner v. New York State Higher Educ. Servs. Corp., 831 F.2d 395, 396 (2d Cir. 1987)), in which the first prong asks whether a debtor can maintain a minimal standard of living based on current income and expenses if required to repay the student loan. The Court had previously found that the debtor did not meet this first prong, in part because she made no actual payments on the student loan debt. The Court was not persuaded by the debtor’s equal protection and due process claims, nor her citations to case law, since the first prong of the Brunner test requires that the Court look at the debtor’s current circumstances. The Court next denied the motion to amend, pointing out that the debtor provided no additional evidence or that the requested amendment would be immaterial. Finally, the Court denied the motion for a new trial since the evidence that the debtor sought to introduce did not meet the stringent requirements for newly discovered evidence.


11 U.S.C. §§ 506(a) and 1325(a) – Validity, Priority, or Extent of Lien

Background: Chapter 13 debtors initiated an adversary proceeding under 11 U.S.C. § 506(a) seeking a determination that junior lien encumbering debtors’ primary residence (“Property”) was wholly unsecured and, therefore, could be stripped off, pursuant to 11 U.S.C. § 1325(a), upon completion of the debtors’ confirmed chapter 13 plan. Junior lienholder, SunTrust Bank (“SunTrust”), filed an answer disputing the debtors’ Property valuation, and requesting that the Court deny the relief sought by the Debtors in their complaint (“Complaint”).

Holding: The Court denied the debtors’ Complaint. In order to be successful in a lien avoidance action, the plaintiff must establish that the lien at issue is wholly unsecured. The Court concluded, therefore, that the ultimate question was whether the debtors’ Property was worth more than the value of the senior lien at the time of the petition. To answer that question, the Court stated that it was first required to determine which party had the burden of proof. The burden of proof in lien avoidance actions, which contemplate several Bankruptcy Code provisions, is not defined by statute. By considering the underlying economic motivations of the parties, the Court concluded that, in an action to strip a lien from a debtor’s primary residence, a chapter 13 debtor bears the burden to prove, by a preponderance of evidence, that he is entitled to relief.

Applying this standard, the Court held that the debtors failed to carry their requisite burden. The real estate appraisal prepared by the debtors’ valuation expert relied on “Real Estate Owned” (“REO”) properties: real estate owned by a lender either after an unsuccessful foreclosure auction or through a deed in lieu thereof. The Court held that to adopt the debtors’ Property valuation would require the Court to ignore the inherent limitations of utilizing REO comparables. In addition, the Court found that adopting the debtors’ Property valuation would require the Court to ignore the...
appraisal prepared by SunTrust’s valuation expert, which did not rely on downward adjustments for deferred maintenance expenses.


**Case dismissal; 11 U.S.C. § 109(h) – Temporary waiver of credit counseling; 11 U.S.C. § 362(c)**

**Background:** A chapter 13 debtor requested an extension of time in which to complete the mandatory credit counseling. The debtor or his wife had filed 4 bankruptcy petitions in the previous 22 months, and the debtor filed the instant petition because of a foreclosure sale scheduled the day after he filed the petition. The house was valued below the amount due to the holder of the first deed of trust and the debtor had little income. The debtor obtained credit counseling in one of the previous cases but had not obtained credit counseling before the present bankruptcy petition. The debtor did not appear at the hearing date for the extension of time to complete the credit counseling, and the Court denied the request. The debtor thereafter filed a motion for reconsideration, but had not obtained credit counseling, nor filed any schedules, or a chapter 13 plan.

**Holding:** The Court denied the motion for reconsideration. The Court has the ability under 11 U.S.C. § 109(h) to temporarily waive the credit counseling requirement where there are exigent circumstances, which in turn requires (1) an immediate need to file bankruptcy and (2) an inability to obtain credit counseling before filing. The Court found that the debtor was well aware of the credit counseling requirement as well as the pending foreclosure on his residence, and had still failed to acquire the necessary credit counseling. Moreover, there was no equity in the property, the sole creditor was the lender secured by this property, and there was insufficient income to support a chapter 13 plan much less service and cure the mortgage. The Court denied the motion without prejudice, however, relying on the protections in 11 U.S.C. § 362(c) to protect the secured lender should the debtor or his wife file another bankruptcy petition.


**11 U.S.C. §§ 362(c)(3) and 707(b)**

**Background:** Chapter 7 debtor, whose previously confirmed chapter 13 case was dismissed within the preceding one year period, filed a motion to extend the automatic stay pursuant to 11 U.S.C. § 362(c)(3). Creditor, who filed a petitition breach of contract action against the debtor arising out of a failed commercial real estate transaction, sought dismissal of the debtor’s chapter 7 case for abuse pursuant to 11 U.S.C. § 707(b) (“Motion to Dismiss”).

**Holding:** The Court granted the Motion to Dismiss. The Court concluded that dismissal pursuant to 11 U.S.C. § 707(b) was not appropriate. Section 707(b)(1) of the Bankruptcy Code authorizes bankruptcy courts to dismiss a case under chapter 7 filed by an individual whose debts are primarily consumer debts. The Court concluded that dismissal of the Case under section 707(b)(1) was not warranted, as the debtor’s debts—which consisted largely of secured and unsecured commercial loan obligations related to investment properties—were not “primarily consumer” in nature.

Nevertheless, the Court concluded that dismissal was authorized under 11 U.S.C. § 707(a). Section 707(a) of the Bankruptcy Code permits bankruptcy courts to dismiss a case under chapter 7 for “cause.” The Bankruptcy Code does not limit the circumstances justifying dismissal for “cause” pursuant to section 707(a). In determining whether “cause” exists, bankruptcy courts within the Fourth Circuit, consider: (1) whether the bankruptcy petition was filed because of sudden illness, calamity, disability or unemployment; (2) whether the debtor incurred cash advanced and made consumer purchases far in excess of his ability to repay; (3) whether the debtor’s proposed family budget is excessive or unreasonable; (4) whether the debtor’s schedules and statement of current income and expenses reasonably and accurately reflect the true financial condition; and (5) whether the petition was filed in good faith. Green v. Staples (In re Green), 934 F.2d 568 (4th Cir. 1991). Applying the factors identified in Green, the Court concluded that “cause” for dismissal was present, as the debtor: (1) materially understated his monthly income on his bankruptcy schedules; (2) converted non exempt assets during the one month interval between his chapter 13 and 7 cases to non-exempt
asset improvements; and (3) utilized disposable income available during his chapter 13 case for family vacations.

In light of its decision to grant the Motion to Dismiss, the Court concluded that the motion to extend the automatic stay was moot.


11 U.S.C. § 547; Lis pendens; Equitable reformation

**Background:** Before filing a chapter 7 petition, the debtor purchased real property through a loan secured by the property. The debtor then refinanced the loan with EVB and also acquired capital to develop the property through his construction business. The loans were to be secured by the debtor’s real property, but the construction deed of trust was erroneously executed by the debtor’s business instead of the debtor and was therefore invalid. An unrelated third party thereafter obtained judgment against the debtor and properly recorded the judgment. A lawsuit was filed in state court for EVB seeking to reform the construction deed of trust and gain priority. A *lis pendens* also was filed. The debtor filed a chapter 7 petition within 90 days of the *lis pendens*, and the matters were removed to the Bankruptcy Court. The chapter 7 trustee sought to avoid any preferential transfer of property under 11 U.S.C. § 547, including the *lis pendens*, and any unperfected lien under 11 U.S.C. § 544, and also sought recovery under 11 U.S.C. § 550.

**Holding:** The Court permitted the chapter 7 trustee to avoid the *lis pendens* under section 547 and sell the property under section 550. Relying heavily on *Wells Fargo Funding v. Gold*, 432 B.R. 216 (E.D. Va. 2009), the Court found that a *lis pendens* would provide the trustee with constructive notice sufficient to defeat the trustee’s power under section 544. Nevertheless, that case held that because any lien interest acquired as a result of the current litigation would relate back to the date that the *lis pendens* was filed, any such interest is avoidable because the *lis pendens* was filed within the 90-day preference window. Although a *lis pendens* merely provides notice of a pending lawsuit, it also allows a creditor to acquire an interest superior to that of a hypothetical future bona fide purchaser, which suffices under section 547. Thus while the Gold court recognized that the “filing of a *lis pendens* certainly does not create a lien, . . . it is a consequential action which section 547 permits the trustee to avoid, provided it occurs within the requisite 90-day period.” 432 B.R. at 224.

EVB argued unsuccessfully that any equitable reformation would date back to the original but erroneous deed of trust. The Bankruptcy Court determined that the existence of an intervening creditor, without notice of any interest held by EVB, trumps the applicability of any equitable remedy which would provide EVB with priority.


11 U.S.C. § 523(a)(4)

**Background:** Prepetition, chapter 7 debtor posted a bond without surety (“Bond”) in connection with his responsibilities as court-appointed conservator and guardian. After the debtor did not appear at a show cause hearing for failure to file a final accounting, the Albemarle Circuit Court issued an order forfeiting the Bond, and directing the Bond issuer, Cincinnati Insurance Company (“Cincinnati”), to pay the Bond’s face value to the beneficiary. Subsequently, Cincinnati obtained default judgment against the debtor—and a damages award exceeding two hundred thousand dollars (“Debt”)—on its state court lawsuit for indemnification under the terms of the Bond agreement. After the debtor filed for chapter 7 bankruptcy, Cincinnati initiated an adversary proceeding under 11 U.S.C. § 523(a)(4), seeking a determination that the Debt was non dischargeable. Cincinnati thereafter filed a motion for summary judgment (“Motion”).

**Holding:** The Court denied the Motion without prejudice. Under the Fourth Circuit Court’s decision in *Kubota Tractor Corp. v. Strack* (In re Strack), 524 F.3d 493, 497 (4th Cir. 2008), a plaintiff seeking a determination that a debt is non-dischargeable under section 523(a)(4) must establish: (1) the debtor was acting in a fiduciary capacity when the debt arose; and (2) that the debt arose from the debtor’s defalcation. With respect to the first prong of the Strack test,
the Court concluded that state law controls whether a debtor was acting in a fiduciary capacity when debt at issue arose. In Virginia, a court-appointed guardian is defined by statute as a “fiduciary.” Accordingly, the Court concluded that the debtor—who conceded he was appointed as a guardian pursuant to Virginia law—was acting in a fiduciary capacity when the Debt arose.

On the other hand, the Court concluded that federal bankruptcy law governs whether a debt resulted from a debtor’s defalcation. The current standard in the Fourth Circuit does not require a finding of recklessness or intentional misconduct to support a determination that a debt is excepted from discharge under section 523(a)(4), but requires merely finding “the failure to meet an obligation or a non-fraudulent default.” In re Uwimana, 274 F.3d 806 (4th Cir. 2001). Nevertheless, the Court concluded that the standard identified by the Fourth Circuit in Uwimana directly contrasted with the approach taken by many other circuits, and that the split of authority on this issue was being weighed by the United States Supreme Court, which recently granted certiorari on a case from the Eleventh Circuit Court of Appeals. See Bullock v. BankChampaign, N.A. (In re Bullock), 670 F.3d 1160 (11th Cir. 2012), cert. granted, 81 U.S.L.W. 3228 (U.S. Oct. 29, 2012) (No. 11-1518). Accordingly, the Court concluded that it was premature to determine if a genuine issue of material fact existed, due to uncertainty as to the appropriate legal standard to be met.


Background: Chapter 13 debtor objected to the priority status of a claim (“Claim”) filed by his ex-wife (“Spouse”) on account of unpaid financial obligations (“Obligation”) under the couple’s ratified separation and property settlement agreement (“Agreement”). Pursuant to the Agreement, the debtor’s Obligations included making direct payments to creditors on account of certain pre-separation joint debts, including car payments and credit card expenses.

Holding: The Court concluded that the Obligations at issue were not entitled to priority expense status. Pursuant to 11 U.S.C. § 507(a)(1)(A), an allowed unsecured claim for domestic support obligation owed to a former spouse as of the petition date is entitled to first priority. To qualify for priority expense status under section 507(a)(1)(A), an obligation must satisfy the definition of “domestic support obligation” under section 101(14A). The burden of establishing that an obligation is a “domestic support obligation” belongs to the party seeking priority. To determine whether an obligation is a domestic support obligation, the critical inquiry is whether the parties intended the obligation as alimony, support, or maintenance: (1) the language and substance of the agreement; (2) the relative financial position of the parties when they entered the agreement; (3) the function of the obligation within the agreement; and (4) evidence of overbearing at the time of the agreement. See In re Austin, 271 B.R. 97, 105 (Bankr. E.D. Va. 2001).

The Court concluded that it was unable to effectively weigh the second and fourth factors based on the limited factual record before it. Applying the first and third factors, the Court concluded that the Obligations at issue were not in the nature of alimony, support, or maintenance. The Agreement contained several provisions specifically waiving the parties’ entitlement to spousal and child support. Each obligation under the Agreement—including the Obligations at issue—were coupled with a corresponding benefit. In light of the lack of supportive purpose, the Court found that Obligations, and the Agreement as a whole, exhibited a quid-pro-quo characteristic more akin to property settlement. Therefore, the Court concluded that the Spouse failed to establish the elements of a domestic support obligation under section 101(14A), and that the Claim was not entitled to priority status pursuant to section 507(a)(1)(A).

11 U.S.C. § 548(c) and Privileged Communications

Background: Chapter 7 bankruptcy trustee ("Trustee") initiated adversary proceeding pursuant to 11 U.S.C. §§ 548(a)(1)(A) and 550(a) seeking to avoid and recover funds transferred by the debtor from Northern Trust Bank ("Northern Trust") to defendant Wells Fargo Bank, N.A. ("Wells Fargo") during the two year prepetition period. During pretrial discovery, Trustee filed a motion ("Motion") to compel production of documents ("Documents") withheld by Wells Fargo under claims of attorney-client privilege and attorney work product doctrine.

Holding: The Court granted the Motion in part, and denied the Motion in part. The Court concluded that Documents fell into one of three categories: (a) documents that were covered by the attorney-client privilege because they sought or gave legal advice from or by Wells Fargo's in-house counsel ("Counsel"); (b) documents that were not covered by the attorney-client privilege but that, nevertheless, were covered by the work-product doctrine, regardless as to whether Counsel was the author or recipient of the document, because Counsel tasked the author or the recipient to act as his agent for purposes of conducting an investigation in anticipation of litigation; and (c) documents for which neither the attorney-client privilege nor the attorney work product doctrine was applicable, and which, therefore, the Court concluded must be produced.

In denying the Motion with respect to the first two categories of Documents, the Court rejected the Trustee’s argument that Wells Fargo waived the applicable privileges because it put its good faith at issue in the litigation by asserting the good faith transferee defense under 11 U.S.C. § 548(c). The Court concluded that, on the narrow facts of given case, the Trustee overstated the “at issue” exception. The Court observed that the attorney-client privilege can be waived by asserting reliance on counsel as an affirmative defense. Courts within the Fourth Circuit have utilized a three-part test for determining when a party has impliedly waived by the privilege by its own affirmative conduct, which involves an examination of whether: (1) the assertion of privilege was the result of some affirmative act, such as filing suit, by the asserting party; (2) through this act, the asserting party put the protected information at issue by making it relevant to the case; and (3) application of the privilege would have denied the opposing party access to information vital to his defense. See Botkin v. Donegal Mut. Ins. Co., 2011 U.S. Dist. LEXIS 63871, at *6 (W.D. Va. 2011).

Applying this test, the Court concluded that Wells Fargo did not put the advice of its Counsel at issue. The assertion of a good faith transferee defense under section 548(c) of the Bankruptcy Code does not, in and of itself, result in waiver of the attorney-client privilege and work product doctrine. The Court concluded that an affirmative act on the part of Counsel was necessary to result in privilege waiver. The Court found that, on the given facts, the most that could be concluded is that Wells Fargo conducted an investigation before accepting funds from Northern Trust.
About the Bankruptcy Law Section

The Bankruptcy Law Section of the Virginia State Bar, established in 1990, maintains a membership of over 600 attorneys. The Section’s primary goal is to enhance the communication and exchange of ideas and information involving bankruptcy issues among Virginia attorneys. A further objective is to foster unity among members of the Section by providing a forum where they can share information and experiences. Finally, the Section seeks to promote public understanding of the field of bankruptcy law.

To further these goals and objectives, the Section conducts and assists with a number of activities, which are described on the Calendar of Events on the Section’s website at www.vsb.org/sections/bk/. Anyone interested in learning more about the Bankruptcy Law Section, in joining one of the Section’s committees, or in becoming a member, may contact the Chair of the Section, Douglas Foley, at 804-783-8300 or any of the Board of Governors.

Application for Membership
Bankruptcy Law Section 2012 - 2013
Virginia State Bar

Name

Virginia State Bar I.D. No. (from your Bar card)

Firm

Address

$20 Annual Membership Dues Enclosed (Check payable to “Virginia State Bar”)

Mail to: Bankruptcy Law Section
Virginia State Bar
Eighth & Main Building
707 East Main Street, Suite 1500
Richmond, Virginia 23219-2803
Virginia State Bar Bankruptcy Law Section
2012-2013 Board of Governors

Douglas M. Foley, Esq.
Chair
McGuireWoods LLP
World Trade Center, Suite 9000
101 West Main Street
Norfolk, VA 23510
(t) 757-640-3715
(f) 757-640-3957

Karen M. Crowley, Esq.
Crowley, Libertore, Ryan & Brogan, P.C.
Town Point Center, Suite 300
150 Boush Street
Norfolk, VA 23510
(t) 757-333-4502
(f) 757-333-4514

Angela Marie Scolforo, Esq.
Chapter 13 Trusteeship
123 East Main Street
Suite 310
Charlottesville, VA 22902
(t) 434-817-9915

Steven B. Ramsdell, Esq.
Vice Chair
Tyler, Bartl, Ramsdell & Counts, P.L.C.
Suite 202
300 North Washington Street
Alexandria, VA 22314
(t) 703-549-5003
(f) 703-549-5011

Malissa Lambert Giles, Esq.
129 East Campbell Ave., Suite 300
Roanoke, VA 24011
(t) 540-981-9000
(f) 540-981-9327

Maria Timoney, Esq.
Southwest Virginia Legal Aid
510 West Fulton Street
Wytheville, VA 24382
(t) 276-783-8300
(f) 276-783-7411

Robert Schaefer Westermann, Esq.
Secretary
Hirschler Fleischer, P.C.
PO Box 500
Richmond, VA 23218-0500
(t) 804-771-5610
(f) 804-644-0957

David Armistead Greer, Esq.
Law Offices of David A. Greer PLC
Suite 1225
500 East Main Street
Norfolk, VA 23510
(t) 757-227-5155
(f) 757-227-5158

Madeline Agnes Trainor, Esq.
Cyrn & Miller LLP
Suite 200
100 North Pitt Street
Alexandria, VA 22314
(t) 703-299-0600
(f) 703-783-7411

Karen M. Crowley, Esq.
Crowley, Libertore, Ryan & Brogan, P.C.
Town Point Center, Suite 300
150 Boush Street
Norfolk, VA 23510
(t) 757-333-4502
(f) 757-333-4514

Christopher A. Jones, Esq.
Whiteford Taylor & Preston LLP
Suite 300
3190 Fairview Park Drive
Falls Church, VA 22042-4510
(t) 703-280-9263
(f) 703-280-9139

Cecelia Ann Weschler, Esq.
Office of The U.S. Trustee
Federal Building, Room 625
200 Granby Street
Norfolk, VA 23510-1814
(t) 757-441-4012 ext.107
(f) 757-441-3266

Mark C. Leffler, Esq.
Newsletter Editor
Boleman Law Firm, P.C.
272 Bendix Road, Suite 130
Virginia Beach, VA 23452
(t) 757-313-3000
(f) 804-358-8704

Michael D. Mueller, Esq.
Christian & Barton, LLP
909 East Main Street
Suite 1200
Richmond, Virginia 23219-3095
(t) 804-697-4147
(f) 804-697-6396

Angela Marie Scolforo, Esq.
Chapter 13 Trusteeship
123 East Main Street
Suite 310
Charlottesville, VA 22902
(t) 434-817-9915

Lynn L. Tavenner, Esq.
Crowley, Libertore, Ryan & Brogan, P.C.
Town Point Center, Suite 300
150 Boush Street
Norfolk, VA 23510
(t) 757-333-4502
(f) 757-333-4514

Maria Timoney, Esq.
Southwest Virginia Legal Aid
510 West Fulton Street
Wytheville, VA 24382
(t) 276-783-8300
(f) 276-783-7411

Robert Schaefer Westermann, Esq.
Secretary
Hirschler Fleischer, P.C.
PO Box 500
Richmond, VA 23218-0500
(t) 804-771-5610
(f) 804-644-0957

Malissa Lambert Giles, Esq.
129 East Campbell Ave., Suite 300
Roanoke, VA 24011
(t) 540-981-9000
(f) 540-981-9327

Madeline Agnes Trainor, Esq.
Cyrn & Miller LLP
Suite 200
100 North Pitt Street
Alexandria, VA 22314
(t) 703-299-0600
(f) 703-783-7411

Lynn L. Tavenner, Esq.
Immediate Past Chair
Tavenner & Beran, PLC
Second Floor
20 North 8th Street
Richmond, VA 23219
(t) 804-783-8300
(f) 804-783-0178

Douglas Edward Little, Esq.
710 East High Street
P.O. Box 254
Charlottesville, VA 22902
(t) 434-977-4500
(f) 434-293-5727

Theresa B. Patrick
Liaison
Virginia State Bar
Suite 1500
707 East Main Street
Richmond, VA 23219
(t) 804-775-0515
(f) 804-775-0501

Mark C. Leffler, Esq.
Newsletter Editor
Boleman Law Firm, P.C.
272 Bendix Road, Suite 130
Virginia Beach, VA 23452
(t) 757-313-3000
(f) 804-358-8704

Michael D. Mueller, Esq.
Christian & Barton, LLP
909 East Main Street
Suite 1200
Richmond, Virginia 23219-3095
(t) 804-697-4147
(f) 804-697-6396
Have an Idea or Comment for the Virginia State Bar?

The Board of Governors of the Virginia State Bar Bankruptcy Section has established a membership committee to evaluate future projects to be undertaken by the Bankruptcy Law Section that would be of benefit and importance to its members. The committee is interested in any ideas or views that the section’s members may have for the planning committee to consider. Any ideas or comments can be directed to Steve Ramsdell at 703-549-5003.

The Bankruptcy Law Section of the Virginia State Bar produces the Bankruptcy Law News for its members. The purpose of the Bankruptcy Law Section is to promote the efficient administration of bankruptcy law and practice, including sponsoring programs, publications, and seminars on bankruptcy law and practice. For more information about the Bankruptcy Law Section, please see our website at www.vsb.org/sections/bk/.