INSIDE THE MINDS™

STRATEGIES FOR CONSUMER BANKRUPTCY APPEALS

LEADING LAWYERS ON ANALYZING BANKRUPTCY TRENDS, NAVIGATING THE APPEAL PROCESS, AND DEVELOPING A STRONG CASE

ASPATORE

Charles J. Schneider, Charles J. Schneider PC
Kathi M. Sandweiss and Roger L. Cohen, Jaburg & Wilk PC
Kenneth M. Richards, Luper Neidenthal & Logan LPA
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Inside the Minds Project Manager, Tiffany Smith; edited by Eddie Fournier; proofread by Melanie Zimmerman

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AN INSIDE PERSPECTIVE ON FILING A BANKRUPTCY APPEAL

Strategies for Consumer Bankruptcy Appeals provides an authoritative, insider's perspective on best practices for ensuring a successful consumer bankruptcy appeal. Featuring experienced consumer bankruptcy practitioners from around the country, this book guides the reader through the logistics of the appellate process, from filing a notice of appeal to receiving the bankruptcy appellate panel's decision. These top lawyers analyze the factors lawyers and clients must take into account when deciding to appeal, such as considering the best timing, determining standing, identifying appealable issues, and weighing possible alternatives to bankruptcy. Additionally, these leaders examine the key trends and cases currently affecting the consumer bankruptcy practice area, and discuss what they mean for lawyers and future appeals. The different niches represented and the breadth of perspectives presented enable readers to get inside some of the great legal minds of today, as these experienced lawyers offer up their thoughts on the keys to success within this ever-evolving field.

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The Nuances of the Consumer Bankruptcy Appeal Process

Charles J. Schneider

Owner

Charles J. Schneider PC

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Introduction: The Appellate Process Should Be a Well-Known Path

There is a 1.1 percent chance that a petition for writ of certiorari will be granted by the US Supreme Court. *Caperton v. A. T. Massey Coal Co.*, 129 S. Ct. 2252, 2272 (U.S. 2009); *see also The Chief Justice's 2010 Year-End Report on the Federal Judiciary*, www.supremecourt.gov/publicinfo/year-end/year-endreports.aspx. Despite the unlikelihood that any case may be granted review by the Supreme Court, there have been at least five published Supreme Court opinions in the 2010 and 2011 calendar years thus far on consumer bankruptcy issues. Three of these cases deal with issues spawned by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA). Although consumer bankruptcy cases do not often make headlines and in most cases individually do not justify the cost of an appeal, the appeals are being heard by the highest court in the land, as they involve a significant segment of the population seeking bankruptcy relief.

The appellate process has considerable impact on how consumer bankruptcy is practiced. Consumer bankruptcy attorneys who are familiar with the appeal process and are known to appeal adverse opinions have a significant advantage in obtaining a favorable outcome for their clients. The appellate process should be a well-known path for all consumer bankruptcy practitioners.

Recent Trends in Consumer Bankruptcy and Appeals

We find ourselves on a bleak economic landscape as consumer bankruptcy attorneys. No longer are we filing bankruptcies to stop the imminent foreclosure on a home or get back the repossessed car. The prevailing trend is to file Chapter 7 bankruptcies because most debtors want to get rid of their homes. The severe undervaluation of homes is making it unwarranted to hang on to the home. Even in circumstances where a totally unsecured second mortgage (such as in *Lane v. W. Interstate Bancorp (In Re Lane)*, 280 F.3d 663 (6th Cir. 2002)) can be stripped, clients are still choosing not to keep their homes, as their value is so dramatically reduced. People are leaving their state of residence, such as in Michigan, to find jobs and are abandoning homes whose values have dramatically fallen. The question posed is how can we keep home ownership a part of the motivation for filing bankruptcy? The answer to this question can be developed through the appeal process.

Is an Accelerated Mortgage Note Subject to Modification?

In the process of foreclosing a mortgage, the mortgagor must declare a default and accelerate the balance owed on the promissory note. The balance, therefore, can no longer be paid in installments but is immediately due and owing. A Chapter 13 plan may modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence. 11 U.S.C. § 1322(b)(2). This provision is tempered by 1322(c)(2), which states that in a case in which the last payment on the "original payment schedule" for a claim secured only by a security interest in real property that is the debtor's principal residence is due before the date on which the final payment under the plan is due, the plan may provide for the payment of the claim as modified pursuant to Section 1325(a)(5). The phrase "original payment schedule" is a term that is not defined in the Bankruptcy Code. Is the definition of that phrase broad enough to encompass the last accelerated payment due on the promissory note? Can the mortgage claim then be bifurcated and crammed down pursuant to 11 U.S.C. § 506(a)(1)? *See In re Nepil*, 206 B.R. 72 (Bankr. D.N.J. 1997); *accord In re Padgett*, 273 B.R. 277 (Bankr. M.D. Fla. 2001). The appellate process can provide the definition lacking in the code to assist clients facing foreclosure to keep their homes.

Can Non-Residential Mortgages Be Modified and Paid Beyond the Term of the Plan?

Landlords with multiple pieces of property—some income-earning and some not—are not subject to the anti-modification mortgage provision of 11 U.S.C. § 1322(b)(2) because they hold non-residential mortgages. Similarly, where the debtor's home mortgage is not protected from modification because the debtor's use of the property is not exclusively as a "principal residence," as it may also include a commercial use, can he or she also modify the mortgage payment by increasing or decreasing the payment, reducing the interest, reducing the payment period, and bifurcate the loan under 11 U.S.C. § 506(a)? The term "principal residence" is not defined by the code. The appellate process can be used by consumer bankruptcy practitioners to expand opportunities for their clients to retain severely devalued homes by defining the term. *See Lomas Mortgage Inc. v. Louis*, 82 F.3d 1, 3–6 (1st Cir. 1996). In some instances, the amortization of the

bifurcated secured loan balance may still create a payment that is too large to pay in five years. May a debtor who is either a landlord or a homeowner who has expanded the use of the home to include commercial purposes amortize the remaining secured loan beyond the maximum of five years permitted for a Chapter 13 plan? Does the debtor have the ability to both modify under § 1322(b)(2) and maintain the regular monthly payments under § 1322(b)(5)? These issues are ripe for appeal. *See Federal Nat'l Mortgage Ass'n v. Ferreira (In re Ferreira)*, 223 B.R. 258, 261–62 (D.R.I. 1998); *Enewally v. Washington Mut. Bank (In re Enewally)*, 276 B.R. 643, 647–52 (Bankr. C.D. Cal. 2002).

Revenue-Strapped States Fight the "Straddling Tax Claim"

Changes in the economy have also provoked income tax authorities to attempt to opt out of Chapter 13 bankruptcy cases. This undoubtedly reflects a governmental policy to increase revenue at the expense of Chapter 13 debtors by immediately enforcing the principal, interest, and penalties due on the tax claims that would otherwise be modified and stayed by the filing of the Chapter 13. In a series of cases, the state of Michigan challenged the Chapter 13 debtor's attempts to include treatment of income tax debt that arises after January 1 but is ultimately due on April 15. *See In re Turner*, 420 B.R. 711 (Bankr. E.D. Mich. Dec. 21, 2009); *Michigan Department of Treasury v. Hight (In re Hight)*, 434 B.R. 505 (W.D. Mich. Aug. 10, 2010); *Michigan Dep't of Treasury v. Senczyszyn (In re Senczyszyn)*, 444 B.R. 750 (E.D. Mich. Feb. 11, 2011). Commonly referred to as the straddling tax claim, it was the position of the state that such a debt could not be included in the Chapter 13 case as a pre-petition tax debt, because although payable it was not yet due and was therefore a post-petition debt. Relying on *United States v Ripley (In re Ripley)*, 926 F.2d 440 (5th Cir. 1991), as authority, the state asserted that only it could file a claim for post–petition taxes, as they became due only after April 15. Although Michigan debtors appear to be prevailing (*Hight* and *Senczyszyn*), consumer bankruptcy practitioners have to remain vigilant against revenue-strapped states. The straddling tax claim issue has far-reaching implications that could also include property tax claims that similarly become payable but not ultimately due until a later date. It represents an issue that will need an appellate resolution.

Must Non-Dischargeable Debts Wait Out the Term of the Chapter 13 Plan?

BAPCPA has made Chapter 13 less attractive to clients, as the "super discharge" (a discharge under the prior 11 U.S.C. § 1328 that discharges debts that would otherwise be non-dischargeable under Chapter 7 discharge) is not as super as it once was. Previously, under Section §1328, the super discharge enabled us to discharge fraudulent debts under 11 U.S.C. § 523(a)(2), breaches of fiduciary debts under § 523(4), and so on. Although these debts may not be discharged under the present § 1328(a), they must nevertheless be filed as adversary cases and meet the same deadlines and procedures for trials that exist in a Chapter 7 case. If there is a determination of non-dischargeabilty, the prevailing creditor's immediate satisfaction of the debt may be postponed by the court's automatic stay and the length of the plan. It will be condemned to non-discriminatory treatment and hence a *pro rata* distribution with other dischargeable unsecured creditors, but only if the automatic stay remains in place. 11 U.S.C. § 362(c)(2)(C) provides for the lift of the automatic stay upon the finding of non-dischargeability by the court. *See Boatmen's Bank v. Embry (In re Embry)*, 10 F.3d 401 (6th Cir. 1993); *In re Mu'min*, 374 B.R. 149 (Bankr. E.D. Pa. 2007). That may not be the case in a Chapter 13. BAPCPA provides yet another issue ripe for appeal.

The Impact of Trends on Lawyers and Clients

Fewer clients are seeking relief through Chapter 13, although BAPCPA was intended to make Chapter 7 less available. From the observations of this attorney, the human resources at the US Trustee's Office were also increased to accomplish that mission. Instead, clients are seeking other means for dealing with debt, such as debt negotiators and credit counselors. Lawyers are losing business despite the bad times clients are facing. There are a significant number of people who still need bankruptcy relief. They are reluctant to pursue bankruptcy relief because they will be ensnared in a Chapter 13 case and the prevailing "pay as much as you can" attitude, as reflected in the opinion of Justice Kagen in *Ransom v. FIA Card Services*, 131 S. Ct. 716,721 (2011). There is an attitude that Chapter 13 is not intended to give clients a fresh start as it was prior to BAPCPA. Instead, the expectation is that debtors should pay the maximum they can afford. Despite the sentiment expressed by Justice Kagen, many bankruptcy judges can recall