Mortgage Foreclosure/Bankruptcy /Ethics and Professionalism

Discussion and role play of the struggles of a restaurant/bar and it's owners in economic distress due the COVID-19 pandemic including: (i) state court foreclosure action commenced against real estate holding company (owned by one of the principals of the restaurant and his wife); (ii) creditor claims against restaurant; (iii) owner guarantee of corporate debt; (iv) non-bankruptcy options for workout of corporate debt; (v) corporate bankruptcy options; (vi) bankruptcy and pre-planning advice to owner/guarantors; and (vii) discussion of related ethical issues and attorney sanctions for violation of bankruptcy rules

Participants: (Biographies t/b provided)

Masters:

Andrew M. Thaler Esq.
Craig Robins Esq
Eric Gruber Esq.
Jaspreet Mayall Esq.
John Reali Esq.
John Brickman Esq.

Associates:
Spiros Avramidis Esq.

Students:
Michael Sugame (Touro Law School Student)

Timed Agenda

Presentation of Fact Pattern 5 minutes

Role play regarding foreclosure of commercial property
Clients with Debtor attorney; Debtor attorney with Bank attorney
(John Reali, Eric Gruber, Jaspreet Mayall and Michael Sugame) 25 minutes

Role play regarding (Business Owners and their attorneys)

Overview of bankruptcy options for restaurant and
real estate holding company 5 minutes

Discussion of personal bankruptcy including
Strategic bankruptcy planning

(Andrew Thaler, Spiros Avramidis, Jaspreet Mayall and Michael Sugame)

35 minutes

Discussion of select bankruptcy topics

Extension of Automatic stay to non-filing
Third parties; Subchapter V modification of
Consumer Mortgages; Update on State and
Federal Moratoriums

(Michael Sugame) 5-7 minutes

Discussion of Ethical Issues/ Sanctions for Violation of Bankruptcy Rules

(Craig Robins, John Brickman) 20-23 minutes

Questions 5 minutes

C.L.E. Credits

.75 Professional Skills
.75 Professional practice
.5 Ethics and Professionalism

Written Materials: t/b provided)

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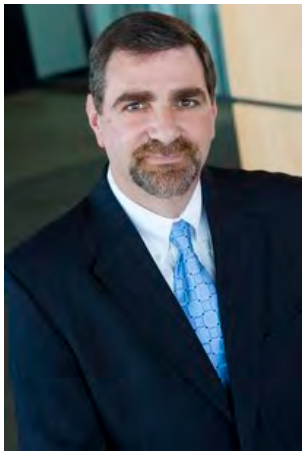

Andrew M. Thaler, Esq.

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Practice Areas
Bankruptcy – Creditor & Debtor Representation,
Chapter 7, 11, & 13; bankruptcy litigation;
Mediator of Commercial Matters

For over 36 years Andy Thaler has dedicated his practice to assisting individuals and companies in financial distress by eliminating and/or reorganizing debt. He also represents creditors, banks, landlords, secured creditors, Chapter 7 Trustees, defendants in fraudulent conveyance and preference actions, asset bidders and others in myriad matters arising in bankruptcy cases. As a bankruptcy boutique, Thaler Law Firm handles all aspects of bankruptcy and insolvency. Mr. Thaler has been a federally appointed Chapter 7 Bankruptcy Trustee since 1990. Thaler Law Firm takes great pride in providing personal and caring service to each and every client from beginning to end of their matter.

As a Commercial Mediator, Mr. Thaler facilitates parties reaching resolution of their disputes without the high cost of conventional litigation.

Mr. Thaler has previously held the positions of Dean of the Nassau Academy of Law, President of the Theodore Roosevelt Inn of Court; Chairperson of the Bankruptcy and Alternative Dispute Resolution Committees of the Nassau County Bar Association and Board Member of the Nassau Bar.

Martindale Hubbell's highest "AV" rating
New York Metro "Super Lawyers" Bankruptcy & Creditor/Debtor Rights.
Pulse Magazine Top Legal Eagle.

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Spiros Avramidis

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Practice Areas
Bankruptcy – Creditor & Debtor Representation
Adversary ProceedingS and Related Litigation

Spiros Avramidis is an associate at Thaler Law Firm PLLC and engages in many aspects of bankruptcy, including chapter 7 trustee representation, chapter 7, 11, and 13 debtor and creditor representation. Additionally, Spiros represents plaintiffs and defendants in adversary proceedings, including non-dischargeability, denial of discharge, fraudulent conveyances and preferences. Spiros also engages in out of court insolvency work.

Spiros received his law degree from St. John's University School of Law in 2014, graduating *cum laude* and serving as Senior Staff for the St. John's Law Review, while being Vice President of the Hellenic Club. Spiros was admitted to practice in New York State and the United States District Courts for the Eastern and Southern Districts of New York in 2015. Spiros received his B.A. in philosophy from Baruch College in 2011.

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Professional Profile

Over the last 34 years, I have utilized a combination of a deep knowledge of the law and sound business judgment to deliver sophisticated, efficient and cost-effective legal services to a diversified commercial and corporate practice representing public and private companies and individuals over a range of practice areas from litigation and dispute resolution to transactional and corporate matters.

An experienced litigator and accomplished trial attorney, I have developed and implemented the legal strategy for a broad range of civil cases, arbitrations, and mediations. I have represented plaintiffs and defendants in various matters across a spectrum of substantive areas, including commercial disputes, partnership and corporate disputes, real estate, construction, business torts, creditors' rights including bankruptcy, securities, telecommunications and general business law in bench and jury trials - to verdict where necessary - before the federal and state courts and engaged in appellate practice before the Second Circuit and state Appellate Courts. I have also represented clients before various arbitration and mediation panels.

On the transactional side, I have experience in asset-based lending and other areas of commercial finance, including workouts, turn-around situations, and bankruptcy matters. I have drafted and negotiated sophisticated commercial finance and equipment leasing transactions for both sides. I have represented lenders taking back mortgages in sophisticated real estate transactions, including drafting, negotiating, and closing a "wrap mortgage" for the lender on a commercial property. I have also represented various business entities in connection with the acquisition and sale of businesses and assets. I also represent landlords, managing agents and businesses in connection with the structuring and negotiation of commercial real estate leases.

I am the outside general counsel for several small and mid-size businesses. I regularly advise business enterprises, real estate owners, developers and managers, healthcare providers, entrepreneurs, investors and high net worth individuals on a wide range of issues in all phases of their day-to-day business operations as well as their business deals and transactions, including business and real estate transactions, general corporate matters, partnership matters and relations, corporate finance, mergers and acquisitions and a wide range of commercial agreements and matters and work closely with these clients to do the planning, due diligence, negotiating, drafting and consummation of such deals and transactions.

Jaspreet S. Mayall

Partner

Jaspreet S. Mayall is a Partner in our Telecommunications Group. He counsels cellular phone companies, master wholesalers, retailers and original equipment manufacturers.

His national client base relies upon his counsel on negotiating their agreements with the wireless carriers, as well as mergers and acquisitions, joint venture agreements, OEM agreements, retail leases, and other agreements in the telecommunications field. He has extensive experience litigating a wide variety of telecommunications cases in state and federal courts.

He also litigates commercial matters. Mr. Mayall began his legal career in our Debtor/Creditor Rights and Bankruptcy Group. In bankruptcy proceedings, he acts as counsel to trustees, debtors, and secured and unsecured creditors. He has significant experience in Trial and Appeals before New York State and Federal Courts.

Mr. Mayall serves as a member of the Committee on Character and Fitness for the Second, Tenth and Eleventh Judicial Districts. The Appellate Division, Second Department of the Supreme Court of the State of New York first appointed him in 2007.

Named consecutively to the New York Metro Super Lawyers list from 2013 through 2020, Mr. Mayall first earned the distinction in 2010. Long Island Business News named him as one of Long Island's 40 Under 40 Rising Stars in 2003. Recently, he was also honored with the India Republic Day Award from the Town of Hempstead.

He earned his Bachelor of Business Administration from Hofstra University and graduated from Hofstra University School of Law. There he was inducted into Phi Alpha Delta, the largest co-ed professional law fraternity in the United States.

An active member of the Nassau County Bar Association, he is admitted to practice in New York; New Jersey; the Eastern, Southern, Western and Northern Districts of New York and the District of New Jersey; and the District of Columbia. He has achieved the highest professional rating by Martindale Hubbell.

Mr. Mayall was appointed to the board of the American Heart Association and is charged with helping the organization build awareness in the South Asian community. He is fluent in Hindi and Punjabi

Practice Areas

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John M. Brickman, head of litigation in the Long Island office of McLaughlin & Stern, LLC, practices primarily in the areas of commercial litigation and trust and estates disputes. He has tried more than 100 cases before federal and state courts and arbitration tribunals, and has argued more than 100 appeals. He devotes particular attention to contract, corporate, partnership, trusts and estates, employment, intellectual property, unfair competition, civil racketeering, franchise, real estate, and construction cases, and frequently represents parties in disputes involving professional practices and substantial closely-held businesses. Recently, he won a million-dollar trial verdict for owners of a Manhattan apartment awarding damages following years of water intrusion into their home. In another trial recently, he secured dismissal of a commercial mortgage foreclosure action, after showing that the lender lacked standing to pursue the case.

Mr. Brickman combines legal practice with public service. He serves as a Commissioner of the New York State Legislative Ethics Commission, to which he was appointed in 2016 and reappointed in 2021. From 2007 until 2011, he was a Commissioner of the New York State Commission on Public Integrity, which enforced state lobbying and public employee ethics laws and regulations. He was a Director of the Nassau Health Care Corporation, which operates the Nassau University Medical Center, from 2005 to 2009. From 2005 to 2008, he served as Chairman of the Correctional Association of New York, an organization founded in 1844 that does research and advocacy in criminal justice issues. Mr. Brickman serves as a director of several not-for-profit organizations, including the Abraham Lincoln Brigade Archives and the NuHealth Foundation. He has been a Director of The Levitt Foundation (from 2011 to 2014 he was also its President), the Long Island Medical Foundation, and the Nassau Health Care Foundation. From 1992 to 1994 he served as a Trustee of The Johns Hopkins University and President of The Johns Hopkins Alumni Association. Since 2006, he has been a member of the National Panel of Arbitrators of the American Arbitrators Association. He has been appointed as Arbitrator in more than sixty AAA cases.

Mr. Brickman is active in bar association, educational, and community activities. Annually, he chairs a Continuing Legal Education program on lawyers' ethics and civility, presented by the New York State Bar Association. From 1991 to 2006, he was Adjunct Professor of Law at Touro College, Jacob D. Fuchsberg Law Center, where he taught the course in Pre-Trial Litigation to senior law students. He writes and speaks regularly on public issues, including government and legal ethics and the administration of correctional and criminal justice agencies. He is pro bono legal counsel to the Manhasset-Great Neck Community Service Center.

Mr. Brickman received his undergraduate degree from The Johns Hopkins University and his J.D. degree cum laude in 1969 from Columbia University School of Law, where he was a Harlan Fiske Stone Scholar and Dean's List Scholar and served as Revision Editor of the Columbia Journal of Law and Social Problems. From 1971 to 1975, he served as Executive Director of the New York City Board of Correction, the agency of New York

City government that oversees the operation of the New York City jail system and issues reports and recommendations for change.

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BA Political Science, Queens College 1957; LLB St. John's University Law School 1961; US Marine Corps Reserves, 1957-1963; Admitted to practice Appellate Division, Second Department 1961; Admitted to practice in U.S. District Court, Eastern District 1965; Member of the Nassau County Bar Association, New York State Bar Association, Columbian Lawyers Association of Nassau County, Nassau County Magistrates Association, American Justinian Society of Jurists and New York State Magistrates Association

Former Director, Nassau County Bar Association; Member of the Nassau County Blue Ribbon Commission to examine procedures of the Nassau County Clerk's Office (1992), Member of NCBA committee on Closing a Law Office; Member, Nassau County Bar Association Town and Village Justice Courts Task Force, Director and Vice President of Nassau County Bar Tech Center (1994) Appointed Conservator by Appellate Division, Second Department, to close law offices of disbarred attorneys; Past President, Columbian Lawyers Association of Nassau County; Past President, Nassau County Magistrates Association; Secretary, American Justinian Society of Jurists; Former Director of the Nassau Suffolk Law Services Committee; Past Chairman of Real Property Law Committee, Past Chairman Veterans & Military Law Committee, Past Chairman of Computer Committee;Former Member of Grievance Committee, Nassau County Bar Association; Member, Theodore Roosevelt Inns of Court; Nassau County Bar Association's Pro Bono Attorney of the Month for February, 2011; New York State Pro Bono Attorney for Nassau/Suffolk Counties, 1994; Nassau Bar Association Mentor, Hempstead Middle School, 1994-1999 ; Co-ordinator and mentor, Jericho Middle School 1999-2017. Former member of the Nassau County Bar Association Nominating Committee. Member of Elder Law, Trusts and Estates, & Environmental Law Committee.

Initiator of the Veterans Legal Advocacy Project at NCBA

Initiator, together with Ed Aulman, former Director of Nassau County Veterans Service Agency, of the Veterans Court in Nassau District Court County.

Recipient of the Hon. Frank J. Santagata award, from the Nassau County Magistrates Association, for ethics, professionalism and devotion to justice.

Participant in NCBA Foreclosure Clinic and Super Storm Sandy Clinic; Volunteer lawyer of the day at Volunteer Lawyers Project in Hempstead Landlord Tenant Court.

Trustee, Village of Sea Cliff 1980-1990; Deputy Mayor 1987-1990

Sea Cliff Village Justice, 1990-2018, Associate Village Justice 2018-2019

MICHAEL V. SUGAMELE

136 Division Avenue, Massapequa, NY 11758
(516) 301-7636 ▪ msugamel@student.touro.edu

EDUCATION

Touro College Jacob D. Fuchsberg Law Center, Central Islip, NY
Juris Doctor Candidate, May 2022
GPA: 3.63
Honors: *Touro Law Review*; Moot Court Honors Board; CALI Awards for Academic Excellence in Torts II and Civil Dispute Resolution and Procedure II; Faculty Recognition Award for Excellence in Legal Process II; Dean's List (Fall 2019); Honors Program Scholar; Bedford Insurance Scholarship
Activities: Student Bar Association, Treasurer; Suffolk County Bar Association – Touro Chapter, Treasurer; Research Assistant to Professor Debbie Lanin; Theodore Roosevelt Inn of Court; Legal Education Access Program

St. John's University, Queens, NY
Bachelor of Science in Criminal Justice, May 2018
Honors: Omicron Delta Kappa Honor Society; National Honor Society of Leadership and Success
Activities: Chi Theta Omega Fraternity, President

LEGAL EXPERIENCE

U.S. Attorney's Office, Eastern District of New York, Central Islip, NY
Legal Extern, Criminal Division August 2020 – December 2020
Conducted legal research on topics including bail and government fraud. Drafted an internal memorandum regarding recommendations for bail. Reviewed case documents. Observed virtual and in-person proceedings, including sentencing hearings, plea bargains, an arraignment, and a violation of supervised release hearing. Discussed case strategy and updates with supervising attorney and other members of the team.

Nassau County Attorney's Office, Mineola, NY
Legal Intern, Litigation Bureau June 2020 – August 2020
Assisted attorneys with personal injury, labor, and civil rights cases. Conducted legal research on topics including racial discrimination claims under § 1983 and New York Civil Service Law. Drafted documents, including memoranda and a motion to reargue in a personal injury case. Reviewed case files, including trial transcripts.

Stern & Stern, P.C., Bellmore, NY
Paralegal March 2019 – June 2020
Prepared documents including motions, orders, and answers related to debt collection matters. Managed attorney calendar and monitored court appearances. Prepared for and assisted with trials, including organizing court documents, conducting legal research, and drafting case summaries.

Law Office of Ronald D. Weiss, Melville, NY
Paralegal (Temporary) December 2018 – February 2019
Assisted attorneys with matters related to bankruptcy and mortgage foreclosure proceedings. Prepared documents including motions, orders and answers. Communicated with clients and opposing counsel. Prepared for and assisted with trials, including organizing court documents and conducting legal research.

The Lavelle Law Firm, Mineola, NY
Paralegal / Intern October 2013 – December 2018
Assisted supervising attorney with representing plaintiffs in personal injury litigation matters. Prepared documents including complaints, motions, orders, pleadings, and subpoenas. Managed attorney calendar and monitored court appearances. Reviewed discovery material and responded to demand requests. Communicated with clients to gather relevant information. Answered telephones and assisted with other administrative tasks.

OTHER

Languages: Conversational Spanish; Basic Mandarin Chinese
Skills: eCourts; Westlaw; LexisNexis; MyCase; Timeslips
Interests: Golf; bowling; softball; running

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Craig D. Robins, Esq., has been a practicing attorney for over 33 years. During most of this time, he has devoted his practice almost exclusively to bankruptcy, foreclosure defense and debt-related matters. Mr. Robins has had experience in thousands of bankruptcy cases which has included representing both consumers in Chapter 7 and 13 cases, and businesses in Chapter 11 cases.

Craig D. Robins, Esq. received a Bachelor of Arts degree from Emory University in 1981. He studied law in London, England from 1982 to 1983 through the Notre Dame Law School Concannon Program in International Law. He received a Juris Doctorate from Western New England Law School in 1984. He was admitted to the Massachusetts and New York Bars in 1985 and the Florida Bar in 1987. He is also admitted to practice in various Federal District Courts, the United States Tax Court, and the United States Claims Court. Mr. Robins briefly interned as a judicial law clerk to the Honorable Richard Wallach, Supreme Court Judge (New York, First Department).

Martindale-Hubbell, the nationally recognized service that rates attorneys by peer review, has rated Mr. Robins "high to very high."

Mr. Robins has written extensively on bankruptcy law and has authored over 200 published articles on a variety of topics including bankruptcy law and procedure, bankruptcy legislation, bankruptcy practice, and the interaction of bankruptcy law on personal injury cases and matrimonial rights. He continues to be a regular columnist on bankruptcy law for the *Suffolk Lawyer* where he has written for about 28 years, and also writes articles for the *Nassau Lawyer*.

Mr. Robins is recognized as an authority on bankruptcy law and practice and is often sought out by the media. He has lectured on bankruptcy law for the Nassau County Bar Association and has discussed bankruptcy law on radio and television talk shows and news programs.

In addition to bankruptcy, Mr. Robins actively defends foreclosure cases brought against Long Island homeowners. The *New York Times* wrote a page-one story about a foreclosure case that he successfully dismissed.

He has been interviewed on News 12 several times and has been interviewed and quoted in *Newsday* about 20 times, and in a host of other periodicals including *New York Times*, *New York Law Journal*, *Boston Globe*, *Washington Post*, and *Long Island Business News*. Since 1991, he has also been actively involved in giving presentations on bankruptcy law and foreclosure law to attorneys and Federal and State Court Judges through the Theodore Roosevelt Chapter of the American Inns of Court, of which he is a member and also sits on its executive board. While Chairman of that organization's annual banquet, he hosted dinners honoring United States Supreme Court Justice Samuel A. Alito, Jr., and New York's highest judge, Judith S. Kay, Chief Judge of the New York State Court of Appeals.

Mr. Robins is active in the Bankruptcy Committees of both the Nassau and Suffolk Bar Associations, and is on the Suffolk County Bar Association Mentor Program where he is called upon to provide assistance to younger members of the Bar. He is a long-time member of the American Bankruptcy Institute and the National Association of Consumer Bankruptcy Attorneys.

Mr. Robins is a founding co-chairman of the Nassau County Bar Association's *Pro Bono* Bankruptcy Committee. He holds the distinction of having represented more *pro bono* debtors than any other attorney on Long Island. The Nassau County Bar Association awarded Mr. Robins a Presidential Recognition Award for his dedication in representing *pro bono* debtors in bankruptcy proceedings and also awarded him the *Pro Bono* Attorney of the Year Award. Mr. Robins was recognized by the Volunteer Lawyers Project for his *pro bono* work when he was named *Pro Bono* Attorney of the Month three times. *Newsday* honored Mr. Robins by naming him in its "Winners" column for his dedication to community work.

Mr. Robins has represented a wide and diverse range of debtors in bankruptcy cases. In addition to representing numerous typical Long Islanders, he represented a former New York Yankees baseball player, dozens of professionals including attorneys, doctors, dentists and C.P.A.'s, and a variety of businesses, ranging from a professional sports franchise to multi-million dollar companies to mom-and-pop storefronts.

When not practicing law, Mr. Robins enjoys traveling and bicycle riding. He has been a competitive bicycle racer for over thirty years and won numerous races. He is also an avid photographer known for his avante garde style. His images, which have won numerous awards, have appeared in museums and galleries, and have been published in *The New York Times* and *Newsday*, and on several magazine covers. He lives in Suffolk County with his wife and son, Max, who recently won the Suffolk County Mock Trial High School Championship.

[Nov. 2018]

Bankruptcy BASICS

Administrative Office
of the United States Courts

Bankruptcy BASICS

Bankruptcy Judges Division

Administrative Office
of the United States Courts

November 2011
Revised Third Edition

While the information presented is accurate as of the date of publication, it should not be cited or relied upon as legal authority. It should not be used as a substitute for reference to the United States Bankruptcy Code (title 11, United States Code) and the Federal Rules of Bankruptcy Procedure, both of which may be reviewed at local law libraries, or to local rules of practice adopted by each bankruptcy court. Finally, this publication should not substitute for the advice of competent legal counsel.

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Bankruptcy Basics

A Publication of the Bankruptcy Judges Division

Introduction

Bankruptcy Basics is designed to provide basic information to debtors, creditors, court personnel, the media, and the general public on different aspects of the federal bankruptcy laws. It also provides individuals who may be considering bankruptcy with a basic explanation of the different chapters under which a bankruptcy case may be filed and to answer some of the most commonly asked questions about the bankruptcy process.

Bankruptcy Basics provides general information only. While every effort has been made to ensure that the information contained in it is accurate as of the date of publication, it is not a full and authoritative statement of the law on any particular topic. The information presented in this publication should not be cited or relied upon as legal authority and should not be used as a substitute for reference to the United States Bankruptcy Code (title 11, United States Code) and the Federal Rules of Bankruptcy Procedure.

Most importantly, Bankruptcy Basics should not substitute for the advice of competent legal counsel or a financial expert. Neither the Bankruptcy Judges Division nor the Administrative Office of the United States Courts can provide legal or financial advice. Such advice may be obtained from a competent attorney, accountant, or financial adviser.

The Process

Article I, Section 8, of the United States Constitution authorizes Congress to enact "uniform Laws on the subject of Bankruptcies." Under this grant of authority, Congress enacted the "Bankruptcy Code" in 1978. The Bankruptcy Code, which is codified as title 11 of the United States Code, has been amended several times since its enactment. It is the uniform federal law that governs all bankruptcy cases.

The procedural aspects of the bankruptcy process are governed by the Federal Rules of Bankruptcy Procedure (often called the "Bankruptcy Rules") and local rules of each bankruptcy court. The Bankruptcy Rules contain a set of official forms for use in bankruptcy cases. The Bankruptcy Code and Bankruptcy Rules (and local rules) set forth the formal legal procedures for dealing with the debt problems of individuals and businesses.

There is a bankruptcy court for each judicial district in the country. Each state has one or more districts. There are 90 bankruptcy districts across the country. The bankruptcy courts generally have their own clerk's offices.

The court official with decision-making power over federal bankruptcy cases is the United States bankruptcy judge, a judicial officer of the United States district court. The bankruptcy judge may decide any matter connected with a bankruptcy case, such as

eligibility to file or whether a debtor should receive a discharge of debts. Much of the bankruptcy process is administrative, however, and is conducted away from the courthouse. In cases under chapters 7, 12, or 13, and sometimes in chapter 11 cases, this administrative process is carried out by a trustee who is appointed to oversee the case.

A debtor's involvement with the bankruptcy judge is usually very limited. A typical chapter 7 debtor will not appear in court and will not see the bankruptcy judge unless an objection is raised in the case. A chapter 13 debtor may only have to appear before the bankruptcy judge at a plan confirmation hearing. Usually, the only formal proceeding at which a debtor must appear is the meeting of creditors, which is usually held at the offices of the U.S. trustee. This meeting is informally called a "341 meeting" because section 341 of the Bankruptcy Code requires that the debtor attend this meeting so that creditors can question the debtor about debts and property.

A fundamental goal of the federal bankruptcy laws enacted by Congress is to give debtors a financial "fresh start" from burdensome debts. The Supreme Court made this point about the purpose of the bankruptcy law in a 1934 decision:

> [I]t gives to the honest but unfortunate debtor…a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt.

Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934). This goal is accomplished through the bankruptcy discharge, which releases debtors from personal liability from specific debts and prohibits creditors from ever taking any action against the debtor to collect those debts. This publication describes the bankruptcy discharge in a question and answer format, discussing the timing of the discharge, the scope of the discharge (what debts are discharged and what debts are not discharged), objections to discharge, and revocation of the discharge. It also describes what a debtor can do if a creditor attempts to collect a discharged debt after the bankruptcy case is concluded.

Six basic types of bankruptcy cases are provided for under the Bankruptcy Code, each of which is discussed in this publication. The cases are traditionally given the names of the chapters that describe them.

Chapter 7, entitled Liquidation, contemplates an orderly, court-supervised procedure by which a trustee takes over the assets of the debtor's estate, reduces them to cash, and makes distributions to creditors, subject to the debtor's right to retain certain exempt property and the rights of secured creditors. Because there is usually little or no nonexempt property in most chapter 7 cases, there may not be an actual liquidation of the debtor's assets. These cases are called "no-asset cases." A creditor holding an unsecured claim will get a distribution from the bankruptcy estate only if the case is an asset case and the creditor files a proof of claim with the bankruptcy court. In most chapter 7 cases, if the debtor is an individual, he or she receives a discharge that releases him or her from personal liability for certain dischargeable debts. The debtor normally receives a discharge just a few months after the petition is filed. Amendments to the Bankruptcy Code enacted in to the Bankruptcy Abuse Prevention and Consumer

Protection Act of 2005 require the application of a "means test" to determine whether individual consumer debtors qualify for relief under chapter 7. If such a debtor's income is in excess of certain thresholds, the debtor may not be eligible for chapter 7 relief.

Chapter 13, entitled Adjustment of Debts of an Individual With Regular Income, is designed for an individual debtor who has a regular source of income. Chapter 13 is often preferable to chapter 7 because it enables the debtor to keep a valuable asset, such as a house, and because it allows the debtor to propose a "plan" to repay creditors over time – usually three to five years. Chapter 13 is also used by consumer debtors who do not qualify for chapter 7 relief under the means test. At a confirmation hearing, the court either approves or disapproves the debtor's repayment plan, depending on whether it meets the Bankruptcy Code's requirements for confirmation. Chapter 13 is very different from chapter 7 since the chapter 13 debtor usually remains in possession of the property of the estate and makes payments to creditors, through the trustee, based on the debtor's anticipated income over the life of the plan. Unlike chapter 7, the debtor does not receive an immediate discharge of debts. The debtor must complete the payments required under the plan before the discharge is received. The debtor is protected from lawsuits, garnishments, and other creditor actions while the plan is in effect. The discharge is also somewhat broader (*i.e.*, more debts are eliminated) under chapter 13 than the discharge under chapter 7.

Chapter 11, entitled Reorganization, ordinarily is used by commercial enterprises that desire to continue operating a business and repay creditors concurrently through a court-approved plan of reorganization. The chapter 11 debtor usually has the exclusive right to file a plan of reorganization for the first 120 days after it files the case and must provide creditors with a disclosure statement containing information adequate to enable creditors to evaluate the plan. The court ultimately approves (confirms) or disapproves the plan of reorganization. Under the confirmed plan, the debtor can reduce its debts by repaying a portion of its obligations and discharging others. The debtor can also terminate burdensome contracts and leases, recover assets, and rescale its operations in order to return to profitability. Under chapter 11, the debtor normally goes through a period of consolidation and emerges with a reduced debt load and a reorganized business.

Chapter 12, entitled Adjustment of Debts of a Family Farmer or Fisherman with Regular Annual Income, provides debt relief to family farmers and fishermen with regular income. The process under chapter 12 is very similar to that of chapter 13, under which the debtor proposes a plan to repay debts over a period of time – no more than three years unless the court approves a longer period, not exceeding five years. There is also a trustee in every chapter 12 case whose duties are very similar to those of a chapter 13 trustee. The chapter 12 trustee's disbursement of payments to creditors under a confirmed plan parallels the procedure under chapter 13. Chapter 12 allows a family farmer or fisherman to continue to operate the business while the plan is being carried out.

Chapter 9, entitled Adjustment of Debts of a Municipality, provides essentially for reorganization, much like a reorganization under chapter 11. Only a "municipality" may file under chapter 9, which includes cities and

towns, as well as villages, counties, taxing districts, municipal utilities, and school districts.

The purpose of Chapter 15, entitled Ancillary and Other Cross-Border Cases, is to provide an effective mechanism for dealing with cases of cross-border insolvency. This publication discusses the applicability of Chapter 15 where a debtor or its property is subject to the laws of the United States and one or more foreign countries.

In addition to the basic types of bankruptcy cases, Bankruptcy Basics provides an overview of the Servicemembers' Civil Relief Act, which, among other things, provides protection to members of the military against the entry of default judgments and gives the court the ability to stay proceedings against military debtors.

This publication also contains a description of liquidation proceedings under the Securities Investor Protection Act ("SIPA"). Although the Bankruptcy Code provides for a stockbroker liquidation proceeding, it is far more likely that a failing brokerage firm will find itself involved in a SIPA proceeding. The purpose of SIPA is to return to investors securities and cash left with failed brokerages. Since being established by Congress in 1970, the Securities Investor Protection Corporation has protected investors who deposit stocks and bonds with brokerage firms by ensuring that every customer's property is protected, up to $500,000 per customer.

The bankruptcy process is complex and relies on legal concepts like the "automatic stay," "discharge," "exemptions," and "assume." Therefore, the final chapter of this publication is a glossary of Bankruptcy Terminology which explains, in layman's terms, most of the legal concepts that apply in cases filed under the Bankruptcy Code.

The Discharge in Bankruptcy

The bankruptcy discharge varies depending on the type of case a debtor files: chapter 7, 11, 12, or 13. Bankruptcy Basics attempts to answer some basic questions about the discharge available to *individual debtors* under all four chapters including:

1. What is a discharge in bankruptcy?

2. When does the discharge occur?

3. How does the debtor get a discharge?

4. Are all the debtor's debts discharged or only some?

5. Does the debtor have a right to a discharge or can creditors object to the discharge?

6. Can the debtor receive a second discharge in a later case?

7. Can the discharge be revoked?

8. May the debtor pay a discharged debt after the bankruptcy case has been concluded?

9. What can the debtor do if a creditor attempts to collect a discharged debt after the case is concluded?

10. May an employer terminate a debtor's employment solely because the person was a debtor or failed to repay a discharged debt?

WHAT IS A DISCHARGE IN BANKRUPTCY?

A bankruptcy discharge releases the debtor from personal liability for certain specified types of debts. In other words, the debtor is no longer legally required to pay any debts that are discharged. The discharge is a permanent order prohibiting the creditors of the debtor from taking any form of collection action on discharged debts, including legal action and communications with the debtor, such as telephone calls, letters, and personal contacts.

Although a debtor is not personally liable for discharged debts, a valid lien (*i.e.*, a charge upon specific property to secure payment of a debt) that has not been avoided (*i.e.*, made unenforceable) in the bankruptcy case will remain after the bankruptcy case. Therefore, a secured creditor may enforce the lien to recover the property secured by the lien.

WHEN DOES THE DISCHARGE OCCUR?

The timing of the discharge varies, depending on the chapter under which the case is filed. In a chapter 7 (liquidation) case, for example, the court usually grants the discharge promptly on expiration of the time fixed for filing a complaint objecting to discharge and the time fixed for filing a motion to dismiss the case for substantial abuse (60 days following the first date set for the 341 meeting). Typically, this occurs about four months after the date the debtor files the petition with the clerk of the bankruptcy court. In individual chapter 11 cases, and in cases under chapter 12 (adjustment of debts of a family farmer or fisherman) and 13 (adjustment of debts of an individual with regular income), the court generally grants the discharge as soon as

practicable after the debtor completes all payments under the plan. Since a chapter 12 or chapter 13 plan may provide for payments to be made over three to five years, the discharge typically occurs about four years after the date of filing. The court may deny an individual debtor's discharge in a chapter 7 or 13 case if the debtor fails to complete "an instructional course concerning financial management." The Bankruptcy Code provides limited exceptions to the "financial management" requirement if the U.S. trustee or bankruptcy administrator determines there are inadequate educational programs available, or if the debtor is disabled or incapacitated or on active military duty in a combat zone.

HOW DOES THE DEBTOR GET A DISCHARGE?

Unless there is litigation involving objections to the discharge, the debtor will usually automatically receive a discharge. The Federal Rules of Bankruptcy Procedure provide for the clerk of the bankruptcy court to mail a copy of the order of discharge to all creditors, the U.S. trustee, the trustee in the case, and the trustee's attorney, if any. The debtor and the debtor's attorney also receive copies of the discharge order. The notice, which is simply a copy of the final order of discharge, is not specific as to those debts determined by the court to be non-dischargeable, *i.e.*, not covered by the discharge. The notice informs creditors generally that the debts owed to them have been discharged and that they should not attempt any further collection. They are cautioned in the notice that continuing collection efforts could subject them to punishment for contempt. Any inadvertent failure on the part of the clerk to send the debtor or any creditor a copy of the discharge order promptly within the time required by the rules does not affect the validity of the order granting the discharge.

ARE ALL OF THE DEBTOR'S DEBTS DISCHARGED OR ONLY SOME?

Not all debts are discharged. The debts discharged vary under each chapter of the Bankruptcy Code. Section 523(a) of the Code specifically excepts various categories of debts from the discharge granted to individual debtors. Therefore, the debtor must still repay those debts after bankruptcy. Congress has determined that these types of debts are not dischargeable for public policy reasons (based either on the nature of the debt or the fact that the debts were incurred due to improper behavior of the debtor, such as the debtor's drunken driving).

There are 19 categories of debt excepted from discharge under chapters 7, 11, and 12. A more limited list of exceptions applies to cases under chapter 13.

Generally speaking, the exceptions to discharge apply automatically if the language prescribed by section 523(a) applies. The most common types of nondischargeable debts are certain types of tax claims, debts not set forth by the debtor on the lists and schedules the debtor must file with the court, debts for spousal or child support or alimony, debts for willful and malicious injuries to person or property, debts to governmental units for fines and penalties, debts for most government funded or guaranteed educational loans or benefit overpayments, debts for personal injury caused by the debtor's operation of a motor vehicle while intoxicated, debts owed to certain tax-advantaged retirement plans, and debts for

certain condominium or cooperative housing fees.

The types of debts described in sections 523(a)(2), (4) and(6) (obligations affected by fraud or maliciousness) are not automatically excepted from discharge. Creditors must ask the court to determine that these debts are excepted from discharge. In the absence of an affirmative request by the creditor and the granting of the request by the court, the types of debts set out in sections 523(a)(2), (4) and (6) will be discharged.

A slightly broader discharge of debts is available to a debtor in a chapter 13 case than in a chapter 7 case. Debts dischargeable in a chapter 13, but not in chapter 7, include debts for willful and malicious injury to property, debts incurred to pay non-dischargeable tax obligations, and debts arising from property settlements in divorce or separation proceedings. Although a chapter 13 debtor generally receives a discharge only after completing all payments required by the court-approved (*i.e.*, "confirmed") repayment plan, there are some limited circumstances under which the debtor may request the court to grant a "hardship discharge" even though the debtor has failed to complete plan payments. Such a discharge is available only to a debtor whose failure to complete plan payments is due to circumstances beyond the debtor's control. The scope of a chapter 13 "hardship discharge" is similar to that in a chapter 7 case with regard to the types of debts that are excepted from the discharge. A hardship discharge also is available in chapter 12 if the failure to complete plan payments is due to "circumstances for which the debtor should not justly be held accountable."

DOES THE DEBTOR HAVE THE RIGHT TO A DISCHARGE OR CAN CREDITORS OBJECT TO THE DISCHARGE?

In chapter 7 cases, the debtor does not have an absolute right to a discharge. An objection to the debtor's discharge may be filed by a creditor, by the trustee in the case, or by the U.S. trustee. Creditors receive a notice shortly after the case is filed that sets forth much important information, including the deadline for objecting to the discharge. To object to the debtor's discharge, a creditor must file a complaint in the bankruptcy court before the deadline set out in the notice. Filing a complaint starts a lawsuit referred to in bankruptcy as an "adversary proceeding."

The court may deny a chapter 7 discharge for any of the reasons described in section 727(a) of the Bankruptcy Code, including failure to provide requested tax documents; failure to complete a course on personal financial management; transfer or concealment of property with intent to hinder, delay, or defraud creditors; destruction or concealment of books or records; perjury and other fraudulent acts; failure to account for the loss of assets; violation of a court order or an earlier discharge in an earlier case commenced within certain time frames (discussed below) before the date the petition was filed. If the issue of the debtor's right to a discharge goes to trial, the objecting party has the burden of proving all the facts essential to the objection.

In chapter 12 and chapter 13 cases, the debtor is usually entitled to a discharge upon completion of all payments under the plan. As

in chapter 7, however, discharge may not occur in chapter 13 if the debtor fails to complete a required course on personal financial management. A debtor is also ineligible for a discharge in chapter 13 if he or she received a prior discharge in another case commenced within time frames discussed the next paragraph. Unlike chapter 7, creditors do not have standing to object to the discharge of a chapter 12 or chapter 13 debtor. Creditors can object to confirmation of the repayment plan, but cannot object to the discharge if the debtor has completed making plan payments.

CAN A DEBTOR RECEIVE A SECOND DISCHARGE IN A LATER CHAPTER 7 CASE?

The court will deny a discharge in a later chapter 7 case if the debtor received a discharge under chapter 7 or chapter 11 in a case filed within eight years before the second petition is filed. The court will also deny a chapter 7 discharge if the debtor previously received a discharge in a chapter 12 or chapter 13 case filed within six years before the date of the filing of the second case unless (1) the debtor paid all "allowed unsecured" claims in the earlier case in full, or (2) the debtor made payments under the plan in the earlier case totaling at least 70 percent of the allowed unsecured claims and the debtor's plan was proposed in good faith and the payments represented the debtor's best effort. A debtor is ineligible for discharge under chapter 13 if he or she received a prior discharge in a chapter 7, 11, or 12 case filed four years before the current case or in a chapter 13 case filed two years before the current case.

CAN THE DISCHARGE BE REVOKED?

The court may revoke a discharge under certain circumstances. For example, a trustee, creditor, or the U.S. trustee may request that the court revoke the debtor's discharge in a chapter 7 case based on allegations that the debtor: obtained the discharge fraudulently; failed to disclose the fact that he or she acquired or became entitled to acquire property that would constitute property of the bankruptcy estate; committed one of several acts of impropriety described in section 727(a)(6) of the Bankruptcy Code; or failed to explain any misstatements discovered in an audit of the case or fails to provide documents or information requested in an audit of the case. Typically, a request to revoke the debtor's discharge must be filed within one year of the discharge or, in some cases, before the date that the case is closed. The court will decide whether such allegations are true and, if so, whether to revoke the discharge.

In a chapter 11, 12 and 13 cases, if confirmation of a plan or the discharge is obtained through fraud, the court can revoke the order of confirmation or discharge.

MAY THE DEBTOR PAY A DISCHARGED DEBT AFTER THE BANKRUPTCY CASE HAS BEEN CONCLUDED?

A debtor who has received a discharge may voluntarily repay any discharged debt. A debtor may repay a discharged debt even though it can no longer be legally enforced. Sometimes a debtor agrees to repay a debt because it is owed to a family member or because it represents an obligation to an individual for whom the debtor's reputation is important, such as a family doctor.

WHAT CAN THE DEBTOR DO IF A CREDITOR ATTEMPTS TO COLLECT A DISCHARGED DEBT AFTER THE CASE IS CONCLUDED?

If a creditor attempts collection efforts on a discharged debt, the debtor can file a motion with the court, reporting the action and asking that the case be reopened to address the matter. The bankruptcy court will often do so to ensure that the discharge is not violated. The discharge constitutes a permanent statutory injunction prohibiting creditors from taking any action, including the filing of a lawsuit, designed to collect a discharged debt. A creditor can be sanctioned by the court for violating the discharge injunction. The normal sanction for violating the discharge injunction is civil contempt, which is often punishable by a fine.

CAN AN EMPLOYER TERMINATE A DEBTOR'S EMPLOYMENT SOLELY BECAUSE THE PERSON WAS A DEBTOR OR FAILED TO PAY A DISCHARGED DEBT?

The law provides express prohibitions against discriminatory treatment of debtors by both governmental units and private employers. A governmental unit or private employer may not discriminate against a person solely because the person was a debtor, was insolvent before or during the case, or has not paid a debt that was discharged in the case. The law prohibits the following forms of governmental discrimination: terminating an employee; discriminating with respect to hiring; or denying, revoking, suspending, or declining to renew a license, franchise, or similar privilege. A private employer may not discriminate with respect to employment if the discrimination is based solely upon the bankruptcy filing.

Chapter 7

Liquidation Under the Bankruptcy Code

ALTERNATIVES TO CHAPTER 7

Debtors should be aware that there are several alternatives to chapter 7 relief. For example, debtors who are engaged in business, including corporations, partnerships, and sole proprietorships, may prefer to remain in business and avoid liquidation. Such debtors should consider filing a petition under chapter 11 of the Bankruptcy Code. Under chapter 11, the debtor may seek an adjustment of debts, either by reducing the debt or by extending the time for repayment, or may seek a more comprehensive reorganization. Sole proprietorships may also be eligible for relief under chapter 13 of the Bankruptcy Code.

In addition, individual debtors who have regular income may seek an adjustment of debts under chapter 13 of the Bankruptcy Code. A particular advantage of chapter 13 is that it provides individual debtors with an opportunity to save their homes from foreclosure by allowing them to "catch up" past due payments through a payment plan. Moreover, the court may dismiss a chapter 7 case filed by an individual whose debts are primarily consumer rather than business debts if the court finds that the granting of relief would be an abuse of chapter 7. 11 U.S.C. § 707(b).

If the debtor's "current monthly income"[1] is more than the state median, the Bankruptcy Code requires application of a "means test" to determine whether the chapter 7 filing is presumptively abusive. Abuse is presumed if the debtor's aggregate current monthly income over 5 years, net of certain statutorily allowed expenses, is more than (i) $11,725, or (ii) 25% of the debtor's nonpriority unsecured debt, as long as that amount is at least $7,025.[2] The debtor may rebut a presumption of abuse only by a showing of special circumstances that justify additional expenses or adjustments of current monthly income. Unless the debtor overcomes the presumption of abuse, the case will generally be converted to chapter 13 (with the debtor's consent) or will be dismissed. 11 U.S.C. § 707(b)(1).

Debtors should also be aware that out-of-court agreements with creditors or debt counseling services may provide an alternative to a bankruptcy filing.

BACKGROUND

A chapter 7 bankruptcy case does not involve the filing of a plan of repayment as in chapter 13. Instead, the bankruptcy trustee gathers and sells the debtor's nonexempt assets and uses the proceeds of such assets to pay holders of claims (creditors) in accordance with the provisions of the Bankruptcy Code. Part of the debtor's property may be subject to liens and mortgages that pledge the property to other creditors. In addition, the Bankruptcy Code will allow the debtor to keep certain "exempt" property; but a trustee will liquidate the debtor's remaining assets. Accordingly, potential debtors should realize that the filing of a petition under chapter 7 may result in the loss of property.

CHAPTER 7 ELIGIBILITY

To qualify for relief under chapter 7 of the Bankruptcy Code, the debtor may be an

individual, a partnership, or a corporation or other business entity. 11 U.S.C. §§ 101(41), 109(b). Subject to the means test described above for individual debtors, relief is available under chapter 7 irrespective of the amount of the debtor's debts or whether the debtor is solvent or insolvent. An individual cannot file under chapter 7 or any other chapter, however, if during the preceding 180 days a prior bankruptcy petition was dismissed due to the debtor's willful failure to appear before the court or comply with orders of the court, or the debtor voluntarily dismissed the previous case after creditors sought relief from the bankruptcy court to recover property upon which they hold liens. 11 U.S.C. §§ 109(g), 362(d) and (e). In addition, no individual may be a debtor under chapter 7 or any chapter of the Bankruptcy Code unless he or she has, within 180 days before filing, received credit counseling from an approved credit counseling agency either in an individual or group briefing. 11 U.S.C. §§ 109, 111. There are exceptions in emergency situations or where the U.S. trustee (or bankruptcy administrator) has determined that there are insufficient approved agencies to provide the required counseling. If a debt management plan is developed during required credit counseling, it must be filed with the court.

One of the primary purposes of bankruptcy is to discharge certain debts to give an honest individual debtor a "fresh start." The debtor has no liability for discharged debts. In a chapter 7 case, however, a discharge is only available to individual debtors, not to partnerships or corporations. 11 U.S.C. § 727(a)(1). Although an individual chapter 7 case usually results in a discharge of debts, the right to a discharge is not absolute, and some types of debts are not discharged. Moreover, a bankruptcy discharge does not extinguish a lien on property.

HOW CHAPTER 7 WORKS

A chapter 7 case begins with the debtor filing a petition with the bankruptcy court serving the area where the individual lives or where the business debtor is organized or has its principal place of business or principal assets.[3] In addition to the petition, the debtor must also file with the court: (1) schedules of assets and liabilities; (2) a schedule of current income and expenditures; (3) a statement of financial affairs; and (4) a schedule of executory contracts and unexpired leases. Fed. R. Bankr. P. 1007(b). Debtors must also provide the assigned case trustee with a copy of the tax return or transcripts for the most recent tax year as well as tax returns filed during the case (including tax returns for prior years that had not been filed when the case began). 11 U.S.C. § 521. Individual debtors with primarily consumer debts have additional document filing requirements. They must file: a certificate of credit counseling and a copy of any debt repayment plan developed through credit counseling; evidence of payment from employers, if any, received 60 days before filing; a statement of monthly net income and any anticipated increase in income or expenses after filing; and a record of any interest the debtor has in federal or state qualified education or tuition accounts. *Id.* A husband and wife may file a joint petition or individual petitions. 11 U.S.C. § 302(a). Even if filing jointly, a husband and wife are subject to all the document filing requirements of individual debtors. (The Official Forms may be purchased at legal stationery stores or downloaded from the internet at http://www.uscourts.gov/bkforms/index.html. They are not available from the court.)

The courts must charge a $245 case filing fee, a $46 miscellaneous administrative fee, and a $15 trustee surcharge. Normally, the fees must be paid to the clerk of the court upon filing. With the court's permission, however, individual debtors may pay in installments. 28 U.S.C. § 1930(a); Fed. R. Bankr. P. 1006(b); Bankruptcy Court Miscellaneous Fee Schedule, Item 8. The number of installments is limited to four, and the debtor must make the final installment no later than 120 days after filing the petition. Fed. R. Bankr. P. 1006. For cause shown, the court may extend the time of any installment, provided that the last installment is paid not later than 180 days after filing the petition. *Id*. The debtor may also pay the $46 administrative fee and the $15 trustee surcharge in installments. If a joint petition is filed, only one filing fee, one administrative fee, and one trustee surcharge are charged. Debtors should be aware that failure to pay these fees may result in dismissal of the case. 11 U.S.C. § 707(a).

If the debtor's income is less than 150% of the poverty level (as defined in the Bankruptcy Code), and the debtor is unable to pay the chapter 7 fees even in installments, the court may waive the requirement that the fees be paid. 28 U.S.C. § 1930(f).

In order to complete the Official Bankruptcy Forms that make up the petition, statement of financial affairs, and schedules, the debtor must provide the following information:

1. A list of all creditors and the amount and nature of their claims;

2. The source, amount, and frequency of the debtor's income;

3. A list of all of the debtor's property; and

4. A detailed list of the debtor's monthly living expenses, *i.e.*, food, clothing, shelter, utilities, taxes, transportation, medicine, etc.

Married individuals must gather this information for their spouse regardless of whether they are filing a joint petition, separate individual petitions, or even if only one spouse is filing. In a situation where only one spouse files, the income and expenses of the non-filing spouse is required so that the court, the trustee and creditors can evaluate the household's financial position.

Among the schedules that an individual debtor will file is a schedule of "exempt" property. The Bankruptcy Code allows an individual debtor[4] to protect some property from the claims of creditors because it is exempt under federal bankruptcy law or under the laws of the debtor's home state. 11 U.S.C. § 522(b). Many states have taken advantage of a provision in the Bankruptcy Code that permits each state to adopt its own exemption law in place of the federal exemptions. In other jurisdictions, the individual debtor has the option of choosing between a federal package of exemptions or the exemptions available under state law. Thus, whether certain property is exempt and may be kept by the debtor is often a question of state law. The debtor should consult an attorney to determine the exemptions available in the state where the debtor lives.

Filing a petition under chapter 7 "automatically stays" (stops) most collection actions against the debtor or the debtor's property. 11 U.S.C. § 362. But filing the petition does not stay certain types of actions listed under 11 U.S.C. § 362(b), and the stay may be effective only for a short time in some situations. The stay arises by operation of law

and requires no judicial action. As long as the stay is in effect, creditors generally may not initiate or continue lawsuits, wage garnishments, or even telephone calls demanding payments. The bankruptcy clerk gives notice of the bankruptcy case to all creditors whose names and addresses are provided by the debtor.

Between 21 and 40 days after the petition is filed, the case trustee (described below) will hold a meeting of creditors. If the U.S. trustee or bankruptcy administrator[5] schedules the meeting at a place that does not have regular U.S. trustee or bankruptcy administrator staffing, the meeting may be held no more than 60 days after the order for relief. Fed. R. Bankr. P. 2003(a). During this meeting, the trustee puts the debtor under oath, and both the trustee and creditors may ask questions. The debtor must attend the meeting and answer questions regarding the debtor's financial affairs and property. 11 U.S.C. § 343. If a husband and wife have filed a joint petition, they both must attend the creditors' meeting and answer questions. Within 14 days of the creditors' meeting, the U.S. trustee will report to the court whether the case should be presumed to be an abuse under the means test described in 11 U.S.C. § 704(b).

It is important for the debtor to cooperate with the trustee and to provide any financial records or documents that the trustee requests. The Bankruptcy Code requires the trustee to ask the debtor questions at the meeting of creditors to ensure that the debtor is aware of the potential consequences of seeking a discharge in bankruptcy such as the effect on credit history, the ability to file a petition under a different chapter, the effect of receiving a discharge, and the effect of reaffirming a debt. Some trustees provide written information on these topics at or before the meeting to ensure that the debtor is aware of this information. In order to preserve their independent judgment, bankruptcy judges are prohibited from attending the meeting of creditors. 11 U.S.C. § 341(c).

In order to accord the debtor complete relief, the Bankruptcy Code allows the debtor to convert a chapter 7 case to case under chapter 11, 12 or 13[6] as long as the debtor is eligible to be a debtor under the new chapter. However, a condition of the debtor's voluntary conversion is that the case has not previously been converted to chapter 7 from another chapter. 11 U.S.C. § 706(a). Thus, the debtor will not be permitted to convert the case repeatedly from one chapter to another.

ROLE OF THE CASE TRUSTEE

When a chapter 7 petition is filed, the U.S. trustee (or the bankruptcy court in Alabama and North Carolina) appoints an impartial case trustee to administer the case and liquidate the debtor's nonexempt assets. 11 U.S.C. §§ 701, 704. If all the debtor's assets are exempt or subject to valid liens, the trustee will normally file a "no asset" report with the court, and there will be no distribution to unsecured creditors. Most chapter 7 cases involving individual debtors are no asset cases. But if the case appears to be an "asset" case at the outset, unsecured creditors[7] must file their claims with the court within 90 days after the first date set for the meeting of creditors. Fed. R. Bankr. P. 3002(c). A governmental unit, however, has 180 days from the date the case is filed to file a claim. 11 U.S.C. § 502(b)(9). In the typical no asset chapter 7 case, there is no need for creditors to file proofs of claim because there will be no distribution. If the trustee later recovers assets

for distribution to unsecured creditors, the Bankruptcy Court will provide notice to creditors and will allow additional time to file proofs of claim. Although a secured creditor does not need to file a proof of claim in a chapter 7 case to preserve its security interest or lien, there may be other reasons to file a claim. A creditor in a chapter 7 case who has a lien on the debtor's property should consult an attorney for advice.

Commencement of a bankruptcy case creates an "estate." The estate technically becomes the temporary legal owner of all the debtor's property. It consists of all legal or equitable interests of the debtor in property as of the commencement of the case, including property owned or held by another person if the debtor has an interest in the property. Generally speaking, the debtor's creditors are paid from nonexempt property of the estate.

The primary role of a chapter 7 trustee in an asset case is to liquidate the debtor's nonexempt assets in a manner that maximizes the return to the debtor's unsecured creditors. The trustee accomplishes this by selling the debtor's property if it is free and clear of liens (as long as the property is not exempt) or if it is worth more than any security interest or lien attached to the property and any exemption that the debtor holds in the property. The trustee may also attempt to recover money or property under the trustee's "avoiding powers." The trustee's avoiding powers include the power to: set aside preferential transfers made to creditors within 90 days before the petition; undo security interests and other prepetition transfers of property that were not properly perfected under nonbankruptcy law at the time of the petition; and pursue nonbankruptcy claims such as fraudulent conveyance and bulk transfer remedies available under state law. In addition, if the debtor is a business, the bankruptcy court may authorize the trustee to operate the business for a limited period of time, if such operation will benefit creditors and enhance the liquidation of the estate. 11 U.S.C. § 721.

Section 726 of the Bankruptcy Code governs the distribution of the property of the estate. Under § 726, there are six classes of claims; and each class must be paid in full before the next lower class is paid anything. The debtor is only paid if all other classes of claims have been paid in full. Accordingly, the debtor is not particularly interested in the trustee's disposition of the estate assets, except with respect to the payment of those debts which for some reason are not dischargeable in the bankruptcy case. The individual debtor's primary concerns in a chapter 7 case are to retain exempt property and to receive a discharge that covers as many debts as possible.

THE CHAPTER 7 DISCHARGE

A discharge releases individual debtors from personal liability for most debts and prevents the creditors owed those debts from taking any collection actions against the debtor. Because a chapter 7 discharge is subject to many exceptions, though, debtors should consult competent legal counsel before filing to discuss the scope of the discharge. Generally, excluding cases that are dismissed or converted, individual debtors receive a discharge in more than 99 percent of chapter 7 cases. In most cases, unless a party in interest files a complaint objecting to the discharge or a motion to extend the time to object, the bankruptcy court will issue a discharge order relatively early in the case –

generally, 60 to 90 days after the date first set for the meeting of creditors. Fed. R. Bankr. P. 4004(c).

The grounds for denying an individual debtor a discharge in a chapter 7 case are narrow and are construed against the moving party. Among other reasons, the court may deny the debtor a discharge if it finds that the debtor: failed to keep or produce adequate books or financial records; failed to explain satisfactorily any loss of assets; committed a bankruptcy crime such as perjury; failed to obey a lawful order of the bankruptcy court; fraudulently transferred, concealed, or destroyed property that would have become property of the estate; or failed to complete an approved instructional course concerning financial management. 11 U.S.C. § 727; Fed. R. Bankr. P. 4005.

Secured creditors may retain some rights to seize property securing an underlying debt even after a discharge is granted. Depending on individual circumstances, if a debtor wishes to keep certain secured property (such as an automobile), he or she may decide to "reaffirm" the debt. A reaffirmation is an agreement between the debtor and the creditor that the debtor will remain liable and will pay all or a portion of the money owed, even though the debt would otherwise be discharged in the bankruptcy. In return, the creditor promises that it will not repossess or take back the automobile or other property so long as the debtor continues to pay the debt.

If the debtor decides to reaffirm a debt, he or she must do so before the discharge is entered. The debtor must sign a written reaffirmation agreement and file it with the court. 11 U.S.C. § 524(c). The Bankruptcy Code requires that reaffirmation agreements contain an extensive set of disclosures described in 11 U.S.C. § 524(k). Among other things, the disclosures must advise the debtor of the amount of the debt being reaffirmed and how it is calculated and that reaffirmation means that the debtor's personal liability for that debt will not be discharged in the bankruptcy. The disclosures also require the debtor to sign and file a statement of his or her current income and expenses which shows that the balance of income paying expenses is sufficient to pay the reaffirmed debt. If the balance is not enough to pay the debt to be reaffirmed, there is a presumption of undue hardship, and the court may decide not to approve the reaffirmation agreement. Unless the debtor is represented by an attorney, the bankruptcy judge must approve the reaffirmation agreement.

If the debtor was represented by an attorney in connection with the reaffirmation agreement, the attorney must certify in writing that he or she advised the debtor of the legal effect and consequences of the agreement, including a default under the agreement. The attorney must also certify that the debtor was fully informed and voluntarily made the agreement and that reaffirmation of the debt will not create an undue hardship for the debtor or the debtor's dependants. 11 U.S.C. § 524(k). The Bankruptcy Code requires a reaffirmation hearing if the debtor has not been represented by an attorney during the negotiating of the agreement, or if the court disapproves the reaffirmation agreement.11 U.S.C. § 524(d) and (m). The debtor may repay any debt voluntarily, however, whether or not a reaffirmation agreement exists. 11 U.S.C. § 524(f).

An individual receives a discharge for most of his or her debts in a chapter 7 bankruptcy

case. A creditor may no longer initiate or continue any legal or other action against the debtor to collect a discharged debt. But not all of an individual's debts are discharged in chapter 7. Debts not discharged include debts for alimony and child support, certain taxes, debts for certain educational benefit overpayments or loans made or guaranteed by a governmental unit, debts for willful and malicious injury by the debtor to another entity or to the property of another entity, debts for death or personal injury caused by the debtor's operation of a motor vehicle while the debtor was intoxicated from alcohol or other substances, and debts for certain criminal restitution orders.11 U.S.C. § 523(a). The debtor will continue to be liable for these types of debts to the extent that they are not paid in the chapter 7 case. Debts for money or property obtained by false pretenses, debts for fraud or defalcation while acting in a fiduciary capacity, and debts for willful and malicious injury by the debtor to another entity or to the property of another entity will be discharged unless a creditor timely files and prevails in an action to have such debts declared nondischargeable. 11 U.S.C. § 523(c); Fed. R. Bankr. P. 4007(c).

The court may revoke a chapter 7 discharge on the request of the trustee, a creditor, or the U.S. trustee if the discharge was obtained through fraud by the debtor, if the debtor acquired property that is property of the estate and knowingly and fraudulently failed to report the acquisition of such property or to surrender the property to the trustee, or if the debtor (without a satisfactory explanation) makes a material misstatement or fails to provide documents or other information in connection with an audit of the debtor's case. 11 U.S.C. § 727(d).

NOTES

1. The "current monthly income" received by the debtor is a defined term in the Bankruptcy Code and means the average monthly income received over the six calendar months before commencement of the bankruptcy case, including regular contributions to household expenses from nondebtors and including income from the debtor's spouse if the petition is a joint petition, but not including social security income or certain payments made because the debtor is the victim of certain crimes. 11 U.S.C. § 101(10A).

2. To determine whether a presumption of abuse arises, all individual debtors with primarily consumer debts who file a chapter 7 case must complete Official Bankruptcy Form B22A, entitled "Statement of Current Monthly Income and Means Test Calculation - For Use in Chapter 7." (The Official Forms may be purchased at legal stationery stores or downloaded from the internet at: http://www.uscourts.gov/bkforms/index.html. They are not available from the court.)

3. An involuntary chapter 7 case may be commenced under certain circumstances by a petition filed by creditors holding claims against the debtor. 11 U.S.C. § 303.

4. Each debtor in a joint case (both husband and wife) can claim exemptions under the federal bankruptcy laws. 11 U.S.C. § 522(m).

5. In North Carolina and Alabama, bankruptcy administrators perform similar functions that U.S. trustees perform in the remaining 48 states. These duties include establishing a panel of private trustees to serve as trustees in chapter 7 cases and supervising the administration of cases and trustees in cases

under chapters 7, 11, 12, and 13 of the Bankruptcy Code. The bankruptcy administrator program is administered by the Administrative Office of the United States Courts, while the U.S. trustee program is administered by the Department of Justice. For purposes of this publication, references to U.S. trustees are also applicable to bankruptcy administrators.

6. A fee is charged for converting, on request of the debtor, a case under chapter 7 to a case under chapter 11. The fee charged is the difference between the filing fee for a chapter 7 and the filing fee for a chapter 11. 28 U.S.C. § 1930(a). Currently, the difference is $755. *Id.* There is no fee for converting from chapter 7 to chapter 13.

7. Unsecured debts generally may be defined as those for which the extension of credit was based purely upon an evaluation by the creditor of the debtor's ability to pay, as opposed to secured debts, for which the extension of credit was based upon the creditor's right to seize collateral on default, in addition to the debtor's ability to pay.

Chapter 13

Individual Debt Adjustment

BACKGROUND

A chapter 13 bankruptcy is also called a wage earner's plan. It enables individuals with regular income to develop a plan to repay all or part of their debts. Under this chapter, debtors propose a repayment plan to make installments to creditors over three to five years. If the debtor's current monthly income is less than the applicable state median, the plan will be for three years unless the court approves a longer period "for cause."[1] If the debtor's current monthly income is greater than the applicable state median, the plan generally must be for five years. In no case may a plan provide for payments over a period longer than five years. 11 U.S.C. §1322(d). During this time the law forbids creditors from starting or continuing collection efforts.

This chapter discusses six aspects of a chapter 13 proceeding: the advantages of choosing chapter 13, the chapter 13 eligibility requirements, how a chapter 13 proceeding works, what may be included in chapter 13 repayment plan and how it is confirmed, making the plan work, and the special chapter 13 discharge.

ADVANTAGES OF CHAPTER 13

Chapter 13 offers individuals a number of advantages over liquidation under chapter 7. Perhaps most significantly, chapter 13 offers individuals an opportunity to save their homes from foreclosure. By filing under this chapter, individuals can stop foreclosure proceedings and may cure delinquent mortgage payments over time. Nevertheless, they must still make all mortgage payments that come due during the chapter 13 plan on time. Another advantage of chapter 13 is that it allows individuals to reschedule secured debts (other than a mortgage for their primary residence) and extend them over the life of the chapter 13 plan. Doing this may lower the payments. Chapter 13 also has a special provision that protects third parties who are liable with the debtor on "consumer debts." This provision may protect co-signers. Finally, chapter 13 acts like a consolidation loan under which the individual makes the plan payments to a chapter 13 trustee who then distributes payments to creditors. Individuals will have no direct contact with creditors while under chapter 13 protection.

CHAPTER 13 ELIGIBILITY

Any individual, even if self-employed or operating an unincorporated business, is eligible for chapter 13 relief as long as the individual's unsecured debts are less than $360,475 and secured debts are less than $1,081,400. 11 U.S.C. § 109(e). These amounts are adjusted periodically to reflect changes in the consumer price index. A corporation or partnership may not be a chapter 13 debtor. *Id.*

An individual cannot file under chapter 13 or any other chapter if, during the preceding 180 days, a prior bankruptcy petition was dismissed due to the debtor's willful failure to appear before the court or comply with orders of the court or was voluntarily dismissed after creditors sought relief from the bankruptcy court to recover property upon which they hold liens. 11 U.S.C. §§ 109(g), 362(d) and (e). In addition, no individual may be a debtor

under chapter 13 or any chapter of the Bankruptcy Code unless he or she has, within 180 days before filing, received credit counseling from an approved credit counseling agency either in an individual or group briefing. 11 U.S.C. §§ 109, 111. There are exceptions in emergency situations or where the U.S. trustee (or bankruptcy administrator) has determined that there are insufficient approved agencies to provide the required counseling. If a debt management plan is developed during required credit counseling, it must be filed with the court.

HOW CHAPTER 13 WORKS

A chapter 13 case begins by filing a petition with the bankruptcy court serving the area where the debtor has a domicile or residence. Unless the court orders otherwise, the debtor must also file with the court: (1) schedules of assets and liabilities; (2) a schedule of current income and expenditures; (3) a schedule of executory contracts and unexpired leases; and (4) a statement of financial affairs. Fed. R. Bankr. P. 1007(b). The debtor must also file a certificate of credit counseling and a copy of any debt repayment plan developed through credit counseling; evidence of payment from employers, if any, received 60 days before filing; a statement of monthly net income and any anticipated increase in income or expenses after filing; and a record of any interest the debtor has in federal or state qualified education or tuition accounts. 11 U.S.C. § 521. The debtor must provide the chapter 13 case trustee with a copy of the tax return or transcripts for the most recent tax year as well as tax returns filed during the case (including tax returns for prior years that had not been filed when the case began). *Id.* A husband and wife may file a joint petition or individual petitions. 11 U.S.C. § 302(a). (The Official Forms may be purchased at legal stationery stores or downloaded from the internet at http://www.uscourts.gov/bkforms/index.html. They are not available from the court.)

The courts must charge a $235 case filing fee and a $46 miscellaneous administrative fee. Normally the fees must be paid to the clerk of the court upon filing. With the court's permission, however, they may be paid in installments. 28 U.S.C. § 1930(a); Fed. R. Bankr. P. 1006(b); Bankruptcy Court Miscellaneous Fee Schedule, Item 8. The number of installments is limited to four, and the debtor must make the final installment no later than 120 days after filing the petition. Fed. R. Bankr. P. 1006(b). For cause shown, the court may extend the time of any installment, as long as the last installment is paid no later than 180 days after filing the petition. *Id.* The debtor may also pay the $46 administrative fee in installments. If a joint petition is filed, only one filing fee and one administrative fee are charged. Debtors should be aware that failure to pay these fees may result in dismissal of the case. 11 U.S.C. § 1307(c)(2).

In order to complete the Official Bankruptcy Forms that make up the petition, statement of financial affairs, and schedules, the debtor must compile the following information:

1. A list of all creditors and the amounts and nature of their claims;

2. The source, amount, and frequency of the debtor's income;

3. A list of all of the debtor's property; and

4. A detailed list of the debtor's monthly living expenses, *i.e.*, food, clothing, shelter, utilities, taxes, transportation, medicine, etc. Married individuals must gather this information for their spouse regardless of whether they are filing a joint petition, separate individual petitions, or even if only one spouse is filing. In a situation where only one spouse files, the income and expenses of the non-filing spouse is required so that the court, the trustee and creditors can evaluate the household's financial position.

When an individual files a chapter 13 petition, an impartial trustee is appointed to administer the case. 11 U.S.C. § 1302. In some districts, the U.S. trustee or bankruptcy administrator[2] appoints a standing trustee to serve in all chapter 13 cases. 28 U.S.C. § 586(b). The chapter 13 trustee both evaluates the case and serves as a disbursing agent, collecting payments from the debtor and making distributions to creditors. 11 U.S.C. § 1302(b).

Filing the petition under chapter 13 "automatically stays" (stops) most collection actions against the debtor or the debtor's property. 11 U.S.C. § 362. Filing the petition does not, however, stay certain types of actions listed under 11 U.S.C. § 362(b), and the stay may be effective only for a short time in some situations. The stay arises by operation of law and requires no judicial action. As long as the stay is in effect, creditors generally may not initiate or continue lawsuits, wage garnishments, or even make telephone calls demanding payments. The bankruptcy clerk gives notice of the bankruptcy case to all creditors whose names and addresses are provided by the debtor.

Chapter 13 also contains a special automatic stay provision that protects co-debtors. Unless the bankruptcy court authorizes otherwise, a creditor may not seek to collect a "consumer debt" from any individual who is liable along with the debtor. 11 U.S.C. § 1301(a). Consumer debts are those incurred by an individual primarily for a personal, family, or household purpose. 11 U.S.C. § 101(8).

Individuals may use a chapter 13 proceeding to save their home from foreclosure. The automatic stay stops the foreclosure proceeding as soon as the individual files the chapter 13 petition. The individual may then bring the past-due payments current over a reasonable period of time. Nevertheless, the debtor may still lose the home if the mortgage company completes the foreclosure sale under state law before the debtor files the petition.11 U.S.C. § 1322(c). The debtor may also lose the home if he or she fails to make the regular mortgage payments that come due after the chapter 13 filing.

Between 21 and 50 days after the debtor files the chapter 13 petition, the chapter 13 trustee will hold a meeting of creditors. If the U.S. trustee or bankruptcy administrator schedules the meeting at a place that does not have regular U.S. trustee or bankruptcy administrator staffing, the meeting may be held no more than 60 days after the debtor files. Fed. R. Bankr. P. 2003(a). During this meeting, the trustee places the debtor under oath, and both the trustee and creditors may ask questions. The debtor must attend the meeting and answer questions regarding his or her financial affairs and the proposed terms of the plan.11 U.S.C. § 343. If a husband and wife file a joint petition, they both must attend the creditors' meeting and answer questions. In order to preserve their independent judgment, bankruptcy judges are prohibited from attending the creditors' meeting. 11

U.S.C. § 341(c). The parties typically resolve problems with the plan either during or shortly after the creditors' meeting. Generally, the debtor can avoid problems by making sure that the petition and plan are complete and accurate, and by consulting with the trustee prior to the meeting.

In a chapter 13 case, to participate in distributions from the bankruptcy estate, unsecured creditors must file their claims with the court within 90 days after the first date set for the meeting of creditors. Fed. R. Bankr. P. 3002(c). A governmental unit, however, has 180 days from the date the case is filed file a proof of claim.11 U.S.C. § 502(b)(9).

After the meeting of creditors, the debtor, the chapter 13 trustee, and those creditors who wish to attend will come to court for a hearing on the debtor's chapter 13 repayment plan.

THE CHAPTER 13 PLAN AND CONFIRMATION HEARING

Unless the court grants an extension, the debtor must file a repayment plan with the petition or within 14 days after the petition is filed. Fed. R. Bankr. P. 3015. A plan must be submitted for court approval and must provide for payments of fixed amounts to the trustee on a regular basis, typically biweekly or monthly. The trustee then distributes the funds to creditors according to the terms of the plan, which may offer creditors less than full payment on their claims.

There are three types of claims: priority, secured, and unsecured. Priority claims are those granted special status by the bankruptcy law, such as most taxes and the costs of bankruptcy proceeding.[3] Secured claims are those for which the creditor has the right take back certain property (*i.e.*, the collateral) if the debtor does not pay the underlying debt. In contrast to secured claims, unsecured claims are generally those for which the creditor has no special rights to collect against particular property owned by the debtor.

The plan must pay priority claims in full unless a particular priority creditor agrees to different treatment of the claim or, in the case of a domestic support obligation, unless the debtor contributes all "disposable income" - discussed below - to a five-year plan.
11 U.S.C. § 1322(a).

If the debtor wants to keep the collateral securing a particular claim, the plan must provide that the holder of the secured claim receive at least the value of the collateral. If the obligation underlying the secured claim was used to buy the collateral (e.g., a car loan), and the debt was incurred within certain time frames before the bankruptcy filing, the plan must provide for full payment of the debt, not just the value of the collateral (which may be less due to depreciation). Payments to certain secured creditors (*i.e.*, the home mortgage lender), may be made over the original loan repayment schedule (which may be longer than the plan) so long as any arrearage is made up during the plan. The debtor should consult an attorney to determine the proper treatment of secured claims in the plan.

The plan need not pay unsecured claims in full as long it provides that the debtor will pay all projected "disposable income" over an "applicable commitment period," and as long as unsecured creditors receive at least as much under the plan as they would receive if the debtor's assets were liquidated under chapter 7. 11 U.S.C. § 1325. In chapter 13, "disposable income" is income (other than child support payments received by the

debtor) less amounts reasonably necessary for the maintenance or support of the debtor or dependents and less charitable contributions up to 15% of the debtor's gross income. If the debtor operates a business, the definition of disposable income excludes those amounts which are necessary for ordinary operating expenses. 11 U.S.C. § 1325(b)(2)(A) and (B). The "applicable commitment period" depends on the debtor's current monthly income. The applicable commitment period must be three years if current monthly income is less than the state median for a family of the same size - and five years if the current monthly income is greater than a family of the same size. 11 U.S.C. § 1325(d). The plan may be less than the applicable commitment period (three or five years) only if unsecured debt is paid in full over a shorter period.

Within 30 days after filing the bankruptcy case, even if the plan has not yet been approved by the court, the debtor must start making plan payments to the trustee. 11 U.S.C. § 1326(a)(1). If any secured loan payments or lease payments come due before the debtor's plan is confirmed (typically home and automobile payments), the debtor must make adequate protection payments directly to the secured lender or lessor - deducting the amount paid from the amount that would otherwise be paid to the trustee. *Id.*

No later than 45 days after the meeting of creditors, the bankruptcy judge must hold a confirmation hearing and decide whether the plan is feasible and meets the standards for confirmation set forth in the Bankruptcy Code. 11 U.S.C. §§ 1324, 1325. Creditors will receive 28 days' notice of the hearing and may object to confirmation. Fed. R. Bankr. P. 2002(b). While a variety of objections may be made, the most frequent ones are that payments offered under the plan are less than creditors would receive if the debtor's assets were liquidated or that the debtor's plan does not commit all of the debtor's projected disposable income for the three or five year applicable commitment period.

If the court confirms the plan, the chapter 13 trustee will distribute funds received under the plan "as soon as is practicable." 11 U.S.C. § 1326(a)(2). If the court declines to confirm the plan, the debtor may file a modified plan. 11 U.S.C. § 1323. The debtor may also convert the case to a liquidation case under chapter 7.[4] 11 U.S.C. § 1307(a). If the court declines to confirm the plan or the modified plan and instead dismisses the case, the court may authorize the trustee to keep some funds for costs, but the trustee must return all remaining funds to the debtor (other than funds already disbursed or due to creditors). 11 U.S.C. § 1326(a)(2).

Occasionally, a change in circumstances may compromise the debtor's ability to make plan payments. For example, a creditor may object or threaten to object to a plan, or the debtor may inadvertently have failed to list all creditors. In such instances, the plan may be modified either before or after confirmation. 11 U.S.C. §§ 1323, 1329. Modification after confirmation is not limited to an initiative by the debtor, but may be at the request of the trustee or an unsecured creditor. 11 U.S.C. § 1329(a).

MAKING THE PLAN WORK

The provisions of a confirmed plan bind the debtor and each creditor. 11 U.S.C. § 1327. Once the court confirms the plan, the debtor must make the plan succeed. The debtor must make regular payments to the trustee either directly or through payroll deduction, which will require adjustment to living on a fixed

budget for a prolonged period. Furthermore, while confirmation of the plan entitles the debtor to retain property as long as payments are made, the debtor may not incur new debt without consulting the trustee, because additional debt may compromise the debtor's ability to complete the plan. 11 U.S.C. §§ 1305(c), 1322(a)(1), 1327.

A debtor may make plan payments through payroll deductions. This practice increases the likelihood that payments will be made on time and that the debtor will complete the plan. In any event, if the debtor fails to make the payments due under the confirmed plan, the court may dismiss the case or convert it to a liquidation case under chapter 7 of the Bankruptcy Code. 11 U.S.C. § 1307(c). The court may also dismiss or convert the debtor's case if the debtor fails to pay any post-filing domestic support obligations (*i.e.*, child support, alimony), or fails to make required tax filings during the case. 11 U.S.C. §§ 1307(c) and (e), 1308, 521.

THE CHAPTER 13 DISCHARGE

The bankruptcy law regarding the scope of the chapter 13 discharge is complex and has recently undergone major changes. Therefore, debtors should consult competent legal counsel prior to filing regarding the scope of the chapter 13 discharge.

A chapter 13 debtor is entitled to a discharge upon completion of all payments under the chapter 13 plan so long as the debtor: (1) certifies (if applicable) that all domestic support obligations that came due prior to making such certification have been paid; (2) has not received a discharge in a prior case filed within a certain time frame (two years for prior chapter 13 cases and four years for prior chapter 7, 11 and 12 cases); and (3) has completed an approved course in financial management (if the U.S. trustee or bankruptcy administrator for the debtor's district has determined that such courses are available to the debtor). 11 U.S.C. § 1328. The court will not enter the discharge, however, until it determines, after notice and a hearing, that there is no reason to believe there is any pending proceeding that might give rise to a limitation on the debtor's homestead exemption. 11 U.S.C. § 1328(h).

The discharge releases the debtor from all debts provided for by the plan or disallowed (under section 502), with limited exceptions. Creditors provided for in full or in part under the chapter 13 plan may no longer initiate or continue any legal or other action against the debtor to collect the discharged obligations.

As a general rule, the discharge releases the debtor from all debts provided for by the plan or disallowed, with the exception of certain debts referenced in 11 U.S.C. § 1328. Debts not discharged in chapter 13 include certain long term obligations (such as a home mortgage), debts for alimony or child support, certain taxes, debts for most government funded or guaranteed educational loans or benefit overpayments, debts arising from death or personal injury caused by driving while intoxicated or under the influence of drugs, and debts for restitution or a criminal fine included in a sentence on the debtor's conviction of a crime. To the extent that they are not fully paid under the chapter 13 plan, the debtor will still be responsible for these debts after the bankruptcy case has concluded. Debts for money or property obtained by false pretenses, debts for fraud or defalcation while acting in a fiduciary capacity, and debts for restitution or damages awarded in a civil case for willful or malicious actions by the debtor that cause personal injury or death to a person

will be discharged unless a creditor timely files and prevails in an action to have such debts declared nondischargeable. 11 U.S.C. §§ 1328, 523(c); Fed. R. Bankr. P. 4007(c).

The discharge in a chapter 13 case is somewhat broader than in a chapter 7 case. Debts dischargeable in a chapter 13, but not in chapter 7, include debts for willful and malicious injury to property (as opposed to a person), debts incurred to pay nondischargeable tax obligations, and debts arising from property settlements in divorce or separation proceedings. 11 U.S.C. § 1328(a).

THE CHAPTER 13 HARDSHIP DISCHARGE

After confirmation of a plan, circumstances may arise that prevent the debtor from completing the plan. In such situations, the debtor may ask the court to grant a "hardship discharge." 11 U.S.C. § 1328(b). Generally, such a discharge is available only if: (1) the debtor's failure to complete plan payments is due to circumstances beyond the debtor's control and through no fault of the debtor; (2) creditors have received at least as much as they would have received in a chapter 7 liquidation case; and (3) modification of the plan is not possible. Injury or illness that precludes employment sufficient to fund even a modified plan may serve as the basis for a hardship discharge. The hardship discharge is more limited than the discharge described above and does not apply to any debts that are nondischargeable in a chapter 7 case. 11 U.S.C. § 523.

NOTES

1. The "current monthly income" received by the debtor is a defined term in the Bankruptcy Code and means the average monthly income received over the six calendar months before commencement of the bankruptcy case, including regular contributions to household expenses from nondebtors and including income from the debtor's spouse if the petition is a joint petition, but not including social security income or certain payments made because the debtor is the victim of certain crimes. 11 U.S.C. § 101(10A).

2. In North Carolina and Alabama, bankruptcy administrators perform similar functions that U.S. trustees perform in the remaining forty-eight states. The bankruptcy administrator program is administered by the Administrative Office of the United States Courts, while the U.S. trustee program is administered by the Department of Justice. For purposes of this publication, references to U.S. trustees are also applicable to bankruptcy administrators.

3. Section 507 sets forth 10 categories of unsecured claims which Congress has, for public policy reasons, given priority of distribution over other unsecured claims.

4. A fee of $15 is charged for converting a case under chapter 13 to a case under chapter 7.

Chapter 11

Reorganization Under the Bankruptcy Code

BACKGROUND

A case filed under chapter 11 of the United States Bankruptcy Code is frequently referred to as a "reorganization" bankruptcy.

An individual cannot file under chapter 11 or any other chapter if, during the preceding 180 days, a prior bankruptcy petition was dismissed due to the debtor's willful failure to appear before the court or comply with orders of the court, or was voluntarily dismissed after creditors sought relief from the bankruptcy court to recover property upon which they hold liens. 11 U.S.C. §§ 109(g), 362(d)-(e). In addition, no individual may be a debtor under chapter 11 or any chapter of the Bankruptcy Code unless he or she has, within 180 days before filing, received credit counseling from an approved credit counseling agency either in an individual or group briefing. 11 U.S.C. §§ 109, 111. There are exceptions in emergency situations or where the U.S. trustee (or bankruptcy administrator) has determined that there are insufficient approved agencies to provide the required counseling. If a debt management plan is developed during required credit counseling, it must be filed with the court.

HOW CHAPTER 11 WORKS

A chapter 11 case begins with the filing of a petition with the bankruptcy court serving the area where the debtor has a domicile or residence. A petition may be a voluntary petition, which is filed by the debtor, or it may be an involuntary petition, which is filed by creditors that meet certain requirements. 11 U.S.C. §§ 301, 303. A voluntary petition must adhere to the format of Form 1 of the Official Forms prescribed by the Judicial Conference of the United States. Unless the court orders otherwise, the debtor also must file with the court: (1) schedules of assets and liabilities; (2) a schedule of current income and expenditures; (3) a schedule of executory contracts and unexpired leases; and (4) a statement of financial affairs. Fed. R. Bankr. P. 1007(b). If the debtor is an individual (or husband and wife), there are additional document filing requirements. Such debtors must file: a certificate of credit counseling and a copy of any debt repayment plan developed through credit counseling; evidence of payment from employers, if any, received 60 days before filing; a statement of monthly net income and any anticipated increase in income or expenses after filing; and a record of any interest the debtor has in federal or state qualified education or tuition accounts.11 U.S.C. § 521. A husband and wife may file a joint petition or individual petitions. 11 U.S.C. § 302(a). (The Official Forms are not available from the court, but may be purchased at legal stationery stores or downloaded from the internet at: http://www.uscourts.gov/bkforms/index.html.)

The courts are required to charge an $1,000 case filing fee and a $46 miscellaneous administrative fee. The fees must be paid to the clerk of the court upon filing or may, with the court's permission, be paid by individual debtors in installments. 28 U.S.C. § 1930(a); Fed. R. Bankr. P. 1006(b); Bankruptcy Court Miscellaneous Fee Schedule, Item 8. Fed. R. Bankr. P. 1006(b) limits to four the number of installments for the filing fee. The final installment must be paid not later than 120 days after filing the petition. For cause shown, the court may extend the time of any

installment, provided that the last installment is paid not later than 180 days after the filing of the petition. Fed. R. Bankr. P. 1006(b). The $46 administrative fee may be paid in installments in the same manner as the filing fee. If a joint petition is filed, only one filing fee and one administrative fee are charged. Debtors should be aware that failure to pay these fees may result in dismissal of the case. 11 U.S.C. § 1112(b)(10).

The voluntary petition will include standard information concerning the debtor's name(s), social security number or tax identification number, residence, location of principal assets (if a business), the debtor's plan or intention to file a plan, and a request for relief under the appropriate chapter of the Bankruptcy Code. Upon filing a voluntary petition for relief under chapter 11 or, in an involuntary case, the entry of an order for relief, the debtor automatically assumes an additional identity as the "debtor in possession." 11 U.S.C. § 1101. The term refers to a debtor that keeps possession and control of its assets while undergoing a reorganization under chapter 11, without the appointment of a case trustee. A debtor will remain a debtor in possession until the debtor's plan of reorganization is confirmed, the debtor's case is dismissed or converted to chapter 7, or a chapter 11 trustee is appointed. The appointment or election of a trustee occurs only in a small number of cases. Generally, the debtor, as "debtor in possession," operates the business and performs many of the functions that a trustee performs in cases under other chapters. 11 U.S.C. § 1107(a).

Generally, a written disclosure statement and a plan of reorganization must be filed with the court. 11 U.S.C. §§ 1121, 1125. The disclosure statement is a document that must contain information concerning the assets, liabilities, and business affairs of the debtor sufficient to enable a creditor to make an informed judgment about the debtor's plan of reorganization. 11 U.S.C. § 1125. The information required is governed by judicial discretion and the circumstances of the case. In a "small business case" (discussed below) the debtor may not need to file a separate disclosure statement if the court determines that adequate information is contained in the plan. 11 U.S.C. § 1125(f). The contents of the plan must include a classification of claims and must specify how each class of claims will be treated under the plan. 11 U.S.C. § 1123. Creditors whose claims are "impaired," *i.e.*, those whose contractual rights are to be modified or who will be paid less than the full value of their claims under the plan, vote on the plan by ballot. 11 U.S.C. § 1126. After the disclosure statement is approved by the court and the ballots are collected and tallied, the court will conduct a confirmation hearing to determine whether to confirm the plan.11 U.S.C. § 1128.

In the case of individuals, chapter 11 bears some similarities to chapter 13. For example, property of the estate for an individual debtor includes the debtor's earnings and property acquired by the debtor after filing until the case is closed, dismissed or converted; funding of the plan may be from the debtor's future earnings; and the plan cannot be confirmed over a creditor's objection without committing all of the debtor's disposable income over five years unless the plan pays the claim in full, with interest, over a shorter period of time. 11 U.S.C. §§ 1115, 1123(a)(8), 1129(a)(15).

THE CHAPTER 11 DEBTOR IN POSSESSION

Chapter 11 is typically used to reorganize a business, which may be a corporation, sole proprietorship, or partnership. A corporation exists separate and apart from its owners, the stockholders. The chapter 11 bankruptcy case of a corporation (corporation as debtor) does not put the personal assets of the stockholders at risk other than the value of their investment in the company's stock. A sole proprietorship (owner as debtor), on the other hand, does not have an identity separate and distinct from its owner(s). Accordingly, a bankruptcy case involving a sole proprietorship includes both the business and personal assets of the owners-debtors. Like a corporation, a partnership exists separate and apart from its partners. In a partnership bankruptcy case (partnership as debtor), however, the partners' personal assets may, in some cases, be used to pay creditors in the bankruptcy case or the partners, themselves, may be forced to file for bankruptcy protection.

Section 1107 of the Bankruptcy Code places the debtor in possession in the position of a fiduciary, with the rights and powers of a chapter 11 trustee, and it requires the debtor to perform of all but the investigative functions and duties of a trustee. These duties, set forth in the Bankruptcy Code and Federal Rules of Bankruptcy Procedure, include accounting for property, examining and objecting to claims, and filing informational reports as required by the court and the U.S. trustee or bankruptcy administrator (discussed below), such as monthly operating reports. 11 U.S.C. §§ 1106, 1107; Fed. R. Bankr. P. 2015(a). The debtor in possession also has many of the other powers and duties of a trustee, including the right, with the court's approval, to employ attorneys, accountants, appraisers, auctioneers, or other professional persons to assist the debtor during its bankruptcy case. Other responsibilities include filing tax returns and reports which are either necessary or ordered by the court after confirmation, such as a final accounting. The U.S. trustee is responsible for monitoring the compliance of the debtor in possession with the reporting requirements.

Railroad reorganizations have specific requirements under subsection IV of chapter 11, which will not be addressed here. In addition, stock and commodity brokers are prohibited from filing under chapter 11 and are restricted to chapter 7. 11 U.S.C. § 109(d).

THE U.S. TRUSTEE OR BANKRUPTCY ADMINISTRATOR

The U.S. trustee plays a major role in monitoring the progress of a chapter 11 case and supervising its administration. The U.S. trustee is responsible for monitoring the debtor in possession's operation of the business and the submission of operating reports and fees. Additionally, the U.S. trustee monitors applications for compensation and reimbursement by professionals, plans and disclosure statements filed with the court, and creditors' committees. The U.S. trustee conducts a meeting of the creditors, often referred to as the "section 341 meeting," in a chapter 11 case. 11 U.S.C. § 341. The U.S. trustee and creditors may question the debtor under oath at the section 341 meeting concerning the debtor's acts, conduct, property, and the administration of the case.

The U.S. trustee also imposes certain requirements on the debtor in possession concerning matters such as reporting its monthly income and operating expenses, establishing new bank accounts, and paying

current employee withholding and other taxes. By law, the debtor in possession must pay a quarterly fee to the U.S. trustee for each quarter of a year until the case is converted or dismissed. 28 U.S.C. § 1930(a)(6). The amount of the fee, which may range from $250 to $10,000, depends on the amount of the debtor's disbursements during each quarter. Should a debtor in possession fail to comply with the reporting requirements of the U.S. trustee or orders of the bankruptcy court, or fail to take the appropriate steps to bring the case to confirmation, the U.S. trustee may file a motion with the court to have the debtor's chapter 11 case converted to another chapter of the Bankruptcy Code or to have the case dismissed.

In North Carolina and Alabama, bankruptcy administrators perform similar functions that U.S. trustees perform in the remaining forty-eight states. The bankruptcy administrator program is administered by the Administrative Office of the United States Courts, while the U.S. trustee program is administered by the Department of Justice. For purposes of this publication, references to U.S. trustees are also applicable to bankruptcy administrators.

CREDITORS' COMMITTEES

Creditors' committees can play a major role in chapter 11 cases. The committee is appointed by the U.S. trustee and ordinarily consists of unsecured creditors who hold the seven largest unsecured claims against the debtor. 11 U.S.C. § 1102. Among other things, the committee: consults with the debtor in possession on administration of the case; investigates the debtor's conduct and operation of the business; and participates in formulating a plan. 11 U.S.C. § 1103. A creditors' committee may, with the court's approval, hire an attorney or other professionals to assist in the performance of the committee's duties. A creditors' committee can be an important safeguard to the proper management of the business by the debtor in possession.

THE SMALL BUSINESS CASE AND THE SMALL BUSINESS DEBTOR

In some smaller cases the U.S. trustee may be unable to find creditors willing to serve on a creditors' committee, or the committee may not be actively involved in the case. The Bankruptcy Code addresses this issue by treating a "small business case" somewhat differently than a regular bankruptcy case. A small business case is defined as a case with a "small business debtor." 11 U.S.C. § 101(51C). Determination of whether a debtor is a "small business debtor" requires application of a two-part test. First, the debtor must be engaged in commercial or business activities (other than primarily owning or operating real property) with total non-contingent liquidated secured and unsecured debts of $2,343,300 or less. Second, the debtor's case must be one in which the U.S. trustee has not appointed a creditors' committee, or the court has determined the creditors' committee is insufficiently active and representative to provide oversight of the debtor. 11 U.S.C. § 101(51D).

In a small business case, the debtor in possession must, among other things, attach the most recently prepared balance sheet, statement of operations, cash-flow statement and most recently filed tax return to the petition or provide a statement under oath explaining the absence of such documents and must attend court and the U.S. trustee meeting through senior management personnel and counsel. The small business debtor must make

ongoing filings with the court concerning its profitability and projected cash receipts and disbursements, and must report whether it is in compliance with the Bankruptcy Code and the Federal Rules of Bankruptcy Procedure and whether it has paid its taxes and filed its tax returns. 11 U.S.C. §§ 308, 1116.

In contrast to other chapter 11 debtors, the small business debtor is subject to additional oversight by the U.S. trustee. Early in the case, the small business debtor must attend an "initial interview" with the U.S. trustee at which time the U.S. trustee will evaluate the debtor's viability, inquire about the debtor's business plan, and explain certain debtor obligations including the debtor's responsibility to file various reports. 28 U.S.C. § 586(a)(7). The U.S. trustee will also monitor the activities of the small business debtor during the case to identify as promptly as possible whether the debtor will be unable to confirm a plan.

Because certain filing deadlines are different and extensions are more difficult to obtain, a case designated as a small business case normally proceeds more quickly than other chapter 11 cases. For example, only the debtor may file a plan during the first 180 days of a small business case. 11 U.S.C. § 1121(e). This "exclusivity period" may be extended by the court, but only to 300 days, and only if the debtor demonstrates by a preponderance of the evidence that the court will confirm a plan within a reasonable period of time. When the case is not a small business case, however, the court may extend the exclusivity period "for cause" up to 18 months.

THE SINGLE ASSET REAL ESTATE DEBTOR

Single asset real estate debtors are subject to special provisions of the Bankruptcy Code. The term "single asset real estate" is defined as "a single property or project, other than residential real property with fewer than four residential units, which generates substantially all of the gross income of a debtor who is not a family farmer and on which no substantial business is being conducted by a debtor other than the business of operating the real property and activities incidental." 11 U.S.C. § 101(51B). The Bankruptcy Code provides circumstances under which creditors of a single asset real estate debtor may obtain relief from the automatic stay which are not available to creditors in ordinary bankruptcy cases. 11 U.S.C. § 362(d). On request of a creditor with a claim secured by the single asset real estate and after notice and a hearing, the court will grant relief from the automatic stay to the creditor unless the debtor files a feasible plan of reorganization or begins making interest payments to the creditor within 90 days from the date of the filing of the case, or within 30 days of the court's determination that the case is a single asset real estate case. The interest payments must be equal to the non-default contract interest rate on the value of the creditor's interest in the real estate. 11 U.S.C. § 362(d)(3).

APPOINTMENT OR ELECTION OF A CASE TRUSTEE

Although the appointment of a case trustee is a rarity in a chapter 11 case, a party in interest or the U.S. trustee can request the appointment of a case trustee or examiner at any time prior to confirmation in a chapter 11 case. The court, on motion by a party in interest or the U.S. trustee and after notice and hearing, shall order the appointment of a case trustee for cause, including fraud, dishonesty, incompetence, or gross mismanagement, or if

such an appointment is in the interest of creditors, any equity security holders, and other interests of the estate. 11 U.S.C. § 1104(a). Moreover, the U.S. trustee is required to move for appointment of a trustee if there are reasonable grounds to believe that any of the parties in control of the debtor "participated in actual fraud, dishonesty or criminal conduct in the management of the debtor or the debtor's financial reporting." 11 U.S.C. § 1104(e). The trustee is appointed by the U.S. trustee, after consultation with parties in interest and subject to the court's approval. Fed. R. Bankr. P. 2007.1. Alternatively, a trustee in a case may be elected if a party in interest requests the election of a trustee within 30 days after the court orders the appointment of a trustee. In that instance, the U.S. trustee convenes a meeting of creditors for the purpose of electing a person to serve as trustee in the case. 11 U.S.C. § 1104(b).

The case trustee is responsible for management of the property of the estate, operation of the debtor's business, and, if appropriate, the filing of a plan of reorganization. Section 1106 of the Bankruptcy Code requires the trustee to file a plan "as soon as practicable" or, alternatively, to file a report explaining why a plan will not be filed or to recommend that the case be converted to another chapter or dismissed. 11 U.S.C. § 1106(a)(5).

Upon the request of a party in interest or the U.S. trustee, the court may terminate the trustee's appointment and restore the debtor in possession to management of bankruptcy estate at any time before confirmation.11 U.S.C. § 1105.

THE ROLE OF AN EXAMINER

The appointment of an examiner in a chapter 11 case is rare. The role of an examiner is generally more limited than that of a trustee. The examiner is authorized to perform the investigatory functions of the trustee and is required to file a statement of any investigation conducted. If ordered to do so by the court, however, an examiner may carry out any other duties of a trustee that the court orders the debtor in possession not to perform. 11 U.S.C. § 1106. Each court has the authority to determine the duties of an examiner in each particular case. In some cases, the examiner may file a plan of reorganization, negotiate or help the parties negotiate, or review the debtor's schedules to determine whether some of the claims are improperly categorized. Sometimes, the examiner may be directed to determine if objections to any proofs of claim should be filed or whether causes of action have sufficient merit so that further legal action should be taken. The examiner may not subsequently serve as a trustee in the case. 11 U.S.C. § 321.

THE AUTOMATIC STAY

The automatic stay provides a period of time in which all judgments, collection activities, foreclosures, and repossessions of property are suspended and may not be pursued by the creditors on any debt or claim that arose before the filing of the bankruptcy petition. As with cases under other chapters of the Bankruptcy Code, a stay of creditor actions against the chapter 11 debtor automatically goes into effect when the bankruptcy petition is filed. 11 U.S.C. § 362(a). The filing of a petition, however, does not operate as a stay for certain types of actions listed under 11 U.S.C. § 362(b). The stay provides a breathing spell for the debtor, during which negotiations can take place to try to resolve

the difficulties in the debtor's financial situation.

Under specific circumstances, the secured creditor can obtain an order from the court granting relief from the automatic stay. For example, when the debtor has no equity in the property and the property is not necessary for an effective reorganization, the secured creditor can seek an order of the court lifting the stay to permit the creditor to foreclose on the property, sell it, and apply the proceeds to the debt. 11 U.S.C. § 362(d).

The Bankruptcy Code permits applications for fees to be made by certain professionals during the case. Thus, a trustee, a debtor's attorney, or any professional person appointed by the court may apply to the court at intervals of 120 days for interim compensation and reimbursement payments. In very large cases with extensive legal work, the court may permit more frequent applications. Although professional fees may be paid if authorized by the court, the debtor cannot make payments to professional creditors on prepetition obligations, *i.e.*, obligations which arose before the filing of the bankruptcy petition. The ordinary expenses of the ongoing business, however, continue to be paid.

WHO CAN FILE A PLAN

The debtor (unless a "small business debtor") has a 120-day period during which it has an exclusive right to file a plan. 11 U.S.C. § 1121(b). This exclusivity period may be extended or reduced by the court. But, in no event, may the exclusivity period, including all extensions, be longer than 18 months. 11 U.S.C. § 1121(d). After the exclusivity period has expired, a creditor or the case trustee may file a competing plan. The U.S. trustee may not file a plan. 11 U.S.C. § 307.

A chapter 11 case may continue for many years unless the court, the U.S. trustee, the committee, or another party in interest acts to ensure the case's timely resolution. The creditors' right to file a competing plan provides incentive for the debtor to file a plan within the exclusivity period and acts as a check on excessive delay in the case.

AVOIDABLE TRANSFERS

The debtor in possession or the trustee, as the case may be, has what are called "avoiding" powers. These powers may be used to undo a transfer of money or property made during a certain period of time before the filing of the bankruptcy petition. By avoiding a particular transfer of property, the debtor in possession can cancel the transaction and force the return or "disgorgement" of the payments or property, which then are available to pay all creditors. Generally, and subject to various defenses, the power to avoid transfers is effective against transfers made by the debtor within 90 days before filing the petition. But transfers to "insiders" (*i.e.*, relatives, general partners, and directors or officers of the debtor) made up to a year before filing may be avoided. 11 U.S.C. §§ 101(31), 101(54), 547, 548. In addition, under 11 U.S.C. § 544, the trustee is authorized to avoid transfers under applicable state law, which often provides for longer time periods. Avoiding powers prevent unfair prepetition payments to one creditor at the expense of all other creditors.

CASH COLLATERAL, ADEQUATE PROTECTION, AND OPERATING CAPITAL

Although the preparation, confirmation, and implementation of a plan of reorganization is at the heart of a chapter 11 case, other issues may arise that must be addressed by the debtor in possession. The debtor in possession may use, sell, or lease property of the estate in the ordinary course of its business, without prior approval, unless the court orders otherwise. 11 U.S.C. § 363(c). If the intended sale or use is outside the ordinary course of its business, the debtor must obtain permission from the court.

A debtor in possession may not use "cash collateral" without the consent of the secured party or authorization by the court, which must first examine whether the interest of the secured party is adequately protected. 11 U.S.C. § 363. Section 363 defines "cash collateral" as cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents, whenever acquired, in which the estate and an entity other than the estate have an interest. It includes the proceeds, products, offspring, rents, or profits of property and the fees, charges, accounts or payments for the use or occupancy of rooms and other public facilities in hotels, motels, or other lodging properties subject to a creditor's security interest.

When "cash collateral" is used (spent), the secured creditors are entitled to receive additional protection under section 363 of the Bankruptcy Code. The debtor in possession must file a motion requesting an order from the court authorizing the use of the cash collateral. Pending consent of the secured creditor or court authorization for the debtor in possession's use of cash collateral, the debtor in possession must segregate and account for all cash collateral in its possession. 11 U.S.C. § 363(c)(4). A party with an interest in property being used by the debtor may request that the court prohibit or condition this use to the extent necessary to provide "adequate protection" to the creditor.

Adequate protection may be required to protect the value of the creditor's interest in the property being used by the debtor in possession. This is especially important when there is a decrease in value of the property. The debtor may make periodic or lump sum cash payments, or provide an additional or replacement lien that will result in the creditor's property interest being adequately protected. 11 U.S.C. § 361.

When a chapter 11 debtor needs operating capital, it may be able to obtain it from a lender by giving the lender a court-approved "superpriority" over other unsecured creditors or a lien on property of the estate. 11 U.S.C. § 364.

MOTIONS

Before confirmation of a plan, several activities may take place in a chapter 11 case. Continued operation of the debtor's business may lead to the filing of a number of contested motions. The most common are those seeking relief from the automatic stay, the use of cash collateral, or to obtain credit. There may also be litigation over executory (*i.e.*, unfulfilled) contracts and unexpired leases and the assumption or rejection of those executory contracts and unexpired leases by the debtor in possession. 11 U.S.C. § 365. Delays in formulating, filing, and obtaining confirmation of a plan often prompt creditors to file motions for relief from stay, to convert

the case to chapter 7, or to dismiss the case altogether.

ADVERSARY PROCEEDINGS

Frequently, the debtor in possession will institute a lawsuit, known as an adversary proceeding, to recover money or property for the estate. Adversary proceedings may take the form of lien avoidance actions, actions to avoid preferences, actions to avoid fraudulent transfers, or actions to avoid post-petition transfers. These proceedings are governed by Part VII of the Federal Rules of Bankruptcy Procedure. At times, a creditors' committee may be authorized by the bankruptcy court to pursue these actions against insiders of the debtor if the plan provides for the committee to do so or if the debtor has refused a demand to do so. Creditors may also initiate adversary proceedings by filing complaints to determine the validity or priority of a lien, revoke an order confirming a plan, determine the dischargeability of a debt, obtain an injunction, or subordinate a claim of another creditor.

CLAIMS

The Bankruptcy Code defines a claim as: (1) a right to payment; (2) or a right to an equitable remedy for a failure of performance if the breach gives rise to a right to payment. 11 U.S.C. § 101(5). Generally, any creditor whose claim is not scheduled (*i.e.*, listed by the debtor on the debtor's schedules) or is scheduled as disputed, contingent, or unliquidated must file a proof of claim (and attach evidence documenting the claim) in order to be treated as a creditor for purposes of voting on the plan and distribution under it. Fed. R. Bankr. P. 3003(c)(2). But filing a proof of claim is not necessary if the creditor's claim is scheduled (but is not listed as disputed, contingent, or unliquidated by the debtor) because the debtor's schedules are deemed to constitute evidence of the validity and amount of those claims. 11 U.S.C. § 1111. If a scheduled creditor chooses to file a claim, a properly filed proof of claim supersedes any scheduling of that claim. Fed. R. Bankr. P. 3003(c)(4). It is the responsibility of the creditor to determine whether the claim is accurately listed on the debtor's schedules. The debtor must provide notification to those creditors whose names are added and whose claims are listed as a result of an amendment to the schedules. The notification also should advise such creditors of their right to file proofs of claim and that their failure to do so may prevent them from voting upon the debtor's plan of reorganization or participating in any distribution under that plan. When a debtor amends the schedule of liabilities to add a creditor or change the status of any claims to disputed, contingent, or unliquidated, the debtor must provide notice of the amendment to any entity affected. Fed. R. Bankr. P. 1009(a).

EQUITY SECURITY HOLDERS

An equity security holder is a holder of an equity security of the debtor. Examples of an equity security are a share in a corporation, an interest of a limited partner in a limited partnership, or a right to purchase, sell, or subscribe to a share, security, or interest of a share in a corporation or an interest in a limited partnership. 11 U.S.C. § 101(16), (17). An equity security holder may vote on the plan of reorganization and may file a proof of interest, rather than a proof of claim. A proof of interest is deemed filed for any interest that appears in the debtor's schedules, unless it is scheduled as disputed, contingent, or unliquidated. 11 U.S.C. § 1111. An equity security holder whose interest is not scheduled

or scheduled as disputed, contingent, or unliquidated must file a proof of interest in order to be treated as a creditor for purposes of voting on the plan and distribution under it. Fed. R. Bankr. P. 3003(c)(2). A properly filed proof of interest supersedes any scheduling of that interest. Fed. R. Bankr. P. 3003(c)(4). Generally, most of the provisions that apply to proofs of claim, as discussed above, are also applicable to proofs of interest.

CONVERSION OR DISMISSAL

A debtor in a case under chapter 11 has a one-time absolute right to convert the chapter 11 case to a case under chapter 7 unless: (1) the debtor is not a debtor in possession; (2) the case originally was commenced as an involuntary case under chapter 11; or (3) the case was converted to a case under chapter 11 other than at the debtor's request. 11 U.S.C. § 1112(a). A debtor in a chapter 11 case does not have an absolute right to have the case dismissed upon request.

A party in interest may file a motion to dismiss or convert a chapter 11 case to a chapter 7 case "for cause." Generally, if cause is established after notice and hearing, the court must convert or dismiss the case (whichever is in the best interests of creditors and the estate) unless it specifically finds that the requested conversion or dismissal is not in the best interest of creditors and the estate. 11 U.S.C. § 1112(b). Alternatively, the court may decide that appointment of a chapter 11 trustee or an examiner is in the best interests of creditors and the estate. 11 U.S.C. § 1104(a)(3). Section 1112(b)(4) of the Bankruptcy Code sets forth numerous examples of cause that would support dismissal or conversion. For example, the moving party may establish cause by showing that there is substantial or continuing loss to the estate and the absence of a reasonable likelihood of rehabilitation; gross mismanagement of the estate; failure to maintain insurance that poses a risk to the estate or the public; or unauthorized use of cash collateral that is substantially harmful to a creditor.

Cause for dismissal or conversion also includes an unexcused failure to timely comply with reporting and filing requirements; failure to attend the meeting of creditors or attend a Fed. R. Bankr. P. 2004 examination without good cause; failure to timely provide information to the U.S. trustee; and failure to timely pay post-petition taxes or timely file post-petition returns. Additionally, failure to file a disclosure statement or to file and confirm a plan within the time fixed by the Bankruptcy Code or order of the court; inability to effectuate a plan; denial or revocation of confirmation; inability to consummate a confirmed plan represent "cause" for dismissal under the statute. In an individual case, failure of the debtor to pay post-petition domestic support obligations constitutes "cause" for dismissal or conversion.

Section 1112(c) of the Bankruptcy Code provides an important exception to the conversion process in a chapter 11 case. Under this provision, the court is prohibited from converting a case involving a farmer or charitable institution to a liquidation case under chapter 7 unless the debtor requests the conversion.

THE DISCLOSURE STATEMENT

Generally, the debtor (or any plan proponent) must file and get court approval of a written disclosure statement before there can be a vote on the plan of reorganization. The

disclosure statement must provide "adequate information" concerning the affairs of the debtor to enable the holder of a claim or interest to make an informed judgment about the plan. 11 U.S.C. § 1125. In a small business case, however, the court may determine that the plan itself contains adequate information and that a separate disclosure statement is unnecessary. 11 U.S.C. § 1125(f). After the disclosure statement is filed, the court must hold a hearing to determine whether the disclosure statement should be approved. Acceptance or rejection of a plan usually cannot be solicited until the court has first approved the written disclosure statement. 11 U.S.C. § 1125(b). An exception to this rule exists if the initial solicitation of the party occurred before the bankruptcy filing, as would be the case in so-called "prepackaged" bankruptcy plans (*i.e.*, where the debtor negotiates a plan with significant creditor constituencies before filing for bankruptcy). Continued post-filing solicitation of such parties is not prohibited. After the court approves the disclosure statement, the debtor or proponent of a plan can begin to solicit acceptances of the plan, and creditors may also solicit rejections of the plan.

Upon approval of a disclosure statement, the plan proponent must mail the following to the U.S. trustee and all creditors and equity security holders: (1) the plan, or a court approved summary of the plan; (2) the disclosure statement approved by the court; (3) notice of the time within which acceptances and rejections of the plan may be filed; and (4) such other information as the court may direct, including any opinion of the court approving the disclosure statement or a court-approved summary of the opinion. Fed. R. Bankr. P. 3017(d). In addition, the debtor must mail to the creditors and equity security holders entitled to vote on the plan or plans: (1) notice of the time fixed for filing objections; (2) notice of the date and time for the hearing on confirmation of the plan; and (3) a ballot for accepting or rejecting the plan and, if appropriate, a designation for the creditors to identify their preference among competing plans. *Id.* But in a small business case, the court may conditionally approve a disclosure statement subject to final approval after notice and a combined disclosure statement/plan confirmation hearing. 11 U.S.C. § 1125(f).

ACCEPTANCE OF THE PLAN OF REORGANIZATION

As noted earlier, only the debtor may file a plan of reorganization during the first 120-day period after the petition is filed (or after entry of the order for relief, if an involuntary petition was filed). The court may grant extension of this exclusive period up to 18 months after the petition date. In addition, the debtor has 180 days after the petition date or entry of the order for relief to obtain acceptances of its plan. 11 U.S.C. § 1121. The court may extend (up to 20 months) or reduce this acceptance exclusive period for cause. 11 U.S.C. § 1121(d). In practice, debtors typically seek extensions of both the plan filing and plan acceptance deadlines at the same time so that any order sought from the court allows the debtor two months to seek acceptances after filing a plan before any competing plan can be filed.

If the exclusive period expires before the debtor has filed and obtained acceptance of a plan, other parties in interest in a case, such as the creditors' committee or a creditor, may file a plan. Such a plan may compete with a plan filed by another party in interest or by the debtor. If a trustee is appointed, the trustee must file a plan, a report explaining why the

trustee will not file a plan, or a recommendation for conversion or dismissal of the case. 11 U.S.C. § 1106(a)(5). A proponent of a plan is subject to the same requirements as the debtor with respect to disclosure and solicitation.

In a chapter 11 case, a liquidating plan is permissible. Such a plan often allows the debtor in possession to liquidate the business under more economically advantageous circumstances than a chapter 7 liquidation. It also permits the creditors to take a more active role in fashioning the liquidation of the assets and the distribution of the proceeds than in a chapter 7 case.

Section 1123(a) of the Bankruptcy Code lists the mandatory provisions of a chapter 11 plan, and section 1123(b) lists the discretionary provisions. Section 1123(a)(1) provides that a chapter 11 plan must designate classes of claims and interests for treatment under the reorganization. Generally, a plan will classify claim holders as secured creditors, unsecured creditors entitled to priority, general unsecured creditors, and equity security holders.

Under section 1126(c) of the Bankruptcy Code, an entire class of claims is deemed to accept a plan if the plan is accepted by creditors that hold at least two-thirds in amount and more than one-half in number of the allowed claims in the class. Under section 1129(a)(10), if there are impaired classes of claims, the court cannot confirm a plan unless it has been accepted by at least one class of non-insiders who hold impaired claims (*i.e.*, claims that are not going to be paid completely or in which some legal, equitable, or contractual right is altered). Moreover, under section 1126(f), holders of unimpaired claims are deemed to have accepted the plan.

Under section 1127(a) of the Bankruptcy Code, the plan proponent may modify the plan at any time before confirmation, but the plan as modified must meet all the requirements of chapter 11. When there is a proposed modification after balloting has been conducted, and the court finds after a hearing that the proposed modification does not adversely affect the treatment of any creditor who has not accepted the modification in writing, the modification is deemed to have been accepted by all creditors who previously accepted the plan. Fed. R. Bankr. P. 3019. If it is determined that the proposed modification does have an adverse effect on the claims of non-consenting creditors, then another balloting must take place.

Because more than one plan may be submitted to the creditors for approval, every proposed plan and modification must be dated and identified with the name of the entity or entities submitting the plan or modification. Fed. R. Bankr. P. 3016(b). When competing plans are presented that meet the requirements for confirmation, the court must consider the preferences of the creditors and equity security holders in determining which plan to confirm.

Any party in interest may file an objection to confirmation of a plan. The Bankruptcy Code requires the court, after notice, to hold a hearing on confirmation of a plan. If no objection to confirmation has been timely filed, the Bankruptcy Code allows the court to determine whether the plan has been proposed in good faith and according to law. Fed. R. Bankr. P. 3020(b)(2). Before confirmation can be granted, the court must be satisfied that there has been compliance with all the other requirements of confirmation set forth in section 1129 of the Bankruptcy Code, even in the absence of any objections. In order to

confirm the plan, the court must find, among other things, that: (1) the plan is feasible; (2) it is proposed in good faith; and (3) the plan and the proponent of the plan are in compliance with the Bankruptcy Code. In order to satisfy the feasibility requirement, the court must find that confirmation of the plan is not likely to be followed by liquidation (unless the plan is a liquidating plan) or the need for further financial reorganization.

THE DISCHARGE

Section 1141(d)(1) generally provides that confirmation of a plan discharges a debtor from any debt that arose before the date of confirmation. After the plan is confirmed, the debtor is required to make plan payments and is bound by the provisions of the plan of reorganization. The confirmed plan creates new contractual rights, replacing or superseding pre-bankruptcy contracts.

There are, of course, exceptions to the general rule that an order confirming a plan operates as a discharge. Confirmation of a plan of reorganization discharges any type of debtor – corporation, partnership, or individual – from most types of prepetition debts. It does not, however, discharge an individual debtor from any debt made nondischargeable by section 523 of the Bankruptcy Code.[1] Moreover, except in limited circumstances, a discharge is not available to an individual debtor unless and until all payments have been made under the plan. 11 U.S.C. § 1141(d)(5). Confirmation does not discharge the debtor if the plan is a liquidation plan, as opposed to one of reorganization, unless the debtor is an individual. When the debtor is an individual, confirmation of a liquidation plan will result in a discharge (after plan payments are made) unless grounds would exist for denying the debtor a discharge if the case were proceeding under chapter 7 instead of chapter 11. 11 U.S.C. §§ 727(a), 1141(d).

POSTCONFIRMATION MODIFICATION OF THE PLAN

At any time after confirmation and before "substantial consummation" of a plan, the proponent of a plan may modify the plan if the modified plan would meet certain Bankruptcy Code requirements. 11 U.S.C. § 1127(b). This should be distinguished from preconfirmation modification of the plan. A modified postconfirmation plan does not automatically become the plan. A modified postconfirmation plan in a chapter 11 case becomes the plan only "if circumstances warrant such modification" and the court, after notice and hearing, confirms the plan as modified. If the debtor is an individual, the plan may be modified postconfirmation upon the request of the debtor, the trustee, the U.S. trustee, or the holder of an allowed unsecured claim to make adjustments to payments due under the plan. 11 U.S.C. § 1127(e).

POSTCONFIRMATION ADMINISTRATION

Notwithstanding the entry of the confirmation order, the court has the authority to issue any other order necessary to administer the estate. Fed. R. Bankr. P. 3020(d). This authority would include the postconfirmation determination of objections to claims or adversary proceedings, which must be resolved before a plan can be fully consummated. Sections 1106(a)(7) and 1107(a) of the Bankruptcy Code require a debtor in possession or a trustee to report on the progress made in implementing a plan after confirmation. A chapter 11 trustee or debtor in possession has a number of responsibilities to perform after confirmation,

including consummating the plan, reporting on the status of consummation, and applying for a final decree.

REVOCATION OF THE CONFIRMATION ORDER

Revocation of the confirmation order is an undoing or cancellation of the confirmation of a plan. A request for revocation of confirmation, if made at all, must be made by a party in interest within 180 days of confirmation. The court, after notice and hearing, may revoke a confirmation order "if and only if the [confirmation] order was procured by fraud." 11 U.S.C. § 1144.

THE FINAL DECREE

A final decree closing the case must be entered after the estate has been "fully administered." Fed. R. Bankr. P. 3022. Local bankruptcy court policies generally determine when the final decree is entered and the case closed.

NOTES

1. Debts not discharged include debts for alimony and child support, certain taxes, debts for certain educational benefit overpayments or loans made or guaranteed by a governmental unit, debts for willful and malicious injury by the debtor to another entity or to the property of another entity, debts for death or personal injury caused by the debtor's operation of a motor vehicle while the debtor was intoxicated from alcohol or other substances, and debts for certain criminal restitution orders.11 U.S.C. § 523(a). The debtor will continue to be liable for these types of debts to the extent that they are not paid in the chapter 11 case. Debts for money or property obtained by false pretenses, debts for fraud or defalcation while acting in a fiduciary capacity, and debts for willful and malicious injury by the debtor to another entity or to the property of another entity will be discharged unless a creditor timely files and prevails in an action to have such debts declared nondischargeable. 11 U.S.C. § 523(c); Fed. R. Bankr. P. 4007(c).

Chapter 12

Family Farmer or Family Fisherman Bankruptcy

BACKGROUND

Chapter 12 is designed for "family farmers" or "family fishermen" with "regular annual income." It enables financially distressed family farmers and fishermen to propose and carry out a plan to repay all or part of their debts. Under chapter 12, debtors propose a repayment plan to make installments to creditors over three to five years. Generally, the plan must provide for payments over three years unless the court approves a longer period "for cause." But unless the plan proposes to pay 100% of domestic support claims (*i.e.*, child support and alimony) if any exist, it must be for five years and must include all of the debtor's disposable income. In no case may a plan provide for payments over a period longer than five years. 11 U.S.C. § 1222(b)-(c).

In tailoring bankruptcy law to meet the economic realities of family farming and the family fisherman, chapter 12 eliminates many of the barriers such debtors would face if seeking to reorganize under either chapter 11 or 13 of the Bankruptcy Code. For example, chapter 12 is more streamlined, less complicated, and less expensive than chapter 11, which is better suited to large corporate reorganizations. In addition, few family farmers or fishermen find chapter 13 to be advantageous because it is designed for wage earners who have smaller debts than those facing family farmers. In chapter 12, Congress sought to combine the features of the Bankruptcy Code which can provide a framework for successful family farmer and fisherman reorganizations.

The Bankruptcy Code provides that only a family farmer or family fisherman with "regular annual income" may file a petition for relief under chapter 12. 11 U.S.C. §§ 101(18), 101(19A), 109(f). The purpose of this requirement is to ensure that the debtor's annual income is sufficiently stable and regular to permit the debtor to make payments under a chapter 12 plan. But chapter 12 makes allowance for situations in which family farmers or fishermen have income that is seasonal in nature. Relief under chapter 12 is voluntary, and only the debtor may file a petition under the chapter.

Under the Bankruptcy Code, "family farmers" and "family fishermen" fall into two categories: (1) an individual or individual and spouse and (2) a corporation or partnership. Farmers or fishermen falling into the first category must meet each of the following four criteria as of the date the petition is filed in order to qualify for relief under chapter 12:

1. The individual or husband and wife must be engaged in a farming operation or a commercial fishing operation.

2. The total debts (secured and unsecured) of the operation must not exceed $3,792,650 (if a farming operation) or $1,757,475 (if a commercial fishing operation).

3. If a family farmer, at least 50%, and if family fisherman at least 80%, of the total debts that are fixed in amount (exclusive of debt for the debtor's home) must be related to the farming or commercial fishing operation.

4. More than 50% of the gross income of the individual or the husband and wife for the

preceding tax year (or, for family farmers only, for each of the 2nd and 3rd prior tax years) must have come from the farming or commercial fishing operation.

In order for a corporation or partnership to fall within the second category of debtors eligible to file as family farmers or family fishermen, the corporation or partnership must meet each of the following criteria as of the date of the filing of the petition:

1. More than one-half the outstanding stock or equity in the corporation or partnership must be owned by one family or by one family and its relatives.

2. The family or the family and its relatives must conduct the farming or commercial fishing operation.

3. More than 80% of the value of the corporate or partnership assets must be related to the farming or fishing operation.

4. The total indebtedness of the corporation or partnership must not exceed $3,792,650 (if a farming operation) or $1,757,475 (if a commercial fishing operation).

5. At least 50% for a farming operation or 80% for a fishing operation of the corporation's or partnership's total debts which are fixed in amount (exclusive of debt for one home occupied by a shareholder) must be related to the farming or fishing operation.

6. If the corporation issues stock, the stock cannot be publicly traded.

A debtor cannot file under chapter 12 (or any other chapter) if during the preceding 180 days a prior bankruptcy petition was dismissed due to the debtor's willful failure to appear before the court or comply with orders of the court or was voluntarily dismissed after creditors sought relief from the bankruptcy court to recover property upon which they hold liens. 11 U.S.C. §§ 109(g), 362(d) and (e). In addition, no individual may be a debtor under chapter 12 or any chapter of the Bankruptcy Code unless he or she has, within 180 days before filing, received credit counseling from an approved credit counseling agency either in an individual or group briefing. 11 U.S.C. §§ 109, 111. There are exceptions in emergency situations or where the U.S. trustee (or bankruptcy administrator)[1] has determined that there are insufficient approved agencies to provide the required counseling. If a debt management plan is developed during required credit counseling, it must be filed with the court.

HOW CHAPTER 12 WORKS

A chapter 12 case begins by filing a petition with the bankruptcy court serving the area where the individual lives or where the corporation or partnership debtor has its principal place of business or principal assets. Unless the court orders otherwise, the debtor also shall file with the court (1) schedules of assets and liabilities, (2) a schedule of current income and expenditures, (3) a schedule of executory contracts and unexpired leases, and (4) a statement of financial affairs. Fed. R. Bankr. P. 1007(b). A husband and wife may file a joint petition or individual petitions. 11 U.S.C. § 302(a). (The Official Forms may be purchased at legal stationery stores or downloaded from the internet at: http://www.uscourts.gov/bkforms/index.html. They are not available from the court.)

The courts must charge a $200 case filing fee and a $46 miscellaneous administrative fee. Normally the fees should be paid to the clerk

of the court upon filing. With the court's permission, however, they may be paid in installments. 28 U.S.C. § 1930(a); Fed. R. Bankr. P. 1006(b); Bankruptcy Court Miscellaneous Fee Schedule, Item 8. The number of such installments is limited to four and the debtor must make the final installment no later than 120 days after filing the petition. Fed. R. Bankr. P. 1006(b). For cause shown, the court may extend the time of any installment, provided that the last installment is paid not later than 180 days after the filing of the petition. *Id.* The debtor may also pay the $46 administrative fee in installments. If a joint petition is filed, only one filing fee and one administrative fee are charged. Debtors should be aware that failure to pay these fees may result in dismissal of the case. 11 U.S.C. § 1208(c)(2).

In order to complete the Official Bankruptcy Forms which make up the petition, statement of financial affairs, and schedules, the debtor will need to compile the following information:

1. A list of all creditors and the amounts and nature of their claims;

2. The source, amount, and frequency of the debtor's income;

3. A list of all of the debtor's property; and

4. A detailed list of the debtor's monthly farming and living expenses, *i.e.*, food, shelter, utilities, taxes, transportation, medicine, feed, fertilizer, etc.

Married individuals must gather this information for each spouse regardless of whether they are filing a joint petition, separate individual petitions, or even if only one spouse is filing. In a situation where only one spouse files, the income and expenses of the non-filing spouse is required so that the court, the trustee, and the creditors can evaluate the household's financial position.

When a chapter 12 petition is filed, an impartial trustee is appointed to administer the case. 11 U.S.C. § 1202. In some districts, the U.S. trustee appoints a standing trustee to serve in all chapter 12 cases. 28 U.S.C. § 586(b). As in chapter 13, the trustee both evaluates the case and serves as a disbursing agent, collecting payments from the debtor and making distributions to creditors. 11 U.S.C. § 1202.

Filing the petition under chapter 12 "automatically stays" (stops) most collection actions against the debtor or the debtor's property. 11 U.S.C. § 362. Filing the petition does not, however, stay certain types of actions listed under 11 U.S.C. § 362(b). The stay arises by operation of law and requires no judicial action. As long as the stay is in effect, creditors generally cannot initiate or continue any lawsuits, wage garnishments, or even telephone calls demanding payments. The bankruptcy clerk gives notice of the bankruptcy case to all creditors whose names and addresses are provided by the debtor.

Chapter 12 also contains a special automatic stay provision that protects co-debtors. Unless the bankruptcy court authorizes otherwise, a creditor may not seek to collect a "consumer debt" from any individual who is liable with the debtor. 11 U.S.C. § 1201(a). Consumer debts are those incurred by an individual primarily for a personal, family, or household purpose. 11 U.S.C. § 101(8).

Between 21 to 35 days after the petition is filed, the chapter 12 trustee will hold a "meeting of creditors." If the U.S. trustee or

bankruptcy administrator schedules the meeting at a place that does not have regular U.S. trustee or bankruptcy administrator staffing, the meeting may be held no more than 60 days after the debtor files. During the meeting the trustee puts the debtor under oath and both the trustee and creditors may ask questions. The debtor must attend the meeting and answer questions regarding the debtor's financial affairs and the proposed terms of the debtor's repayment plan. 11 U.S.C. § 343; Fed. R. Bankr. P. 4002. If a husband and wife have filed a joint petition, they both must attend the creditors' meeting. In order to preserve their independent judgment, bankruptcy judges are prohibited from attending. 11 U.S.C. § 341(c). The parties typically resolve problems with the plan either during or shortly after the creditors' meeting. Generally, the debtor can avoid problems by making sure that the petition and plan are complete and accurate, and by consulting with the trustee prior to the meeting.

In a chapter 12 case, to participate in distributions from the bankruptcy estate, unsecured creditors must file their claims with the court within 90 days after the first date set for the meeting of creditors. Fed. R. Bankr. P. 3002(c). A governmental unit, however, has 180 days from the date the case is filed file a proof of claim. 11 U.S.C. § 502(b)(9).

After the meeting of creditors, the debtor, the chapter 12 trustee, and interested creditors will attend a hearing on confirmation of the debtor's chapter 12 repayment plan.

THE CHAPTER 12 PLAN AND CONFIRMATION HEARING

Unless the court grants an extension, the debtor must file a plan of repayment with the petition or within 90 days after filing the petition. 11 U.S.C. § 1221. The plan, which must be submitted to the court for approval, provides for payments of fixed amounts to the trustee on a regular basis. The trustee then distributes the funds to creditors according to the terms of the plan, which typically offers creditors less than full payment on their claims.

There are three types of claims: priority, secured, and unsecured. Priority claims are those granted special status by the bankruptcy law, such as most taxes and the costs of bankruptcy proceeding.[2] Secured claims are those for which the creditor has the right to liquidate certain property if the debtor does not pay the underlying debt. In contrast to secured claims, unsecured claims are generally those for which the creditor has no special rights to collect against particular property owned by the debtor.

A chapter 12 plan usually lasts three to five years. It must provide for full payment of all priority claims, unless a priority creditor agrees to different treatment of the claim or, in the case of a domestic support obligation, unless the debtor contributes all "disposable income" - discussed below - to a five-year plan. 11 U.S.C. § 1222(a)(2), (4).

Secured creditors must be paid at least as much as the value of the collateral pledged for the debt. One of the features of Chapter 12 is that payments to secured creditors can sometimes continue longer than the three-to-five-year period of the plan. For example, if the debtor's underlying debt obligation was scheduled to be paid over more than five years (*i.e.*, an equipment loan or a mortgage), the debtor may be able to pay the loan off over the original loan repayment schedule as long as any arrearage is made up during the plan.

The plan does not have to pay unsecured claims in full, as long as it commits all of the debtor's projected "disposable income" (or property of equivalent value) to plan payments over a 3 to 5 year period ,and as long as the unsecured creditors are to receive at least as much as they would receive if the debtor's nonexempt assets were liquidated under chapter 7. 11 U.S.C. § 1225. "Disposable income" is defined as income not reasonably necessary for the maintenance or support of the debtor or dependents or for making payments needed to continue, preserve, and operate the debtor's business. 11 U.S.C. § 1225(b)(2).

Within 45 days after filing the plan, the presiding bankruptcy judge decides at a "confirmation hearing" whether the plan is feasible and meets the standards for confirmation under the Bankruptcy Code. 11 U.S.C. §§ 1224, 1225. Creditors, who receive 21 days' notice, may appear at the hearing and object to confirmation. Fed. R. Bankr. P. 2002(a)(8). While a variety of objections may be made, the typical arguments are that payments offered under the plan are less than creditors would receive if the debtor's assets were liquidated, or that the plan does not commit all of the debtor's disposable income for the three-to-five-year period of the plan.

If the court confirms the plan, the chapter 12 trustee will distribute funds received in accordance with the terms of the plan.11 U.S.C. § 1226(a). If the court does not confirm the plan, the debtor may file a modified plan. 11 U.S.C. § 1223. The debtor may also convert the case to a liquidation under chapter 7.[3] 11 U.S.C. § 1208(a). If the debtor fails to confirm a plan and the case is dismissed, the court may authorize the trustee to keep some of the funds for costs, but the trustee must return all remaining funds to the debtor (other than funds already disbursed to creditors). 11 U.S.C. § 1226(a).

On occasion, changed circumstances will affect the debtor's ability to make plan payments. A creditor may object or threaten to object to a plan, or the debtor may inadvertently have failed to list all creditors. In such instances, the plan may be modified either before or after confirmation. 11 U.S.C. §§ 1223, 1229. Modification after confirmation is not limited to an initiative by the debtor, but may also be made at the request of the trustee or an unsecured creditor.11 U.S.C. § 1229(a).

MAKING THE PLAN WORK

The provisions of a confirmed plan bind the debtor and each creditor. 11 U.S.C. § 1227. Once the court confirms the plan, the debtor must make the plan succeed. The debtor must make regular payments to the trustee, which will require adjustment to living on a fixed budget for a prolonged period. Furthermore, while confirmation of the plan entitles the debtor to retain property as long as payments are made, the debtor may not incur any significant new debt without consulting the trustee, because additional debt may compromise the debtor's ability to complete the plan.11 U.S.C. §§ 1222(a)(1), 1227. In any event, failure to make the plan payments may result in dismissal of the case. 11 U.S.C. § 1208(c). In addition, the court may dismiss the case or convert the case to a liquidation case under chapter 7 of the Bankruptcy Code upon a showing that the debtor has committed fraud in connection with the case. 11 U.S.C. § 1208(d).

THE CHAPTER 12 DISCHARGE

The debtor will receive a discharge after completing all payments under the chapter 12 plan as long as the debtor certifies (if applicable) that all domestic support obligations that came due before making such certification have been paid. The discharge has the effect of releasing the debtor from all debts provided for by the plan allowed under section 503 or disallowed under section 502, with limited exceptions. Those creditors who were provided for in full or in part under the plan may no longer initiate or continue any legal or other action against the debtor to collect the discharged obligations.

Certain categories of debts are not discharged in chapter 12 proceedings. 11 U.S.C. § 1228(a). Those categories include debts for alimony and child support; money obtained through filing false financial statements; debts for willful and malicious injury to person or property; debts for death or personal injury caused by the debtor's operation of a motor vehicle while the debtor was intoxicated; and debts from fraud or defalcation while acting in a fiduciary capacity, embezzlement or larceny. The bankruptcy law regarding the scope of a chapter 12 discharge is complex, however, and debtors should consult competent legal counsel in this regard prior to filing. Those debts which will not be discharged should be paid in full under a plan. With respect to secured obligations, those debts may be paid beyond the end of the plan payment period and, accordingly, are not discharged.

CHAPTER 12 HARDSHIP DISCHARGE

The court may grant a "hardship discharge" to a chapter 12 debtor even though the debtor has failed to complete plan payments. 11 U.S.C. § 1228(b). Generally, a hardship discharge is available only to a debtor whose failure to complete plan payments is due to circumstances beyond the debtor's control and through no fault of the debtor. Creditors must have received at least as much as they would have received in a chapter 7 liquidation case, and the debtor must be unable to modify the plan. For example, injury or illness that precludes employment sufficient to fund even a modified plan may serve as the basis for a hardship discharge. The hardship discharge does not apply to any debts that are nondischargeable in a chapter 7 case. 11 U.S.C. § 523.

NOTES

1. In North Carolina and Alabama, bankruptcy administrators perform similar functions that U.S. trustees perform in the remaining forty-eight states. The bankruptcy administrator program is administered by the Administrative Office of the United States Courts, while the U.S. trustee program is administered by the Department of Justice. For purposes of this publication, references to U.S. trustees are also applicable to bankruptcy administrators.

2. Section 507 sets forth 10 categories of unsecured claims which Congress has, for public policy reasons, given priority of distribution over other unsecured claims.

3. A fee of $15 is charged for converting a case under chapter 12 to a case under chapter 7.

Chapter 9

Municipality Bankruptcy

The first municipal bankruptcy legislation was enacted in 1934 during the Great Depression. Pub. L. No. 251, 48 Stat. 798 (1934). Although Congress took care to draft the legislation so as not to interfere with the sovereign powers of the states guaranteed by the Tenth Amendment to the Constitution, the Supreme Court held the 1934 Act unconstitutional as an improper interference with the sovereignty of the states. *Ashton v. Cameron County Water Improvement Dist. No. 1*, 298 U.S. 513, 532 (1936). Congress enacted a revised Municipal Bankruptcy Act in 1937, Pub. L. No. 302, 50 Stat. 653 (1937), which was upheld by the Supreme Court. *United States v. Bekins*, 304 U.S. 27, 54 (1938). The law has been amended several times since 1937. In the more than 60 years since Congress established a federal mechanism for the resolution of municipal debts, there have been fewer than 500 municipal bankruptcy petitions filed. Although chapter 9 cases are rare, a filing by a large municipality can— like the 1994 filing by Orange County, California—involve many millions of dollars in municipal debt.

PURPOSE OF MUNICIPAL BANKRUPTCY

The purpose of chapter 9 is to provide a financially-distressed municipality protection from its creditors while it develops and negotiates a plan for adjusting its debts. Reorganization of the debts of a municipality is typically accomplished either by extending debt maturities, reducing the amount of principal or interest, or refinancing the debt by obtaining a new loan.

Although similar to other chapters in some respects, chapter 9 is significantly different in that there is no provision in the law for liquidation of the assets of the municipality and distribution of the proceeds to creditors. Such a liquidation or dissolution would undoubtedly violate the Tenth Amendment to the Constitution and the reservation to the states of sovereignty over their internal affairs. Indeed, due to the severe limitations placed upon the power of the bankruptcy court in chapter 9 cases (required by the Tenth Amendment and the Supreme Court's decisions in cases upholding municipal bankruptcy legislation), the bankruptcy court generally is not as active in managing a municipal bankruptcy case as it is in corporate reorganizations under chapter 11.

The functions of the bankruptcy court in chapter 9 cases are generally limited to approving the petition (if the debtor is eligible), confirming a plan of debt adjustment, and ensuring implementation of the plan. As a practical matter, however, the municipality may consent to have the court exercise jurisdiction in many of the traditional areas of court oversight in bankruptcy, in order to obtain the protection of court orders and eliminate the need for multiple forums to decide issues.

ELIGIBILITY

Only a "municipality" may file for relief under chapter 9. 11 U.S.C. § 109(c). The term "municipality" is defined in the Bankruptcy Code as a "political subdivision or public agency or instrumentality of a State." 11 U.S.C. § 101(40). The definition is broad enough to include cities, counties, townships, school districts, and public improvement districts. It also includes revenue-producing bodies that provide

services which are paid for by users rather than by general taxes, such as bridge authorities, highway authorities, and gas authorities.

Section 109(c) of the Bankruptcy Codes sets forth four additional eligibility requirements for chapter 9:

1.The municipality must be *specifically* authorized to be a debtor by State law or by a governmental officer or organization empowered by State law to authorize the municipality to be a debtor;

2.The municipality must be insolvent, as defined in 11 U.S.C. § 101(32)(C);

3.The municipality must desire to effect a plan to adjust its debts; and

4.The municipality must either:

- obtain the agreement of creditors holding at least a majority in amount of the claims of each class that the debtor intends to impair under a plan in a case under chapter 9;
- negotiate in good faith with creditors and fail to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that the debtor intends to impair under a plan;
- be unable to negotiate with creditors because such negotiation is impracticable; or
- reasonably believe that a creditor may attempt to obtain a preference.

COMMENCEMENT OF THE CASE

Municipalities must voluntarily seek protection under the Bankruptcy Code. 11 U.S.C. §§ 303, 901(a). They may file a petition only under chapter 9. A case under chapter 9 concerning an unincorporated tax or special assessment district that does not have its own officials is commenced by the filing of a voluntary "petition under this chapter by such district's governing authority or the board or body having authority to levy taxes or assessments to meet the obligations of such district." 11 U.S.C. § 921(a).

A municipal debtor must file a list of creditors. 11 U.S.C. § 924. Normally, the debtor files the list of creditors with the petition. However, the bankruptcy court has discretion to fix a different time if the debtor is unable to prepare the list of creditors in the form and with the detail required by the Bankruptcy Rules at the time of filing. Fed. R. Bankr. P. 1007.

ASSIGNMENT OF CASE TO A BANKRUPTCY JUDGE

One significant difference between chapter 9 cases and cases filed under other chapters is that the clerk of court does not automatically assign the case to a particular judge. "The chief judge of the court of appeals for the circuit embracing the district in which the case is commenced [designates] the bankruptcy judge to conduct the case." 11 U.S.C. § 921(b). This provision was designed to remove politics from the issue of which judge will preside over the chapter 9 case of a major municipality and to ensure that a municipal case will be handled by a judge who has the time and capability of doing so.

NOTICE OF CASE/OBJECTIONS/ ORDER FOR RELIEF

The Bankruptcy Code requires that notice be given of the commencement of the case and the order for relief. 11 U.S.C. § 923. The Bankruptcy Rules provide that the clerk, or such other person as the court may direct, is to give notice. Fed. R. Bankr. P. 2002(f). The notice must also be published "at least once a week for three successive weeks in at least one newspaper of general circulation published within the district in which the case is commenced, and in such other newspaper having a general circulation among bond dealers and bondholders as the court designates." 11 U.S.C. § 923. The court typically enters an order designating who is to give and receive notice by mail and identifying the newspapers in which the additional notice is to be published. Fed. R. Bankr. P. 9007, 9008.

The Bankruptcy Code permits objections to the petition. 11 U.S.C. § 921(c). Typically, objections concern issues like whether negotiations have been conducted in good faith, whether the state has authorized the municipality to file, and whether the petition was filed in good faith. If an objection to the petition is filed, the court must hold a hearing on the objection. *Id.* The court may dismiss a petition if it determines that the debtor did not file the petition in good faith or that the petition does not meet the requirements of title 11. *Id*.

If the petition is not dismissed upon an objection, the Bankruptcy Code requires the court to order relief, allowing the case to proceed under chapter 9. 11 U.S.C. § 921(d).

AUTOMATIC STAY

The automatic stay of section 362 of the Bankruptcy Code is applicable in chapter 9 cases. 11 U.S.C. §§ 362(a), 901(a). The stay operates to stop all collection actions against the debtor and its property upon the filing of the petition. Additional automatic stay provisions are applicable in chapter 9 that prohibit actions against officers and inhabitants of the debtor if the action seeks to enforce a claim against the debtor. 11 U.S.C. § 922(a). Thus, the stay prohibits a creditor from bringing a mandamus action against an officer of a municipality on account of a prepetition debt. It also prohibits a creditor from bringing an action against an inhabitant of the debtor to enforce a lien on or arising out of taxes or assessments owed to the debtor.

Section 922(d) of title 11 limits the applicability of the stay. Under that section, a chapter 9 petition does not operate to stay application of pledged special revenues to payment of indebtedness secured by such revenues. Thus, an indenture trustee or other paying agent may apply pledged funds to payments coming due or distribute the pledged funds to bondholders without violating the automatic stay.

PROOFS OF CLAIM

In a chapter 9 case, the court fixes the time within which proofs of claim or interest may be filed. Fed. R. Bankr. P. 3003(c)(3). Many creditors may not be required to file a proof of claim in a chapter 9 case. For example, a proof of claim is deemed filed if it appears on the list of creditors filed by the debtor, unless the debt is listed as disputed, contingent, or unliquidated. 11 U.S.C. § 925. Thus, a creditor must file a proof of claim if the creditor's claim appears on the list of creditors as disputed, contingent, or unliquidated.

COURT'S LIMITED POWER

Sections 903 and 904 of the Bankruptcy Code are designed to recognize the court's limited power over operations of the debtor.

Section 904 limits the power of the bankruptcy court to "interfere with – (1) any of the political or governmental powers of the debtor; (2) any of the property or revenues of the debtor; or (3) the debtor's use or enjoyment of any income-producing property" unless the debtor consents or the plan so provides. The provision makes it clear that the debtor's day-to-day activities are not subject to court approval and that the debtor may borrow money without court authority. In addition, the court cannot appoint a trustee (except for limited purposes specified in 11 U.S.C. § 926(a)) and cannot convert the case to a liquidation proceeding.

The court also cannot interfere with the operations of the debtor or with the debtor's use of its property and revenues. This is due, at least in part, to the fact that in a chapter 9 case, there is no property of the estate and thus no estate to administer. 11 U.S.C. § 902(1). Moreover, a chapter 9 debtor may employ professionals without court approval, and the only court review of fees is in the context of plan confirmation, when the court determines the reasonableness of the fees.

The restrictions imposed by 11 U.S.C. § 904 are necessary to ensure the constitutionality of chapter 9 and to avoid the possibility that the court might substitute its control over the political or governmental affairs or property of the debtor for that of the state and the elected officials of the municipality.

Similarly, 11 U.S.C. § 903 states that "chapter [9] does not limit or impair the power of a State to control, by legislation or otherwise, a municipality of or in such State in the exercise of the political or governmental powers of the municipality, including expenditures for such exercise," with two exceptions—a state law prescribing a method of composition of municipal debt does not bind any non-consenting creditor, nor does any judgment entered under such state law bind a nonconsenting creditor.

ROLE OF THE U.S. TRUSTEE/BANKRUPTCY ADMINISTRATOR

In a chapter 9 case, the role of the U.S. trustee (or the bankruptcy administrator in North Carolina or Alabama)[1] is typically more limited than in chapter 11 cases. Although the U.S. trustee appoints a creditors' committee, the U.S. trustee does not examine the debtor at a meeting of creditors (there is no meeting of creditors), does not have the authority to move for appointment of a trustee or examiner or for conversion of the case, and does not supervise the administration of the case. Further, the U.S. trustee does not monitor the financial operations of the debtor or review the fees of professionals retained in the case.

ROLE OF CREDITORS

The role of creditors is more limited in chapter 9 than in other cases. There is no first meeting of creditors, and creditors may not propose competing plans. If certain requirements are met, the debtor's plan is binding on dissenting creditors. The chapter 9 debtor has more freedom to operate without court-imposed restrictions.

In each chapter 9 case, however, there is a creditors' committee that has powers and duties that are very similar to those of a committee in a chapter 11 case. These

powers and duties include selecting and authorizing the employment of one or more attorneys, accountants, or other agents to represent the committee; consulting with the debtor concerning administration of the case; investigating the acts, conduct, assets, liabilities, and financial condition of the debtor; participating in the formulation of a plan; and performing such other services as are in the interest of those represented. 11 U.S.C. §§ 901(a), 1103.

INTERVENTION/RIGHT OF OTHERS TO BE HEARD

When cities or counties file for relief under chapter 9, there may be a great deal of interest in the case from entities wanting to appear and be heard. The Bankruptcy Rules provide that "[t]he Secretary of the Treasury of the United States may, or if requested by the court shall, intervene in a chapter 9 case." Fed. R. Bankr. P. 2018(c). Further, "[r]epresentatives of the state in which the debtor is located may intervene in a chapter 9 case." *Id*. In addition, the Bankruptcy Code permits the Securities and Exchange Commission to appear and be heard on any issue and gives parties in interest the right to appear and be heard on any issue in a case. 11 U.S.C. §§ 901(a), 1109. Parties in interest include municipal employees, local residents, non-resident owners of real property, special tax payers, securities firms, and local banks.

POWERS OF THE DEBTOR

Due to statutory limitations placed upon the power of the court in a municipal debt adjustment proceeding, the court is far less involved in the conduct of a municipal bankruptcy case (and in the operation of the municipal entity) while the debtor's financial affairs are undergoing reorganization. The municipal debtor has broad powers to use its property, raise taxes, and make expenditures as it sees fit. It is also permitted to adjust burdensome non-debt contractual relationships under the power to reject executory contracts and unexpired leases, subject to court approval, and it has the same avoiding powers as other debtors. Municipalities may also reject collective bargaining agreements and retiree benefit plans without going through the usual procedures required in chapter 11 cases.

A municipality has authority to borrow money during a chapter 9 case as an administrative expense. 11 U.S.C. §§ 364, 901(a). This ability is important to the survival of a municipality that has exhausted all other resources. A chapter 9 municipality has the same power to obtain credit as it does outside of bankruptcy. The court does not have supervisory authority over the amount of debt the municipality incurs in its operation. The municipality may employ professionals without court approval, and the professional fees incurred are reviewed only within the context of plan confirmation.

DISMISSAL

As previously noted, the court may dismiss a chapter 9 petition, after notice and a hearing, if it concludes the debtor did not file the petition in good faith or if the petition does not meet the requirements of chapter 9. 11 U.S.C. § 921(c). The court may also dismiss the petition for cause, such as for lack of prosecution, unreasonable delay by the debtor that is prejudicial to creditors, failure to propose or confirm a

plan within the time fixed by the court, material default by the debtor under a confirmed plan, or termination of a confirmed plan by reason of the occurrence of a condition specified in the plan. 11 U.S.C. § 930.

TREATMENT OF BONDHOLDERS AND OTHER LENDERS

Different types of bonds receive different treatment in municipal bankruptcy cases. General obligation bonds are treated as general debt in the chapter 9 case. The municipality is not required to make payments of either principal or interest on account of such bonds during the case. The obligations created by general obligation bonds are subject to negotiation and possible restructuring under the plan of adjustment.

Special revenue bonds, by contrast, will continue to be secured and serviced during the pendency of the chapter 9 case through continuing application and payment of ongoing special revenues. 11 U.S.C. § 928. Holders of special revenue bonds can expect to receive payment on such bonds during the chapter 9 case if special revenues are available. The application of pledged special revenues to indebtedness secured by such revenues is not stayed as long as the pledge is consistent with 11 U.S.C. § 928 [§ 922(d) erroneously refers to § 927 rather than § 928], which insures that a lien of special revenues is subordinate to the operating expenses of the project or system from which the revenues are derived. 11 U.S.C. § 922(d).

Bondholders generally do not have to worry about the threat of preference liability with respect to any prepetition payments on account of bonds or notes, whether special revenue or general obligations. Any transfer of the municipal debtor's property to a noteholder or bondholder on account of a note or bond cannot be avoided as a preference, *i.e.*, as an unauthorized payment to a creditor made while the debtor was insolvent. 11 U.S.C. § 926(b).

PLAN FOR ADJUSTMENT OF DEBTS

The Bankruptcy Code provides that the debtor must file a plan. 11 U.S.C. § 941. The plan must be filed with the petition or at such later time as the court fixes. There is no provision in chapter 9 allowing creditors or other parties in interest to file a plan. This limitation is required by the Supreme Court's pronouncements in *Ashton*, 298 U.S. at 528, and *Bekins*, 304 U.S. at 51, which interpreted the Tenth Amendment as requiring that a municipality be left in control of its governmental affairs during a chapter 9 case. Neither creditors nor the court may control the affairs of a municipality indirectly through the mechanism of proposing a plan of adjustment of the municipality's debts that would in effect determine the municipality's future tax and spending decisions.

CONFIRMATION STANDARDS

The standards for plan confirmation in chapter 9 cases are a combination of the statutory requirements of 11 U.S.C. § 943(b) and those portions of 11 U.S.C. § 1129 (the chapter 11 confirmation standards) made applicable by 11 U.S.C. § 901(a). Section 943(b) lists seven general conditions required for confirmation of a

plan. The court must confirm a plan if the following conditions are met:

1. the plan complies with the provisions of title 11 made applicable by sections 103(e) and 901;

2. the plan complies with the provisions of chapter 9;

3. all amounts to be paid by the debtor or by any person for services or expenses in the case or incident to the plan have been fully disclosed and are reasonable;

4. the debtor is not prohibited by law from taking any action necessary to carry out the plan;

5. except to the extent that the holder of a particular claim has agreed to a different treatment of such claim, the plan provides that on the effective date of the plan, each holder of a claim of a kind specified in section 507(a)(1) will receive on account of such claim cash equal to the allowed amount of such claim;

6. any regulatory or electoral approval necessary under applicable nonbankruptcy law in order to carry out any provision of the plan has been obtained, or such provision is expressly conditioned on such approval; and

7. the plan is in the best interests of creditors and is feasible.

11 U.S.C. § 943(b).

Section 943(b)(1) requires as a condition for confirmation that the plan comply with the provisions of the Bankruptcy Code made applicable by sections 103(e) and 901(a) of the Bankruptcy Code. The most important of these for purposes of confirming a plan are those provisions of 11 U.S.C. § 1129 (*i.e.*, § 1129(a)(2), (a)(3), (a)(6), (a)(8), (a)(10)) that are made applicable by 11 U.S.C. § 901(a). Section 1129(a)(8) requires, as a condition to confirmation, that the plan has been accepted by each class of claims or interests impaired under the plan. Therefore, if the plan proposes treatment for a class of creditors such that the class is impaired (*i.e.*, the creditor's legal, equitable, or contractual rights are altered), then that class's acceptance is required. If the class is not impaired, then acceptance by that class is not required as a condition to confirmation. Under 11 U.S.C. § 1129(a)(10), the court may confirm the plan only if, should any class of claims be impaired under the plan, at least one impaired class has accepted the plan. If only one impaired class of creditors consents to the plan, plan confirmation is still possible under the "cram down" provisions of 11 U.S.C. § 1129(b). Under "cram down," if all other requirements are met except the § 1129(a)(8) requirement that all classes either be unimpaired or have accepted the plan, then the plan is confirmable if it does not discriminate unfairly and is fair and equitable.

The requirement that the plan be in the "best interests of creditors" means something different under chapter 9 than under chapter 11. Under chapter 11, a plan is said to be in the "best interest of creditors" if creditors would receive as much under the plan as they would if the debtor were liquidated. 11 U.S.C. § 1129(a)(7)(A)(ii). Obviously, a different interpretation is needed in chapter 9 cases because a municipality's assets cannot be liquidated to pay creditors. In the chapter 9 context, the "best interests of creditors" test has generally been interpreted to mean that the plan must be better than other alternatives available to the creditors. *See* 6 COLLIER ON BANKRUPTCY

§ 943.03[7] (15th ed. rev. 2005). Generally speaking, the alternative to chapter 9 is dismissal of the case, permitting every creditor to fend for itself. An interpretation of the " best interests of creditors" test to require that the municipality devote all resources available to the repayment of creditors would appear to exceed the standard. The courts generally apply the test to require a reasonable effort by the municipal debtor that is a better alternative for its creditors than dismissal of the case. *Id.*

Parties in interest may object to confirmation, including creditors whose claims are affected by the plan, an organization of employees of the debtor, and other tax payers, as well as the Securities and Exchange Commission. 11 U.S.C. §§ 901(a), 943, 1109, 1128(b).

DISCHARGE

A municipal debtor receives a discharge in a chapter 9 case after: (1) confirmation of the plan; (2) deposit by the debtor of any consideration to be distributed under the plan with the disbursing agent appointed by the court; and (3) a determination by the court that securities deposited with the disbursing agent will constitute valid legal obligations of the debtor and that any provision made to pay or secure payment of such obligations is valid. 11 U.S.C. § 944(b). Thus, the discharge is conditioned not only upon confirmation, but also upon deposit of the consideration to be distributed under the plan and a court determination of the validity of securities to be issued.

There are two exceptions to the discharge in chapter 9 cases. The first is for any debt excepted from discharge by the plan or order confirming the plan. The second is for a debt owed to an entity that, before confirmation of the plan, had neither notice nor actual knowledge of the case. 11 U.S.C. § 944(c).

At any time within 180 days after entry of the confirmation order, the court may, after notice and a hearing, revoke the order of confirmation if the order was procured by fraud. 11 U.S.C. §§ 901(a), 1144.

NOTES

1. In North Carolina and Alabama, bankruptcy administrators perform similar functions that United States trustees perform in the remaining forty-eight states. The bankruptcy administrator program is administered by the Administrative Office of the United States Courts, while the United States trustee program is administered by the Department of Justice. For purposes of this publication, references to United States trustees are also applicable to bankruptcy administrators.

Chapter 15

Ancillary and Other Cross-Border Cases

Chapter 15 is a new chapter added to the Bankruptcy Code by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. It is the U.S. domestic adoption of the Model Law on Cross-Border Insolvency promulgated by the United Nations Commission on International Trade Law ("UNCITRAL") in 1997, and it replaces section 304 of the Bankruptcy Code. Because of the UNCITRAL source for chapter 15, the U.S. interpretation must be coordinated with the interpretation given by other countries that have adopted it as internal law to promote a uniform and coordinated legal regime for cross-border insolvency cases.

The purpose of Chapter 15, and the Model Law on which it is based, is to provide effective mechanisms for dealing with insolvency cases involving debtors, assets, claimants and other parties in interest involving more than one country. This general purpose is realized through five objectives specified in the statute: (1) to promote cooperation between the United States courts and parties in interest and the courts and other competent authorities of foreign countries involved in cross-border insolvency cases; (2) to establish greater legal certainty for trade and investment; (3) to provide for the fair and efficient administration of cross-border insolvencies that protects the interests of all creditors and other interested entities, including the debtor; (4) to afford protection and maximization of the value of the debtor's assets; and (5) to facilitate the rescue of financially troubled businesses, thereby protecting investment and preserving employment. 11 U.S.C. § 1501.

Generally, a chapter 15 case is ancillary to a primary proceeding brought in another country, typically the debtor's home country. As an alternative, the debtor or a creditor may commence a full chapter 7 or chapter 11 case in the United States if the assets in the United States are sufficiently complex to merit a full-blown domestic bankruptcy case. 11 U.S.C. § 1520(c). In addition, under chapter 15 a U.S. court may authorize a trustee or other entity (including an examiner) to act in a foreign country on behalf of a U.S. bankruptcy estate. 11 U.S.C. § 1505.

An ancillary case is commenced under chapter 15 by a "foreign representative" filing a petition for recognition of a "foreign proceeding."[1] 11 U.S.C. § 1504. Chapter 15 gives the foreign representative the right of direct access to U.S. courts for this purpose. 11 U.S.C. § 1509. The petition must be accompanied by documents showing the existence of the foreign proceeding and the appointment and authority of the foreign representative. 11 U.S.C. § 1515. After notice and a hearing, the court is authorized to issue an order recognizing the foreign proceeding as either a "foreign main proceeding" (a proceeding pending in a country where the debtor's center of main interests are located) or a "foreign non-main proceeding" (a proceeding pending in a country where the debtor has an establishment,[2] but not its center of main interests). 11 U.S.C. § 1517. Immediately upon the recognition of a foreign main proceeding, the automatic stay and selected other provisions of the Bankruptcy Code take effect within the United States. 11 U.S.C. § 1520. The foreign representative is also authorized to operate the debtor's business in the ordinary course. *Id.* The U.S.

court is authorized to issue preliminary relief as soon as the petition for recognition is filed. 11 U.S.C.
§ 1519.

Through the recognition process, chapter 15 operates as the principal door of a foreign representative to the federal and state courts of the United States. 11 U.S.C. § 1509. Once recognized, a foreign representative may seek additional relief from the bankruptcy court or from other state and federal courts and is authorized to bring a full (as opposed to ancillary) bankruptcy case. 11 U.S.C. §§ 1509, 1511. In addition, the representative is authorized to participate as a party in interest in a pending U.S. insolvency case and to intervene in any other U.S. case where the debtor is a party. 11 U.S.C. §§ 1512, 1524.

Chapter 15 also gives foreign creditors the right to participate in U.S. bankruptcy cases and it prohibits discrimination against foreign creditors (except certain foreign government and tax claims, which may be governed by treaty). 11 U.S.C. § 1513. It also requires notice to foreign creditors concerning a U.S. bankruptcy case, including notice of the right to file claims. 11 U.S.C. § 1514.

One of the most important goals of chapter 15 is to promote cooperation and communication between U.S. courts and parties in interest with foreign courts and parties in interest in cross-border cases. This goal is accomplished by, among other things, explicitly charging the court and estate representatives to "cooperate to the maximum extent possible" with foreign courts and foreign representatives and authorizing direct communication between the court and authorized estate representatives and the foreign courts and foreign representatives. 11 U.S.C. §§ 1525 - 1527.

If a full bankruptcy case is initiated by a foreign representative (when there is a foreign main proceeding pending in another country), bankruptcy court jurisdiction is generally limited to the debtor's assets that are located in the United States. 11 U.S.C. § 1528. The limitation promotes cooperation with the foreign main proceeding by limiting the assets subject to U.S. jurisdiction, so as not to interfere with the foreign main proceeding. Chapter 15 also provides rules to further cooperation where a case was filed under the Bankruptcy Code prior to recognition of the foreign representative and for coordination of more than on foreign proceeding. 11 U.S.C. §§ 1529 - 1530.

The UNCITRAL Model Law has also been adopted (with certain variations) in Canada, Mexico, Japan and several other countries. Adoption is pending in the United Kingdom and Australia, as well as other countries with significant international economic interests.

NOTES

1. A "foreign proceeding" is a "judicial or administrative proceeding in a foreign country ... under a law relating to insolvency or adjustment of debt in which proceeding the [debtor's assets and affairs] are subject to control or supervision by a foreign court for the purpose of reorganization or liquidation." 11 U.S.C. § 101(23). A "foreign representative" is the person or entity authorized in the foreign proceeding "to administer the reorganization or liquidation of the debtor's assets or affairs or to act as a representative of such foreign proceeding."

2. An establishment is a place of operations where the debtor carries out a long term economic activity. 11 U.S.C. § 1502(2).

Servicemembers' Civil Relief Act

BACKGROUND

The Servicemembers' Civil Relief Act ("SCRA") is found at 50 U.S.C. app. §§ 501 et seq. The purpose of the SCRA is strengthen and expedite national defense by giving servicemembers certain protections in civil actions. By providing for the temporary suspension of judicial and administrative proceedings and transactions that may adversely affect servicemembers during their military service, the SCRA enables servicemembers to focus their energy on the defense of the United States. Among other things, the SCRA allows for forbearance and reduced interest on certain obligations incurred prior to military service, and it restricts default judgments against servicemembers and rental evictions of servicemembers and all their dependents. The SCRA applies to all members of the United States military on active duty, and to U.S. citizens serving in the military of United States allies in the prosecution of a war or military action. The provisions of the SCRA generally end when a servicemember is discharged from active duty or within 90 days of discharge, or when the servicemember dies. Portions of the SCRA also apply to reservists and inductees who have received orders but not yet reported to active duty or induction into the military service.

GENERAL PROVISIONS

There are three primary areas of coverage under the SCRA: (1) protection against the entry of default judgments; (2) stay of proceedings where the servicemember has notice of the proceeding; and (3) stay or vacation of execution of judgments, attachments and garnishments. 50 U.S.C. app. §§ 521, 522 and 524.

Protection Against Default Judgements

Section 521 of the SCRA establishes certain procedures that must be followed in all civil proceedings in order to protect servicemember defendants against the entry of default judgements. These procedures are outlined below:

•If a defendant is in default for failure to appear in the action filed by the plaintiff, the plaintiff must file an affidavit[1] with the court before a default judgment may be entered. The affidavit must state whether the defendant is in the military, or that the plaintiff was unable to determine whether the defendant is in the military.

•If, based on the filed affidavits, the court cannot determine whether the defendant is in the military, it may condition entry of judgment against the defendant upon the plaintiff's filing of a bond. The bond would indemnify the defendant against any loss or damage incurred because of the judgment if the judgment is later set aside in whole or in part.

•The court may not order entry of judgment against the defendant if the defendant is in the military until after the court appoints an attorney to represent the defendant.

•If requested by counsel for a servicemember defendant, or upon the

court's own motion, the court will grant a stay of proceedings for no less than 90 days if it determines that (1) there may be a defense and the defense cannot be presented without the defendant's presence; or (2) after due diligence the defendant's attorney has not been able to contact the defendant or otherwise determine if a meritorious defense exists.

•The court may, in its discretion, make further orders or enter further judgments to protect the rights of the defendant under the SCRA.

•If a judgment is entered against the defendant while he or she is in military service or within 60 days of discharge from military service, and the defendant was prejudiced in making his or her defense because of his or her military service, the judgment may, upon application by the defendant, be opened by the court and the defendant may then provide a defense. Before the judgment may be opened, however, the defendant must show that he or she has a meritorious or legal defense to some or all of the action.

Stay of Proceedings Where Servicemember Has Notice

Outside the default context, and at any time before final judgement in a civil action, a person covered by the SCRA who has received notice of a proceeding may ask the court to stay the proceeding. 50 U.S.C. app. § 522. The court may also order a stay on its own motion. *Id.* The court will grant the servicemember's stay application and will stay the proceeding for at least 90 days if the application includes: (1) a letter or other communication setting forth facts demonstrating that the individual's current military duty requirements materially affect the servicemember's ability to appear along with a date when the servicemember will be able to appear; and (2) a letter or other communication from the servicemember's commanding officer stating that the servicemember's current military duty prevents his or her appearance and that military leave is not authorized for the servicemember at the time of the letter. The court has discretion to grant additional stays upon further application.

Stay or Vacation of Execution of Judgements, Attachments and Garnishments

In addition to the court's ability to regulate default judgments and stay proceedings, the court may on its own motion and must upon application: (1) stay the execution of any judgment or order entered against a servicemember; and (2) vacate or stay any attachment or garnishment of the servicemember's property or assets, whether before or after judgment if it finds that the servicemember's ability to comply with the judgment or garnishment is materially affected by military service. 50 U.S.C. app. § 524. The stay of execution may be ordered for any part of the servicemember's military service plus 90 days after discharge from the service. The court may also order the servicemember to make installment payments during any stay ordered.

Additional Protections

Several additional rights are available under the SCRA. For example, when an action for compliance with a contract is stayed under the SCRA, contractual penalties do not accrue during the period of the stay. 50 U.S.C. app. § 523. The SCRA also provides

in most instances that a landlord cannot evict a servicemember or dependants from a primary residence without a court order. In an eviction proceeding, the court may also adjust the lease obligations to protect the interests of the parties. 50 U.S.C. app. § 531. If the court stay the eviction proceeding, it may provide equitable relief to the landlord by ordering garnishment of a portion of the servicemember's pay. *Id*. Under the SCRA a servicemember may terminate residential and automotive leases if he or she is transferred after the lease is made. 50 U.S.C. app. § 535. A court may also extend some of the protections afforded a servicemember under the SCRA to persons co-liable or secondarily liable on the servicemember's obligation. 50 U.S.C. app. § 513.

APPLICABILITY TO BANKRUPTCY PROCEEDINGS

The language of the SCRA states that it is generally applicable in any action or proceeding commenced in any court. 50 U.S.C. app. §§ 521, 522 and 524. Therefore, absent contravening language with respect to bankruptcy proceedings, the SCRA applies to all actions or proceedings before a bankruptcy court.

The applicability of the SCRA in bankruptcy proceedings is also evident in the Federal Rules of Civil Procedure and the Federal Rules of Bankruptcy Procedure. For example, the advisory committee note to Federal Rule for default judgments, Fed. R. Civ. P. 55(b), states that it is directly affected by the SCRA.[2] Under Fed. R. Bankr. P. 7055 and 9014 of the Federal Rules of Bankruptcy Procedure, Fed. R. Civ. P. 55 is applicable in bankruptcy adversary proceedings and contested matters. Thus, the default judgment protections of the SCRA clearly apply in bankruptcy cases.

The bankruptcy court clerk's office is aware of the requirement that the plaintiff must provide an affidavit stating whether the defendant is in the military before default may be entered against the defendant. Bankruptcy Procedural Forms B260, B261A, and B261B, and their accompanying instructions, provide additional guidance concerning the applicability of the SCRA to default judgments and related procedural requirements.

NOTES

1. The requirement for an affidavit may be satisfied by a statement, declaration, verification, or certificate in writing subscribed and certified or declared to be true under penalty of perjury. 50 U.S.C. app. § 521(4).

2. The advisory committee note to Fed. R. Civ. P. 55 comments on the applicability of the Servicemembers' Civil Relief Act (formally known as the Soldiers' and Sailors' Civil Relief Act of 1940) to default judgements as follows:

The operation of Rule 55(b) (Judgment) is directly affected by the Soldiers' and Sailors' Civil Relief Act of 1940, 50 U.S.C. Appendix, § 501 et seq. Section 200 of the Act [50 U.S.C. Appendix, § 520] imposes specific requirements which must be fulfilled before a default judgment can be entered, e.g., *Ledwith v. Storkan*, D.Neb.1942, 6 Fed. Rules Serv. 60b.24, Case 2, 2 F.R.D. 539, and also provides for the vacation of a judgment in certain circumstances. See discussion in Commentary, Effect of Conscription Legislation on the Federal Rules, 1940, 3

Fed. Rules Serv. 725; 3 *Moore's Federal Practice*, 1938, Cum. Supplement § 55.02.

Securities Investor Protection Act

OVERVIEW

Typically, when a brokerage firm fails, the Securities Investor Protection Corporation ("SIPC") arranges the transfer of the failed brokerage's accounts to a different securities brokerage firm. If the SIPC is unable to arrange the accounts' transfer, the failed firm is liquidated. In that case, the SIPC sends investors either certificates for the stock that was lost or a check for the market value of the shares.

Although the Bankruptcy Code provides for a stockbroker liquidation proceeding, 11 U.S.C. § 741 *et seq*., it is far more likely that a failing brokerage will find itself involved in a proceeding under the Securities Investor Protection Act of 1970 ("SIPA") (15 U.S.C. §§ 78aaa *et seq*.), rather than a Bankruptcy Code liquidation case. Brokerage firms may be liquidated under the Bankruptcy Code, however, if the SIPC does not file an application for a protective decree with the district court or if the district court finds that customers of the brokerage firm are not in need of protection under the SIPA. 15 U.S.C. §§ 78eee.

HISTORY

Before 1938, little protection existed for customers of a bankrupt stockbroker unless they could trace cash and securities held by failed stockbrokers. In 1938 Congress enacted section 60(e) of the Bankruptcy Act creating a single and separate fund concept to minimize losses to customers by giving them priority over claims of general creditors. *1898 Bankruptcy Act § 60(e)(2) (repealed)*. Because the fund was normally inadequate, however, customer losses continued.

Following a period of great expansion in the securities industry during the 1960's, a serious business contraction hit the industry in 1969-1970. This situation led to voluntary liquidations, mergers, receiverships, and bankruptcies of a substantial number of brokerage houses. Annotation, *Validity, Construction, and Application of Securities Investor Protection Act of 1970*, 23 A.L.R. Fed. 157, 179 (1975). The cash and securities customers that had deposited with these failed firms were dissipated or tied up in lengthy bankruptcy proceedings. In addition to mounting customer losses and the subsequent erosion of investor confidence, the Congress was concerned with a possible "domino effect" involving otherwise solvent brokers that had substantial open transactions with firms that failed.

Congress enacted the SIPA in reaction to this growing concern. The goal was to prevent the failure of more brokerage houses, restore investor confidence in the capital markets, and upgrade the financial responsibility requirements for registered brokers and dealers. *Securities Investor Protection Corp. v. Barbour*, 421 U.S. 412, 414 (1975). Congress designed the SIPA to apportion responsibility for carrying out the various goals of the legislation to several groups. Among them are the Securities and Exchange Commission (hereinafter referred to as SEC), various securities industry self-regulatory organizations, and the SIPC. The SIPA was designed to create a new form of liquidation proceeding. It is applicable only to member firms and was designed to accomplish the completion of open

transactions and the speedy return of most customer property. *Id*.

SIPA

The SIPA is codified in Title 15 of the United States Code at Sections 78aaa - 111. The SIPA created the SIPC, a nonprofit, private membership corporation to which most registered brokers and dealers are required to belong. 15 U.S.C. § 78ccc. The SIPC fund, which constitutes an insurance program, is authorized under 15 U.S.C. § 78ddd(a), and assessments against members are authorized by 15 U.S.C. §§ 78ddd(c) and (d). The fund is designed to protect the customers of brokers or dealers subject to the SIPA from loss in case of financial failure of the member. The fund is supported by assessments upon its members. If the fund should become inadequate, the SIPA authorizes borrowing against the U.S. Treasury. An analogy could be made to the role of the Federal Deposit Insurance Corporation in the banking industry.

BANKRUPTCY LIQUIDATION VERSUS THE SIPA LIQUIDATION IN BANKRUPTCY COURT

The essential difference between a liquidation under the Bankruptcy Code and one under the SIPA is that under the Bankruptcy Code the trustee is charged with converting securities to cash as quickly as possible and, with the exception of the delivery of customer name securities, making cash distributions to customers of the debtor in satisfaction of their claims. A SIPC trustee, on the other hand, is required to distribute securities to customers to the greatest extent practicable in satisfaction of their claims against the debtor.

There is a fundamental difference in orientation between the two proceedings. There is a statutory grant of authority to a SIPC trustee to purchase securities to satisfy customer net equity claims to specified securities. 15 U.S.C. §78fff-2(d). The trustee is required to return customer name securities to customers of the debtor (15 U.S.C. § 78fff-2(c)(2)), distribute the fund of "customer property" ratably to customers (15 U.S.C. § 78fff-2(b)), and pay, with money from the SIPC fund, remaining customer net equity claims, to the extent provided by the Act (15 U.S.C. §§ 78fff-2(b) and 3(a)). A trustee operating under the Bankruptcy Code lacks similar resources. The Code seeks to protect the filing date value of a customer's securities account by liquidating all non-customer name securities. SIPA seeks to preserve an investor's portfolio as it stood on the filing date. Under SIPA, the customer will receive securities whenever possible.

ROLE OF THE DISTRICT COURT

15 U.S.C. § 78eee(a)(3)(A) provides that the SIPC may file an application for a protective decree with the U.S. district court if the SIPC determines that any member has failed or is in danger of failing to meet obligations to customers and meets one of the four conditions specified in 15 U.S.C. § 78eee(b)(1). This application is filed as a civil case in which the SIPC or the SEC or both are named as plaintiff, and the member securities firm is named as the debtor-defendant. In the event that the SIPC refuses to act under the SIPA, the SEC may apply to the U.S. District Court for the District of Columbia to require the SIPC to discharge its obligations under the SIPA. 15 U.S.C. § 78ggg(b). By contrast, customers of failing broker-dealers do not have an implied right of action under the SIPA to compel the SIPC to exercise its statutory authority for their benefit. *Barbour,* 421 U.S.

at 425. Upon the filing of an application, the district court has exclusive jurisdiction of the debtor-defendant and its property.

The institution of a case under the SIPA brings a pending bankruptcy liquidation to a halt. Irrespective of the automatic stay, the SIPC may file an application for a protective decree under SIPA. 11 U.S.C. § 742; 15 U.S.C. § 78aaa *et seq*. The filing stays all proceedings in the bankruptcy case until the SIPC action is completed. *Id*. Pending issuance of a protective decree, the district court:

> [i.] *shall* stay any pending *bankruptcy*, mortgage foreclosure, equity receivership, or other proceeding to reorganize, conserve, or liquidate the debtor or its property and any other suit against any receiver, conservator, or trustee of the debtor or its property, and shall continue such stay upon appointment of a trustee ...
>
> [ii.] *may* stay any proceeding to enforce a lien against property of the debtor or any other suit against the debtor, including a suit by stockholders of the debtor which interferes with prosecution by the trustee of claims against former directors, officers, or employees of the debtor, and may continue such stay upon appointment of a trustee ...
>
> [iii.] *may* stay enforcement of, and upon appointment of a trustee ... [if a protective decree is issued] ... may continue the stay for such period of time as may be appropriate, but shall not abrogate any right of setoff, except to the extent such right may be affected under section 553 of Title 11, ... and shall not abrogate the right to enforce a valid, nonpreferential lien or pledge against the property of the debtor; and
>
> [iv.] *may* appoint a temporary receiver.

15 U.S.C. § 78eee(b)(2)(B)(I - iv) (emphasis added).

In addition, upon the filing of a SIPC application, 11 U.S.C. § 362 comes into effect.

The SIPA provides that the district court will issue a protective decree if the debtor consents, the debtor fails to contest the application for a protective decree, or the district court finds that one of the conditions specified in 15 U.S.C. § 78eee(b)(1) exist. If the court issues a protective decree, then the court will appoint a trustee and an attorney for the trustee whom the SIPC, in its sole discretion, specifies. 15 U.S.C. § 78eee(b)(3). Upon the issuance of a protective decree and appointment of a trustee, or a trustee and counsel, the district court will order the removal of the entire liquidation proceeding to the bankruptcy court in the same judicial district. 15 U.S.C. § 78eee(b)(4).

REMOVAL TO BANKRUPTCY COURT

The case is removed to the bankruptcy court as an adversary proceeding for liquidation. No filing or removal fee is charged. The reason for using an adversary proceeding number is historical. Although the SIPA proceedings are not bankruptcy cases, by law certain procedures prescribed in chapters 1, 3, and 5, and subchapters I and II of chapter 7 of Title 11 of the U.S. Code are applicable in SIPA proceedings. In addition,

there is no related bankruptcy case number. Statistical reports to the Administrative Office should repeat the adversary number so that the Statistics Division will know it is a SIPA matter. Forms B111A (Adversary Proceeding Opening Report) and B111B (Adversary Proceeding Closing Report) should be used since this is an adversary proceeding. For adversary proceedings within the adversary SIPA proceeding, the clerk's office should use the original adversary proceeding number for the related case number.

The SIPA requires that the bankruptcy court hold a hearing with 10 days notice to customers, creditors, and stockholders on the disinterestedness of the trustee or attorney for the trustee. 15 U.S.C. § 78eee(b)(6)(B). At the hearing, the court will entertain grounds for objection to the retention of the trustee or attorney for the trustee including, among other things, insider considerations. 15 U.S.C. § 78eee(b)(6)(A). If SIPC appoints itself as trustee, it should be deemed disinterested, and where a SIPC employee has been specified, the employee can not be disqualified solely because of his employment. *Id.* Neither the Bankruptcy Code, Bankruptcy Rules, nor SIPA provide for U.S. trustee or bankruptcy administrator involvement.

The SIPA provides for noticing of both customers and creditors. The noticing requirements provided for in 15 U.S.C. § 78fff-2(a)(1) are performed by the trustee, not the clerk of the bankruptcy court. While the SIPA does not require a formal proof of claim for customers (other than certain insiders and their relatives), it does require a written statement of claim. The trustee will normally provide customers with claim forms and instructions. The claim form must be filed with the trustee rather than the clerk of the bankruptcy court. 15 U.S.C. § 78fff-2(a)(2). With limited, specified exceptions, no claim of a customer or other creditor can be allowed unless it is received by the trustee within six months after the initial publication of notice. 15 U.S.C. § 78fff-2(a)(3).

LIQUIDATION PROCEEDINGS

The purposes of a SIPA liquidation are: (1) to deliver customer name securities to or on behalf of customers; (2) to distribute customer property and otherwise satisfy net equity claims of customers; (3) to sell or transfer offices and other productive units of the debtor's business; (4) to enforce the rights of subrogation; and (5) to liquidate the business as promptly as possible. 15 U.S.C. § 78fff(a). To the extent possible, consistent with SIPA, the liquidation is conducted in accordance with chapters 1, 3, 5 and subchapters I and II of chapter 7 of Title 11. 15 U.S.C. § 78fff(b). A section 341 meeting of creditors is conducted by the trustee. Noncustomer claims are handled as in an asset case. Costs and expenses, and priorities of distribution from the estate, are allowed as provided in section 726 of Title 11. Funds advanced by SIPC to the trustee for costs and expenses are recouped from the estate, to the extent there is any estate. 11 U.S.C. § 507.

POWERS OF THE TRUSTEE

The powers of the trustee in a SIPC case are essentially the same as those vested in a chapter 7 trustee appointed under Title 11. "In addition, a trustee may, with the approval of SIPC but without any need for court approval:

> (1) hire and fix the compensation of all personnel (including officers and employees of the debtor and of its

examining authority) and other persons (including accountants) that are deemed by the trustee necessary for all or any purposes of the liquidation proceeding;

(2) utilize SIPC employees for all or any purposes of a liquidation proceeding; and

(3) margin and maintain customer accounts of the debtor . . .”

15 U.S.C. § 78fff-1(a).

A SIPC trustee may reduce to money customer securities constituting customer property or in the general estate of the debtor. 15 U.S.C. § 78fff-1(b). The trustee must, however, deliver securities to customers to the maximum extent practicable. 15 U.S.C. § 78fff-1(b)(1). Subject to prior approval of SIPC, but again without any need for court approval, the trustee may also pay or guarantee any part of the debtor’s indebtedness to a bank, person, or other lender when certain conditions exist. 15 U.S.C. § 78fff-1(b)(2).

The trustee is responsible for investigating the acts, conduct, and condition of the debtor and reporting thereon to the court. 15 U.S.C. § 78fff-1(d)(1). The trustee must also provide a statement on the investigation to SIPC and to other persons as the court might direct. 15 U.S.C. § 78fff-1(d)(4). Moreover, the trustee must make periodic reports to the court and to SIPC on the progress of distribution of cash and securities to customers. 15 U.S.C. § 78fff-1(c).

CLAIMS

Upon receipt of a written statement of claim, the trustee promptly discharges obligations of the debtor relating to cash and securities by delivering securities or making payments to or on behalf of the customer insofar as such obligations are ascertainable from books and records of the debtor, or are otherwise established to the satisfaction of the trustee. The value of securities delivered in this regard are calculated as of the close of business on the filing date. 15 U.S.C. § 78fff-2(b).

The court must authorize the trustee to satisfy claims out of monies advanced by SIPC for this purpose, notwithstanding that the estate may not have sufficient funds for such payment. 15 U.S.C. § 78fff-2(b)(1). The court is generally not involved in the process except to the extent that a dispute arises between the trustee and customers regarding specific claims. Simple objections stay with the initial adversary proceeding. Occasionally, however, significant litigation arises in this area which generates related actions in the form of additional adversary proceedings.

DISTRIBUTION

Customer related property of the debtor is allocated in the following order:

1. To SIPC in repayment of advances made to the extent they were used to recover securities apportioned to customer property;

2. To customers of the debtor on the basis of their net equities;
3. To SIPC as subrogee for the claims of customers; and

4. To SIPC in repayment of advances made by SIPC to transfer or sell customer accounts to another SIPC member firm.

15 U.S.C. § 78fff-2(c)(1).

The trustee must deliver customer name securities to the customer if the customer is not indebted to the debtor. If indebted, the customer may, with the approval of the trustee, reclaim securities in his or her name upon payment to the trustee of all such indebtedness. 15 U.S.C. § 78fff-2(c)(2).

The trustee may, with the approval of the SIPC, sell or otherwise transfer to another member of the SIPC, without consent of any customer, all or any part of the account of a customer. 15 U.S.C. § 78fff-2(f). The trustee may also enter into any agreement, and the SIPC will advance funds as necessary, to indemnify the member firm against shortages of cash or securities in customer accounts sold or transferred. 15 U.S.C. § 78fff-2(f)(2). In addition, the trustee may purchase securities in a fair and orderly market in order to deliver securities to customers in satisfaction of their claims. 15 U.S.C. § 78fff-2(d).

To the extent customer property and the SIPC advances are not sufficient to pay or satisfy in full the net equity claims of customers, then customers are entitled to participate in the estate as unsecured creditors. 15 U.S.C. § 78fff-2(c)(1).

ADVANCES

The law requires that SIPC make advances to the trustee in order to satisfy claims and otherwise liquidate the business. These advances are made to satisfy customer claims in cash, to purchase securities to satisfy net equity claims in lieu of cash, and to pay all necessary costs and expenses of administration and liquidation of the estate to the extent the estate of the debtor is insufficient to pay said costs and expenses. Any amount advanced in satisfaction of customer claims may not exceed $500,000 per customer. 15 U.S.C. § 78fff-3(a). If part of the claim is for cash, the total amount advanced for cash payment must not exceed $100,000. 15 U.S.C. § 78fff-3(a)(1). The difference between cash payments and the maximum amount allowed can be satisfied by the delivery of securities, or cash in lieu of securities.

DIRECT PAYMENT UNDER SIPA OUTSIDE THE BANKRUPTCY COURT

In certain situations, the SIPC may elect to utilize a direct payment procedure to the customers of a debtor, thereby avoiding a trustee and the courts. Certain preconditions must exist. The claims of all customers must aggregate less than $250,000, the debtor must be financially distressed as defined in the law, and the cost to the SIPC for direct payment process must be less than for liquidation through the courts. 15 U.S.C. § 78fff-4(a).

If direct payment is utilized, the entire proceeding remains outside the court. The process remains essentially a transaction between the SIPC and the debtor's customers.

Although the SIPA provides for a direct payment procedure in lieu of instituting a liquidation proceeding, the bankruptcy court may still become involved in disputes regarding the direct payment procedure. A person aggrieved by a SIPC determination with respect to a claim in a direct payment procedure may, within six months following mailing of a SIPC determination, seek a final adjudication of such claim by the court. 15 U.S.C. § 78fff-4(e). The courts having jurisdiction over cases under Title 11

have original and exclusive jurisdiction of any civil action for the adjudication of such claims. The action is to be brought in the judicial district where the head office of the debtor is located. It would be brought as an adversary proceeding in the bankruptcy court even though there is no main case.

ROLE OF SECURITIES AND EXCHANGE COMMISSION

The SEC is responsible for regulating and supervising the activities of the SIPC. The SEC promulgates operating rules that establish the role of self-regulatory organizations and examining authorities, and their reporting responsibilities to the SIPC of inspections and reviews of its member firms. The SIPC's member firms are also required to provide information and documentation as necessary to assist in accomplishing these inspections. The penalties for fraud, deceit, or withholding of information throughout the processes covered by this law are severe. 15 U.S.C. § 78jjj(c).

COMPENSATION IN A SIPA ACTION

The SIPA specifies that the bankruptcy court must grant reasonable compensation for the services and expenses of the trustee and the attorney for the trustee. Interim allowances are also permitted. 15 U.S.C. § 78eee(b)(5)(A). Any person seeking allowances must file an application complying in form and content with provisions in Title 11, and must also serve a copy on the debtor, SIPC, creditors and other persons the court may designate. The court is required to fix a time for a hearing on the application. Notice need not be given to customers whose claims have been or will be paid in full or creditors who cannot reasonably be expected to receive any distribution. 15 U.S.C. § 78eee(b)(5)(B).

The SIPC will review the application and file its recommendation with respect to such allowances prior to the hearing on the application. In any case where the allowances are to be paid by SIPC without reasonable expectation of recoupment and there is no difference between the amount applied for and the amount recommended by SIPC, the bankruptcy court must award that amount. 15 U.S.C. § 78eee(b)(5)(C). If there is a difference, the court must, among other considerations, place considerable reliance on the recommendation of SIPC. If the estate is insufficient to cover these awards as costs of administration, 15 U.S.C. § 78eee(b)(5)(E) provides that SIPC will advance the necessary funds to cover the costs.

Bankruptcy Terminology

Most debtors who file a bankruptcy petition, and many of their creditors, know very little about the bankruptcy process. Bankruptcy Basics is designed to provide debtors, creditors, judiciary employees, and the general public with a basic explanation of bankruptcy and how it works. This glossary of bankruptcy terminology explains, in layman's terms, many of the legal terms that are used in cases filed under the Bankruptcy Code.

adversary proceeding A lawsuit arising in or related to a bankruptcy case that is commenced by filing a complaint with the court. A nonexclusive list of adversary proceedings is set forth in Fed. R. Bankr. P. 7001.

assume An agreement to continue performing duties under a contract or lease.

automatic stay An injunction that automatically stops lawsuits, foreclosures, garnishments, and all collection activity against the debtor the moment a bankruptcy petition is filed.

bankruptcy A legal procedure for dealing with debt problems of individuals and businesses; specifically, a case filed under one of the chapters of title 11 of the United States Code (the Bankruptcy Code).

bankruptcy administrator An officer of the judiciary serving in the judicial districts of Alabama and North Carolina who, like the U.S. trustee, is responsible for supervising the administration of bankruptcy cases, estates, and trustees; monitoring plans and disclosure statements; monitoring creditors' committees; monitoring fee applications; and performing other statutory duties. *Compare* **U.S. trustee.**

Bankruptcy Code The informal name for title 11 of the United States Code (11 U.S.C. §§ 101-1330), the federal bankruptcy law.

bankruptcy court The bankruptcy judges in regular active service in each federal judicial district; a unit of the district court.

bankruptcy estate All legal or equitable interests of the debtor in property at the time of the bankruptcy filing. (The estate includes all property in which the debtor has an interest, even if it is owned or held by another person.)

bankruptcy judge A judicial officer of the United States district court who is the court official with decision-making power over federal bankruptcy cases.

bankruptcy petition The document filed by the debtor (in a voluntary case) or by creditors (in an involuntary case) by which opens the bankruptcy case. (There are official forms for bankruptcy petitions.)

chapter 7 The chapter of the Bankruptcy Code providing for "liquidation" (*i.e.*, the sale of a debtor's nonexempt property and the distribution of the proceeds to creditors).

chapter 9 The chapter of the Bankruptcy Code providing for reorganization of municipalities (which includes cities and towns, as well as villages, counties, taxing districts, municipal utilities, and school districts).

chapter 11 The chapter of the Bankruptcy Code providing (generally) for reorganization, usually involving a corporation or partnership. (A chapter 11 debtor usually proposes a plan of

reorganization to keep its business alive and pay creditors over time. People in business or individuals can also seek relief in chapter 11.)

chapter 12 The chapter of the Bankruptcy Code providing for adjustment of debts of a "family farmer," or a "family fisherman" as those terms are defined in the Bankruptcy Code.

chapter 13 The chapter of the Bankruptcy Code providing for adjustment of debts of an individual with regular income. (Chapter 13 allows a debtor to keep property and pay debts over time, usually three to five years.)

chapter 15 The chapter of the Bankruptcy Code dealing with cases of cross-border insolvency.

claim A creditor's assertion of a right to payment from the debtor or the debtor's property.

confirmation Bankruptcy judges's approval of a plan of reorganization or liquidation in chapter 11, or payment plan in chapter 12 or 13.

consumer debtor A debtor whose debts are primarily consumer debts.

consumer debts Debts incurred for personal, as opposed to business, needs.

contested matter Those matters, other than objections to claims, that are disputed but are not within the definition of adversary proceeding contained in Rule 7001.

contingent claim A claim that may be owed by the debtor under certain circumstances, *e.g.,* where the debtor is a cosigner on another person's loan and that person fails to pay.

creditor One to whom the debtor owes money or who claims to be owed money by the debtor.

credit counseling Generally refers to two events in individual bankruptcy cases: (1) the "individual or group briefing" from a nonprofit budget and credit counseling agency that individual debtors must attend prior to filing under any chapter of the Bankruptcy Code; and (2) the "instructional course in personal financial management" in chapters 7 and 13 that an individual debtor must complete before a discharge is entered. There are exceptions to both requirements for certain categories of debtors, exigent circumstances, or if the U.S. trustee or bankruptcy administrator have determined that there are insufficient approved credit counseling agencies available to provide the necessary counseling.

creditors' meeting *see* **341 meeting**

current monthly income The average monthly income received by the debtor over the six calendar months before commencement of the bankruptcy case, including regular contributions to household expenses from nondebtors and income from the debtor's spouse if the petition is a joint petition, but not including social security income and certain other payments made because the debtor is the victim of certain crimes. 11 U.S.C. § 101(10A).

debtor A person who has filed a petition for relief under the Bankruptcy Code.

debtor education *see* **credit counseling**

defendant An individual (or business) against whom a lawsuit is filed.

discharge A release of a debtor from personal liability for certain dischargeable debts set forth in the Bankruptcy Code. (A discharge releases a debtor from personal liability for certain debts known as dischargeable debts and prevents the creditors owed those debts from taking any action against the debtor to collect the debts. The discharge also prohibits creditors from communicating with the debtor regarding the debt, including telephone calls, letters, and personal contact.)

dischargeable debt A debt for which the Bankruptcy Code allows the debtor's personal liability to be eliminated.

disclosure statement A written document prepared by a chapter 11 debtor or other plan proponent designed to provide "adequate information" to creditors to enable them to evaluate the chapter 11 plan of reorganization.

equity The value of a debtor's interest in property that remains after liens and other creditors' interests are considered. (Example: If a house valued at $100,000 is subject to a $80,000 mortgage, there is $20,000 of equity.)

executory contract or lease Generally includes contracts or leases under which both parties to the agreement have duties remaining to be performed. (If a contract or lease is executory, a debtor may assume it or reject it.)

exemptions, exempt property Certain property owned by an individual debtor that the Bankruptcy Code or applicable state law permits the debtor to keep from unsecured creditors. For example, in some states the debtor may be able to exempt all or a portion of the equity in the debtor's primary residence (homestead exemption), or some or all "tools of the trade" used by the debtor to make a living (*i.e.*, auto tools for an auto mechanic or dental tools for a dentist). The availability and amount of property the debtor may exempt depends on the state the debtor lives in.

family farmer or family fisherman An individual, individual and spouse, corporation, or partnership engaged in a farming or fishing operation that meets certain debt limits and other statutory criteria for filing a petition under chapter 12.

fraudulent transfer A transfer of a debtor's property made with intent to defraud or for which the debtor receives less than the transferred property's value.

fresh start The characterization of a debtor's status after bankruptcy, *i.e.*, free of most debts. (Giving debtors a fresh start is one purpose of the Bankruptcy Code.)

insider (of an individual debtor) Any relative of the debtor or of a general partner of the debtor; partnership in which the debtor is a general partner; general partner of the debtor; or a corporation of which the debtor is a director, officer, or person in control.

insider (of a corporate debtor) A director, officer, or person in control of the debtor; a partnership in which the debtor is a general partner; a general partner of the debtor; or a relative of a general partner, director, officer, or person in control of the debtor.

joint administration A court-approved mechanism under which two or more cases can be administered together. (Assuming no conflicts of interest, these separate businesses or individuals can pool their resources, hire the same professionals, etc.)

joint petition One bankruptcy petition filed by a husband and wife together.

lien The right to take and hold or sell the property of a debtor as security or payment for a debt or duty.

liquidation A sale of a debtor's property with the proceeds to be used for the benefit of creditors.

liquidated claim A creditor's claim for a fixed amount of money.

means test Section 707(b)(2) of the Bankruptcy Code applies a "means test" to determine whether an individual debtor's chapter 7 filing is presumed to be an abuse of the Bankruptcy Code requiring dismissal or conversion of the case (generally to chapter 13). Abuse is presumed if the debtor's aggregate current monthly income (see definition above) over 5 years, net of certain statutorily allowed expenses is more than (i) $10,950, or (ii) 25% of the debtor's nonpriority unsecured debt, as long as that amount is at least $6,575. The debtor may rebut a presumption of abuse only by a showing of special circumstances that justify additional expenses or adjustments of current monthly income.

motion to lift the automatic stay A request by a creditor to allow the creditor to take action against the debtor or the debtor's property that would otherwise be prohibited by the automatic stay.

no-asset case A chapter 7 case where there are no assets available to satisfy any portion of the creditors' unsecured claims.

nondischargeable debt A debt that cannot be eliminated in bankruptcy. Examples include a home mortgage, debts for alimony or child support, certain taxes, debts for most government funded or guaranteed educational loans or benefit overpayments, debts arising from death or personal injury caused by driving while intoxicated or under the influence of drugs, and debts for restitution or a criminal fine included in a sentence on the debtor's conviction of a crime. Some debts, such as debts for money or property obtained by false pretenses and debts for fraud or defalcation while acting in a fiduciary capacity may be declared nondischargeable only if a creditor timely files and prevails in a nondischargeability action.

objection to dischargeability A trustee's or creditor's objection to the debtor being released from personal liability for certain dischargeable debts. Common reasons include allegations that the debt to be discharged was incurred by false pretenses or that debt arose because of the debtor's fraud while acting as a fiduciary.

objection to exemptions A trustee's or creditor's objection to the debtor's attempt to claim certain property as exempt from liquidation by the trustee to creditors.

party in interest A party who has standing to be heard by the court in a matter to be decided in the bankruptcy case. The debtor, the U.S. trustee or bankruptcy administrator, the case trustee and creditors are parties in interest for most matters.

petition preparer A business not authorized to practice law that prepares bankruptcy petitions.

plan A debtor's detailed description of how the debtor proposes to pay creditors' claims over a fixed period of time.

plaintiff A person or business that files a formal complaint with the court.

postpetition transfer A transfer of the debtor's property made after the commencement of the case.

prebankruptcy planning The arrangement (or rearrangement) of a debtor's property to allow the debtor to take maximum advantage of exemptions. (Prebankruptcy planning typically includes converting nonexempt assets into exempt assets.)

preference or preferential debt payment A debt payment made to a creditor in the 90-day period before a debtor files bankruptcy (or within one year if the creditor was an insider) that gives the creditor more than the creditor would receive in the debtor's chapter 7 case.

presumption of abuse *see* **means test**

priority The Bankruptcy Code's statutory ranking of unsecured claims that determines the order in which unsecured claims will be paid if there is not enough money to pay all unsecured claims in full. For example, under the Bankruptcy Code's priority scheme, money owed to the case trustee or for prepetition alimony and/or child support must be paid in full before any general unsecured debt (*i.e.* trade debt or credit card debt) is paid.

priority claim An unsecured claim that is entitled to be paid ahead of other unsecured claims that are not entitled to priority status. Priority refers to the order in which these unsecured claims are to be paid.

proof of claim A written statement and verifying documentation filed by a creditor that describes the reason the debtor owes the creditor money. (There is an official form for this purpose.)

property of the estate All legal or equitable interests of the debtor in property as of the commencement of the case.

reaffirmation agreement An agreement by a chapter 7 debtor to continue paying a dischargeable debt (such as an auto loan) after the bankruptcy, usually for the purpose of keeping collateral (*i.e.* the car) that would otherwise be subject to repossession.

secured creditor A creditor holding a claim against the debtor who has the right to take and hold or sell certain property of the debtor in satisfaction of some or all of the claim.

secured debt Debt backed by a mortgage, pledge of collateral, or other lien; debt for which the creditor has the right to pursue specific pledged property upon default. Examples include home mortgages, auto loans and tax liens.

schedules Detailed lists filed by the debtor along with (or shortly after filing) the petition showing the debtor's assets, liabilities, and other financial information. (There are official forms a debtor must use.)

small business case A special type of chapter 11 case in which there is no creditors' committee (or the creditors' committee is deemed inactive by the court) and in which the debtor is subject to more oversight by the U.S. trustee than other chapter 11 debtors. The Bankruptcy Code

contains certain provisions designed to reduce the time a small business debtor is in bankruptcy.

statement of financial affairs A series of questions the debtor must answer in writing concerning sources of income, transfers of property, lawsuits by creditors, etc. (There is an official form a debtor must use.)

statement of intention A declaration made by a chapter 7 debtor concerning plans for dealing with consumer debts that are secured by property of the estate.

substantive consolidation Putting the assets and liabilities of two or more related debtors into a single pool to pay creditors. (Courts are reluctant to allow substantive consolidation since the action must not only justify the benefit that one set of creditors receives, but also the harm that other creditors suffer as a result.)

341 meeting The meeting of creditors required by section 341 of the Bankruptcy Code at which the debtor is questioned under oath by creditors, a trustee, examiner, or the U.S. trustee about his/her financial affairs. Also called **creditors' meeting**

transfer Any mode or means by which a debtor disposes of or parts with the debtor's property.

trustee The representative of the bankruptcy estate who exercises statutory powers, principally for the benefit of the unsecured creditors, under the general supervision of the court and the direct supervision of the U.S. trustee or bankruptcy administrator. The trustee is a private individual or corporation appointed in all chapter 7, chapter 12, and chapter 13 cases and some chapter 11 cases. The trustee's responsibilities include reviewing the debtor's petition and schedules and bringing actions against creditors or the debtor to recover property of the bankruptcy estate. In chapter 7, the trustee liquidates property of the estate, and makes distributions to creditors. Trustees in chapter 12 and 13 have similar duties to a chapter 7 trustee and the additional responsibilities of overseeing the debtor's plan, receiving payments from debtors, and disbursing plan payments to creditors.

U.S. trustee An officer of the Justice Department responsible for supervising the administration of bankruptcy cases, estates, and trustees; monitoring plans and disclosure statements; monitoring creditors' committees; monitoring fee applications; and performing other statutory duties. *Compare*, **bankruptcy administrator**.

undersecured claim A debt secured by property that is worth less than the full amount of the debt.

unliquidated claim A claim for which a specific value has not been determined.

unscheduled debt A debt that should have been listed by the debtor in the schedules filed with the court but was not. (Depending on the circumstances, an unscheduled debt may or may not be discharged.)

unsecured claim A claim or debt for which a creditor holds no special assurance of payment, such as a mortgage or lien; a debt for which credit was extended based solely upon the creditor's assessment of the debtor's future ability to pay.

voluntary transfer A transfer of a debtor's property with the debtor's consent.

Everyone Should Plan for a Financial Catastrophe

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For years I have advocated that everyone, particularly business owners, should make a concerted effort to learn what would happen if a financial disaster befell them or their business. As a bankruptcy attorney I have seen once wealthy individuals and thriving businesses fall on bad times, often due to health reasons, business reversals, and divorce. However, who would have thought that the entire world would be struck with the devastating consequences of the COVID-19 Virus? There is no better example than COVID-19 that a catastrophe can hit any one of us at any time. Sadly, we have only seen the beginning of business failures due to COVID-19. Many closely held small businesses have shut their doors never to re-open. Where does that leave the owners of those businesses? The answer may rest with whether they planned for a financial catastrophe or were just lucky.

Financially successful individuals and business owners do want to think about what might happen if an unfortunate life altering event were to happen to them. It's like not wanting to spend time and thought making one's own funeral arrangements. Who wants to focus on negative events, even those that are inevitable like death? But, not planning for what might happen in the future is like not having car, fire or health insurance. One event can financially ruin a once successful person or business. That is why everyone should have at least a modicum of knowledge that could protect assets should a catastrophic event occur.

Simply incorporating a business shields the owners from most personal liability exposure. However most small business owners often sign papers they do not understand. Moreover many do not even keep copies of what they signed for future reference. While it may be difficult, co-signing or personally guaranteeing a corporate obligation should be avoided if possible. All paperwork should be maintained for future reference. Very often clients do not even know that they are personally liable for business debts until they are sued in their individual name.

If married and starting or engaged in a business, consideration should be given whether it is advisable to transfer the marital residence to the other spouse if that person is less likely to be at potential personal financial risk in the future. This assumes a solid marriage and that the conveyance is not a fraud on creditors (which is a whole other article in itself).

If a home is jointly owned by a husband and wife, in New York a judgment creditor of only one spouse is prohibited from selling the marital home to satisfy the debt. However judgments obtained against one spouse and filed with the County Clerk will remain a lien against that spouse's interest for ten years. The lien can be renewed prior to the expiration of the tenth year. The judgment will also incur statutory interest of 9% a year, a tremendous interest rate in today's market. When owners seek to refinance or sell their home the judgment will have to be satisfied. In a bankruptcy scenario, (if appropriate) a judgment debtor that owns a house will be able to shield and keep up to $170,825 (in the New York Metropolitan area) from a judgment creditor. The same exemption applies in a forced judgment foreclosure sale. Interestingly some judgment creditors with liens on real property that have a lot of equity and are capable of being foreclosed upon (i.e. not owned with a spouse) are quite comfortable sitting with their judgment knowing that they cannot generate a 9% rate of return on their money elsewhere.

Business owners in distress often sign Confessions of Judgment (usually associated with merchant cash advances) take out home equity loans or grant collateral mortgages on their home to lenders to secure business obligations. This places their most precious asset at risk when other options may have been available to discharge that debt and preserve exempt equity in their residence. Worse is where a spouse, who is not obligated for the debt or involved in the business, agrees to guarantee the debt or consents to placement of a mortgage against their interest in the home.

Similarly, pensions and retirement accounts that are outside the reach of most creditors (some exceptions: IRS debt and domestic support obligations) are often lost by being sunk into businesses destined to fail. An entire lifetime of savings meant for retirement can be lost very quickly if proper planning is not done.

Fiduciary taxes, (sales and withholding) carry personal liability to not only the officers of a company but to those with check writing privileges. These taxes cannot be discharged in bankruptcy.

Sometimes it makes sense to invest one's personal funds or those of willing family members into a business. Too often those transactions are not supported by proper paperwork and the people the business owner wants to protect the most, including themselves and family members, are not protected at all. Transactions with family members should be documented the same way an arms-length creditor would require. The transaction will then more likely pass muster as a legitimate debtor/creditor relationship, not a gift or a capital contribution. The devil is always in the details. If the transaction is well thought out it can accomplish the intent of the parties and less likely be exposed to outside legal attack when things do not go as planned.

The bottom line is that everyone needs to think about what might happen if a catastrophe arises for them. Consulting with the proper professional can likely lessen the financial damage of an unexpected event.

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N.Y. Debt. & Cred. Law § 282

Section 282 - Permissible exemptions in bankruptcy

Under section five hundred twenty-two of title eleven of the United States Code, entitled "Bankruptcy", an individual debtor domiciled in this state may exempt from the property of the estate, to the extent permitted by subsection (b) thereof, only (i) personal and real property exempt from application to the satisfaction of money judgments under sections fifty-two hundred five and fifty-two hundred six of the civil practice law and rules, (ii) insurance policies and annuity contracts and the proceeds and avails thereof as provided in section three thousand two hundred twelve of the insurance law and (iii) the following property:

1. Bankruptcy exemption of a motor vehicle. One motor vehicle not exceeding four thousand dollars in value above liens and encumbrances of the debtor; provided, however, if such vehicle has been equipped for use by a disabled debtor, then ten thousand dollars in value above liens and encumbrances of the debtor.

2. Bankruptcy exemption for right to receive benefits. The debtor's right to receive or the debtor's interest in: (a) a social security benefit, unemployment compensation or a local public assistance benefit; (b) a veterans' benefit; (c) a disability, illness, or unemployment benefit; (d) alimony, support, or separate maintenance, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor; and (e) all payments under a stock bonus, pension, profit sharing, or similar plan or contract on account of illness, disability, death, age, or length of service unless (i) such plan or contract, except those qualified under section 401, 408 or 408A of the United States Internal Revenue Code of 1986, as amended, was established by the debtor or under the auspices of an insider that employed the debtor at the time the debtor's rights under such plan or contract arose, (ii) such plan is on account of age or length of service, and (iii) such plan or contract does not qualify under section four hundred one (a), four hundred three (a), four hundred three (b), four hundred eight, four hundred eight A, four hundred nine or four hundred fifty-seven of the Internal Revenue Code of nineteen hundred eighty-six, as amended.

3. Bankruptcy exemption for right to receive certain property. The debtor's right to receive, or property that is traceable to: (i) an award under a crime victim's reparation law; (ii) a payment on account of the wrongful death of an individual of whom the debtor was a dependent to the extent reasonably necessary for the support of the debtor and any dependent of the debtor; (iii) a payment, not to exceed seventy-five hundred dollars on account of personal bodily injury, not including pain and suffering or compensation for actual pecuniary loss, of the debtor or an individual of whom the debtor is a dependent; and (iv) a payment in compensation of loss of future earnings of the debtor or an individual of whom the debtor is or was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor.

N.Y. Debt. and Cred. Law § 282

N.Y. Debt. & Cred. Law § 283

Section 283 - Aggregate individual bankruptcy exemption for certain annuities and personal property

1. General application. The aggregate amount the debtor may exempt from the property of the estate for personal property exempt from application to the satisfaction of a money judgment under subdivision (a) of section fifty-two hundred five of the civil practice law and rules and for benefits, rights, privileges, and options of annuity contracts described in the following sentence shall not exceed ten thousand dollars. Annuity contracts subject to the foregoing limitation are those that are: (a) initially purchased by the debtor within six months of the debtor's filing a petition in bankruptcy, (b) not described in any paragraph of section eight hundred five (d) of the Internal Revenue Code of nineteen hundred fifty-four, and (c) not purchased by application of proceeds under settlement options of annuity contracts purchased more than six months before the debtor's filing a petition in bankruptcy or under settlement options of life insurance policies.

2. Contingent alternative bankruptcy exemption. Notwithstanding section two hundred eighty-two of this article, a debtor, who (a) does not elect, claim, or otherwise avail himself of an exemption described in section fifty-two hundred six of the civil practice law and rules; (b) utilizes to the fullest extent permitted by law as applied to said debtor's property, the exemptions referred to in subdivision one of this section which are subject to the ten thousand dollar aggregate limit; and (c) does not reach such aggregate limit, may exempt cash in the amount by which ten thousand dollars exceeds the aggregate of his or her exemptions referred to in subdivision one of this section or in the amount of five thousand dollars, whichever amount is less. For purposes of this subdivision, cash means currency of the United States at face value, savings bonds of the United States at face value, the right to receive a refund of federal, state and local income taxes, and deposit accounts in any state or federally chartered depository institution.

N.Y. Debt. and Cred. Law § 283

11 U.S.C. § 362

Section 362 - Automatic stay

(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970, operates as a stay, applicable to all entities, of-

(1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;

(2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;

(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;

(4) any act to create, perfect, or enforce any lien against property of the estate;

(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;

(6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;

(7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and

(8) the commencement or continuation of a proceeding before the United States Tax Court concerning a tax liability of a debtor that is a corporation for a taxable period the bankruptcy court may determine or concerning the tax liability of a debtor who is an individual for a taxable period ending before the date of the order for relief under this title.

(b) The filing of a petition under section 301, 302, or 303 of this title, or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, does not operate as a stay-

(1) under subsection (a) of this section, of the commencement or continuation of a criminal action or proceeding against the debtor;

(2) under subsection (a)-

(A) of the commencement or continuation of a civil action or proceeding-

(i) for the establishment of paternity;

(ii) for the establishment or modification of an order for domestic support obligations;

(iii) concerning child custody or visitation;

(iv) for the dissolution of a marriage, except to the extent that such proceeding seeks to determine the division of property that is property of the estate; or

(v) regarding domestic violence;

(B) of the collection of a domestic support obligation from property that is not property of the estate;

(C) with respect to the withholding of income that is property of the estate or property of the debtor for payment of a domestic support obligation under a judicial or administrative order or a statute;

(D) of the withholding, suspension, or restriction of a driver's license, a professional or occupational license, or a recreational license, under State law, as specified in section 466(a)(16) of the Social Security Act;

(E) of the reporting of overdue support owed by a parent to any consumer reporting agency as specified in section 466(a)(7) of the Social Security Act;

(F) of the interception of a tax refund, as specified in sections 464 and 466(a)(3) of the Social Security Act or under an analogous State law; or

(G) of the enforcement of a medical obligation, as specified under title IV of the Social Security Act;

(3) under subsection (a) of this section, of any act to perfect, or to maintain or continue the perfection of, an interest in property to the extent that the trustee's rights and powers are subject to such perfection under section 546(b) of this title or to the extent that such act is accomplished within the period provided under section 547(e)(2)(A) of this title;

(4) under paragraph (1), (2), (3), or (6) of subsection (a) of this section, of the commencement or continuation of an action or proceeding by a governmental unit or any organization exercising authority under the Convention on the Prohibition of the Development, Production, Stockpiling and Use of Chemical Weapons and on Their Destruction, opened for signature on January 13, 1993, to enforce such governmental unit's or organization's police and regulatory power, including the enforcement of a judgment other than a money judgment, obtained in an action or proceeding by the governmental unit to enforce such governmental unit's or organization's police or regulatory power;

[(5) Repealed. Pub. L. 105-277, div. I, title VI, §603(1), Oct. 21, 1998, 112 Stat. 2681-866;]

(6) under subsection (a) of this section, of the exercise by a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities

clearing agency of any contractual right (as defined in section 555 or 556) under any security agreement or arrangement or other credit enhancement forming a part of or related to any commodity contract, forward contract or securities contract, or of any contractual right (as defined in section 555 or 556) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such contracts, including any master agreement for such contracts;

(7) under subsection (a) of this section, of the exercise by a repo participant or financial participant of any contractual right (as defined in section 559) under any security agreement or arrangement or other credit enhancement forming a part of or related to any repurchase agreement, or of any contractual right (as defined in section 559) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such agreements, including any master agreement for such agreements;

(8) under subsection (a) of this section, of the commencement of any action by the Secretary of Housing and Urban Development to foreclose a mortgage or deed of trust in any case in which the mortgage or deed of trust held by the Secretary is insured or was formerly insured under the National Housing Act and covers property, or combinations of property, consisting of five or more living units;

(9) under subsection (a), of-

(A) an audit by a governmental unit to determine tax liability;

(B) the issuance to the debtor by a governmental unit of a notice of tax deficiency;

(C) a demand for tax returns; or

(D) the making of an assessment for any tax and issuance of a notice and demand for payment of such an assessment (but any tax lien that would otherwise attach to property of the estate by reason of such an assessment shall not take effect unless such tax is a debt of the debtor that will not be discharged in the case and such property or its proceeds are transferred out of the estate to, or otherwise revested in, the debtor).

(10) under subsection (a) of this section, of any act by a lessor to the debtor under a lease of nonresidential real property that has terminated by the expiration of the stated term of the lease before the commencement of or during a case under this title to obtain possession of such property;

(11) under subsection (a) of this section, of the presentment of a negotiable instrument and the giving of notice of and protesting dishonor of such an instrument;

(12) under subsection (a) of this section, after the date which is 90 days after the filing of such petition, of the commencement or continuation, and conclusion to the entry of final judgment, of an action which involves a debtor subject to reorganization pursuant to chapter 11 of this title and which was brought by the Secretary of Transportation under section 31325 of title 46 (including distribution of any proceeds of sale) to foreclose a preferred ship or fleet mortgage, or a security interest in or relating to a vessel or vessel

under construction, held by the Secretary of Transportation under chapter 537 of title 46 or section 109(h) of title 49, or under applicable State law;

(13) under subsection (a) of this section, after the date which is 90 days after the filing of such petition, of the commencement or continuation, and conclusion to the entry of final judgment, of an action which involves a debtor subject to reorganization pursuant to chapter 11 of this title and which was brought by the Secretary of Commerce under section 31325 of title 46 (including distribution of any proceeds of sale) to foreclose a preferred ship or fleet mortgage in a vessel or a mortgage, deed of trust, or other security interest in a fishing facility held by the Secretary of Commerce under chapter 537 of title 46;

(14) under subsection (a) of this section, of any action by an accrediting agency regarding the accreditation status of the debtor as an educational institution;

(15) under subsection (a) of this section, of any action by a State licensing body regarding the licensure of the debtor as an educational institution;

(16) under subsection (a) of this section, of any action by a guaranty agency, as defined in section 435(j) of the Higher Education Act of 1965 or the Secretary of Education regarding the eligibility of the debtor to participate in programs authorized under such Act;

(17) under subsection (a) of this section, of the exercise by a swap participant or financial participant of any contractual right (as defined in section 560) under any security agreement or arrangement or other credit enhancement forming a part of or related to any swap agreement, or of any contractual right (as defined in section 560) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such agreements, including any master agreement for such agreements;

(18) under subsection (a) of the creation or perfection of a statutory lien for an ad valorem property tax, or a special tax or special assessment on real property whether or not ad valorem, imposed by a governmental unit, if such tax or assessment comes due after the date of the filing of the petition;

(19) under subsection (a), of withholding of income from a debtor's wages and collection of amounts withheld, under the debtor's agreement authorizing that withholding and collection for the benefit of a pension, profit-sharing, stock bonus, or other plan established under section 401, 403, 408, 408A, 414, 457, or 501(c) of the Internal Revenue Code of 1986, that is sponsored by the employer of the debtor, or an affiliate, successor, or predecessor of such employer-

(A) to the extent that the amounts withheld and collected are used solely for payments relating to a loan from a plan under section 408(b)(1) of the Employee Retirement Income Security Act of 1974 or is subject to section 72(p) of the Internal Revenue Code of 1986; or

(B) a loan from a thrift savings plan permitted under subchapter III of chapter 84 of title 5, that satisfies the requirements of section 8433(g) of such title;
but nothing in this paragraph may be construed to provide that any loan made under a governmental plan under section 414(d), or a contract or account under section 403(b), of the Internal Revenue Code of 1986 constitutes a claim or a debt under this title;

(20) under subsection (a), of any act to enforce any lien against or security interest in real property following entry of the order under subsection (d)(4) as to such real property in any prior case under this title, for a period of 2 years after the date of the entry of such an order, except that the debtor, in a subsequent case under this title, may move for relief from such order based upon changed circumstances or for other good cause shown, after notice and a hearing;

(21) under subsection (a), of any act to enforce any lien against or security interest in real property-

(A) if the debtor is ineligible under section 109(g) to be a debtor in a case under this title; or

(B) if the case under this title was filed in violation of a bankruptcy court order in a prior case under this title prohibiting the debtor from being a debtor in another case under this title;

(22) subject to subsection (l), under subsection (a)(3), of the continuation of any eviction, unlawful detainer action, or similar proceeding by a lessor against a debtor involving residential property in which the debtor resides as a tenant under a lease or rental agreement and with respect to which the lessor has obtained before the date of the filing of the bankruptcy petition, a judgment for possession of such property against the debtor;

(23) subject to subsection (m), under subsection (a)(3), of an eviction action that seeks possession of the residential property in which the debtor resides as a tenant under a lease or rental agreement based on endangerment of such property or the illegal use of controlled substances on such property, but only if the lessor files with the court, and serves upon the debtor, a certification under penalty of perjury that such an eviction action has been filed, or that the debtor, during the 30-day period preceding the date of the filing of the certification, has endangered property or illegally used or allowed to be used a controlled substance on the property;

(24) under subsection (a), of any transfer that is not avoidable under section 544 and that is not avoidable under section 549;

(25) under subsection (a), of-

(A) the commencement or continuation of an investigation or action by a securities self regulatory organization to enforce such organization's regulatory power;

(B) the enforcement of an order or decision, other than for monetary sanctions, obtained in an action by such securities self regulatory organization to enforce such organization's regulatory power; or

(C) any act taken by such securities self regulatory organization to delist, delete, or refuse to permit quotation of any stock that does not meet applicable regulatory requirements;

(26) under subsection (a), of the setoff under applicable nonbankruptcy law of an income tax refund, by a governmental unit, with respect to a taxable period that ended before the date of the order for relief against an income tax liability for a taxable period that also ended before the date of the order for relief, except that in any case in which the setoff of an income tax refund is not permitted under applicable nonbankruptcy law because of a pending action to determine the amount or legality of a tax liability, the governmental unit may hold the refund pending the resolution of the action, unless the court, on the motion of the trustee and after notice and a hearing, grants the taxing authority adequate protection (within the meaning of section 361) for the secured claim of such authority in the setoff under section 506(a);

(27) under subsection (a) of this section, of the exercise by a master netting agreement participant of any contractual right (as defined in section 555, 556, 559, or 560) under any security agreement or arrangement or other credit enhancement forming a part of or related to any master netting agreement, or of any contractual right (as defined in section 555, 556, 559, or 560) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such master netting agreements to the extent that such participant is eligible to exercise such rights under paragraph (6), (7), or (17) for each individual contract covered by the master netting agreement in issue; and

(28) under subsection (a), of the exclusion by the Secretary of Health and Human Services of the debtor from participation in the medicare program or any other Federal health care program (as defined in section 1128B(f) of the Social Security Act pursuant to title XI or XVIII of such Act).

The provisions of paragraphs (12) and (13) of this subsection shall apply with respect to any such petition filed on or before December 31, 1989.

(c) Except as provided in subsections (d), (e), (f), and (h) of this section-

(1) the stay of an act against property of the estate under subsection (a) of this section continues until such property is no longer property of the estate;

(2) the stay of any other act under subsection (a) of this section continues until the earliest of-

(A) the time the case is closed;

(B) the time the case is dismissed; or

(C) if the case is a case under chapter 7 of this title concerning an individual or a case under chapter 9, 11, 12, or 13 of this title, the time a discharge is granted or denied;

(3) if a single or joint case is filed by or against a debtor who is an individual in a case under chapter 7, 11, or 13, and if a single or joint case of the debtor was pending within

the preceding 1-year period but was dismissed, other than a case refiled under a chapter other than chapter 7 after dismissal under section 707(b)-

(A) the stay under subsection (a) with respect to any action taken with respect to a debt or property securing such debt or with respect to any lease shall terminate with respect to the debtor on the 30th day after the filing of the later case;

(B) on the motion of a party in interest for continuation of the automatic stay and upon notice and a hearing, the court may extend the stay in particular cases as to any or all creditors (subject to such conditions or limitations as the court may then impose) after notice and a hearing completed before the expiration of the 30-day period only if the party in interest demonstrates that the filing of the later case is in good faith as to the creditors to be stayed; and

(C) for purposes of subparagraph (B), a case is presumptively filed not in good faith (but such presumption may be rebutted by clear and convincing evidence to the contrary)-

(i) as to all creditors, if-

(I) more than 1 previous case under any of chapters 7, 11, and 13 in which the individual was a debtor was pending within the preceding 1-year period;

(II) a previous case under any of chapters 7, 11, and 13 in which the individual was a debtor was dismissed within such 1-year period, after the debtor failed to-

(aa) file or amend the petition or other documents as required by this title or the court without substantial excuse (but mere inadvertence or negligence shall not be a substantial excuse unless the dismissal was caused by the negligence of the debtor's attorney);

(bb) provide adequate protection as ordered by the court; or

(cc) perform the terms of a plan confirmed by the court; or

(III) there has not been a substantial change in the financial or personal affairs of the debtor since the dismissal of the next most previous case under chapter 7, 11, or 13 or any other reason to conclude that the later case will be concluded-

(aa) if a case under chapter 7, with a discharge; or

(bb) if a case under chapter 11 or 13, with a confirmed plan that will be fully performed; and

(ii) as to any creditor that commenced an action under subsection (d) in a previous case in which the individual was a debtor if, as of the date of dismissal of such case, that action was still pending or had been resolved by terminating, conditioning, or limiting the stay as to actions of such creditor; and

(4)

(A)

(i) if a single or joint case is filed by or against a debtor who is an individual under this title, and if 2 or more single or joint cases of the debtor were pending within the

previous year but were dismissed, other than a case refiled under a chapter other than chapter 7 after dismissal under section 707(b), the stay under subsection (a) shall not go into effect upon the filing of the later case; and

(ii) on request of a party in interest, the court shall promptly enter an order confirming that no stay is in effect;

(B) if, within 30 days after the filing of the later case, a party in interest requests the court may order the stay to take effect in the case as to any or all creditors (subject to such conditions or limitations as the court may impose), after notice and a hearing, only if the party in interest demonstrates that the filing of the later case is in good faith as to the creditors to be stayed;

(C) a stay imposed under subparagraph (B) shall be effective on the date of the entry of the order allowing the stay to go into effect; and

(D) for purposes of subparagraph (B), a case is presumptively filed not in good faith (but such presumption may be rebutted by clear and convincing evidence to the contrary)-

(i) as to all creditors if-

(I) 2 or more previous cases under this title in which the individual was a debtor were pending within the 1-year period;

(II) a previous case under this title in which the individual was a debtor was dismissed within the time period stated in this paragraph after the debtor failed to file or amend the petition or other documents as required by this title or the court without substantial excuse (but mere inadvertence or negligence shall not be substantial excuse unless the dismissal was caused by the negligence of the debtor's attorney), failed to provide adequate protection as ordered by the court, or failed to perform the terms of a plan confirmed by the court; or

(III) there has not been a substantial change in the financial or personal affairs of the debtor since the dismissal of the next most previous case under this title, or any other reason to conclude that the later case will not be concluded, if a case under chapter 7, with a discharge, and if a case under chapter 11 or 13, with a confirmed plan that will be fully performed; or

(ii) as to any creditor that commenced an action under subsection (d) in a previous case in which the individual was a debtor if, as of the date of dismissal of such case, such action was still pending or had been resolved by terminating, conditioning, or limiting the stay as to such action of such creditor.

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay-

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest;

(2) with respect to a stay of an act against property under subsection (a) of this section, if-

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization;

(3) with respect to a stay of an act against single asset real estate under subsection (a), by a creditor whose claim is secured by an interest in such real estate, unless, not later than the date that is 90 days after the entry of the order for relief (or such later date as the court may determine for cause by order entered within that 90-day period) or 30 days after the court determines that the debtor is subject to this paragraph, whichever is later-

(A) the debtor has filed a plan of reorganization that has a reasonable possibility of being confirmed within a reasonable time; or

(B) the debtor has commenced monthly payments that-

(i) may, in the debtor's sole discretion, notwithstanding section 363(c)(2), be made from rents or other income generated before, on, or after the date of the commencement of the case by or from the property to each creditor whose claim is secured by such real estate (other than a claim secured by a judgment lien or by an unmatured statutory lien); and

(ii) are in an amount equal to interest at the then applicable nondefault contract rate of interest on the value of the creditor's interest in the real estate; or

(4) with respect to a stay of an act against real property under subsection (a), by a creditor whose claim is secured by an interest in such real property, if the court finds that the filing of the petition was part of a scheme to delay, hinder, or defraud creditors that involved either-

(A) transfer of all or part ownership of, or other interest in, such real property without the consent of the secured creditor or court approval; or

(B) multiple bankruptcy filings affecting such real property.

If recorded in compliance with applicable State laws governing notices of interests or liens in real property, an order entered under paragraph (4) shall be binding in any other case under this title purporting to affect such real property filed not later than 2 years after the date of the entry of such order by the court, except that a debtor in a subsequent case under this title may move for relief from such order based upon changed circumstances or for good cause shown, after notice and a hearing. Any Federal, State, or local governmental unit that accepts notices of interests or liens in real property shall accept any certified copy of an order described in this subsection for indexing and recording.

(e)

(1) Thirty days after a request under subsection (d) of this section for relief from the stay of any act against property of the estate under subsection (a) of this section, such stay is terminated with respect to the party in interest making such request, unless the court, after notice and a hearing, orders such stay continued in effect pending the conclusion of, or as a result of, a final hearing and determination under subsection (d) of this section. A

hearing under this subsection may be a preliminary hearing, or may be consolidated with the final hearing under subsection (d) of this section. The court shall order such stay continued in effect pending the conclusion of the final hearing under subsection (d) of this section if there is a reasonable likelihood that the party opposing relief from such stay will prevail at the conclusion of such final hearing. If the hearing under this subsection is a preliminary hearing, then such final hearing shall be concluded not later than thirty days after the conclusion of such preliminary hearing, unless the 30-day period is extended with the consent of the parties in interest or for a specific time which the court finds is required by compelling circumstances.

(2) Notwithstanding paragraph (1), in a case under chapter 7, 11, or 13 in which the debtor is an individual, the stay under subsection (a) shall terminate on the date that is 60 days after a request is made by a party in interest under subsection (d), unless-

(A) a final decision is rendered by the court during the 60-day period beginning on the date of the request; or

(B) such 60-day period is extended-

(i) by agreement of all parties in interest; or

(ii) by the court for such specific period of time as the court finds is required for good cause, as described in findings made by the court.

(f) Upon request of a party in interest, the court, with or without a hearing, shall grant such relief from the stay provided under subsection (a) of this section as is necessary to prevent irreparable damage to the interest of an entity in property, if such interest will suffer such damage before there is an opportunity for notice and a hearing under subsection (d) or (e) of this section.

(g) In any hearing under subsection (d) or (e) of this section concerning relief from the stay of any act under subsection (a) of this section-

(1) the party requesting such relief has the burden of proof on the issue of the debtor's equity in property; and

(2) the party opposing such relief has the burden of proof on all other issues.

(h)

(1) In a case in which the debtor is an individual, the stay provided by subsection (a) is terminated with respect to personal property of the estate or of the debtor securing in whole or in part a claim, or subject to an unexpired lease, and such personal property shall no longer be property of the estate if the debtor fails within the applicable time set by section 521(a)(2)-

(A) to file timely any statement of intention required under section 521(a)(2) with respect to such personal property or to indicate in such statement that the debtor will either surrender such personal property or retain it and, if retaining such personal property, either redeem such personal property pursuant to section 722, enter into an agreement of the kind specified in section 524(c) applicable to the debt secured by such personal property, or assume such unexpired lease pursuant to section 365(p) if the trustee does not do so, as applicable; and

(B) to take timely the action specified in such statement, as it may be amended before expiration of the period for taking action, unless such statement specifies the debtor's intention to reaffirm such debt on the original contract terms and the creditor refuses to agree to the reaffirmation on such terms.

(2) Paragraph (1) does not apply if the court determines, on the motion of the trustee filed before the expiration of the applicable time set by section 521(a)(2), after notice and a hearing, that such personal property is of consequential value or benefit to the estate, and orders appropriate adequate protection of the creditor's interest, and orders the debtor to deliver any collateral in the debtor's possession to the trustee. If the court does not so determine, the stay provided by subsection (a) shall terminate upon the conclusion of the hearing on the motion.

(i) If a case commenced under chapter 7, 11, or 13 is dismissed due to the creation of a debt repayment plan, for purposes of subsection (c)(3), any subsequent case commenced by the debtor under any such chapter shall not be presumed to be filed not in good faith.
(j) On request of a party in interest, the court shall issue an order under subsection (c) confirming that the automatic stay has been terminated.
(k)

(1) Except as provided in paragraph (2), an individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages.

(2) If such violation is based on an action taken by an entity in the good faith belief that subsection (h) applies to the debtor, the recovery under paragraph (1) of this subsection against such entity shall be limited to actual damages.

(l)

(1) Except as otherwise provided in this subsection, subsection (b)(22) shall apply on the date that is 30 days after the date on which the bankruptcy petition is filed, if the debtor files with the petition and serves upon the lessor a certification under penalty of perjury that-

(A) under nonbankruptcy law applicable in the jurisdiction, there are circumstances under which the debtor would be permitted to cure the entire monetary default that gave rise to the judgment for possession, after that judgment for possession was entered; and

(B) the debtor (or an adult dependent of the debtor) has deposited with the clerk of the court, any rent that would become due during the 30-day period after the filing of the bankruptcy petition.

(2) If, within the 30-day period after the filing of the bankruptcy petition, the debtor (or an adult dependent of the debtor) complies with paragraph (1) and files with the court and serves upon the lessor a further certification under penalty of perjury that the debtor (or an adult dependent of the debtor) has cured, under nonbankruptcy law applicable in the jurisdiction, the entire monetary default that gave rise to the judgment under which possession is sought by the lessor, subsection (b)(22) shall not apply, unless ordered to apply by the court under paragraph (3).

(3)

(A) If the lessor files an objection to any certification filed by the debtor under paragraph (1) or (2), and serves such objection upon the debtor, the court shall hold a hearing within 10 days after the filing and service of such objection to determine if the certification filed by the debtor under paragraph (1) or (2) is true.

(B) If the court upholds the objection of the lessor filed under subparagraph (A)-

(i) subsection (b)(22) shall apply immediately and relief from the stay provided under subsection (a)(3) shall not be required to enable the lessor to complete the process to recover full possession of the property; and

(ii) the clerk of the court shall immediately serve upon the lessor and the debtor a certified copy of the court's order upholding the lessor's objection.

(4) If a debtor, in accordance with paragraph (5), indicates on the petition that there was a judgment for possession of the residential rental property in which the debtor resides and does not file a certification under paragraph (1) or (2)-

(A) subsection (b)(22) shall apply immediately upon failure to file such certification, and relief from the stay provided under subsection (a)(3) shall not be required to enable the lessor to complete the process to recover full possession of the property; and

(B) the clerk of the court shall immediately serve upon the lessor and the debtor a certified copy of the docket indicating the absence of a filed certification and the applicability of the exception to the stay under subsection (b)(22).

(5)

(A) Where a judgment for possession of residential property in which the debtor resides as a tenant under a lease or rental agreement has been obtained by the lessor, the debtor shall so indicate on the bankruptcy petition and shall provide the name and address of the lessor that obtained that pre-petition judgment on the petition and on any certification filed under this subsection.

(B) The form of certification filed with the petition, as specified in this subsection, shall provide for the debtor to certify, and the debtor shall certify-

(i) whether a judgment for possession of residential rental housing in which the debtor resides has been obtained against the debtor before the date of the filing of the petition; and

(ii) whether the debtor is claiming under paragraph (1) that under nonbankruptcy law applicable in the jurisdiction, there are circumstances under which the debtor would be permitted to cure the entire monetary default that gave rise to the judgment for possession, after that judgment of possession was entered, and has made the appropriate deposit with the court.

(C) The standard forms (electronic and otherwise) used in a bankruptcy proceeding shall be amended to reflect the requirements of this subsection.

(D) The clerk of the court shall arrange for the prompt transmittal of the rent deposited in accordance with paragraph (1)(B) to the lessor.

(m)

(1) Except as otherwise provided in this subsection, subsection (b)(23) shall apply on the date that is 15 days after the date on which the lessor files and serves a certification described in subsection (b)(23).

(2)

(A) If the debtor files with the court an objection to the truth or legal sufficiency of the certification described in subsection (b)(23) and serves such objection upon the lessor, subsection (b)(23) shall not apply, unless ordered to apply by the court under this subsection.

(B) If the debtor files and serves the objection under subparagraph (A), the court shall hold a hearing within 10 days after the filing and service of such objection to determine if the situation giving rise to the lessor's certification under paragraph (1) existed or has been remedied.

(C) If the debtor can demonstrate to the satisfaction of the court that the situation giving rise to the lessor's certification under paragraph (1) did not exist or has been remedied, the stay provided under subsection (a)(3) shall remain in effect until the termination of the stay under this section.

(D) If the debtor cannot demonstrate to the satisfaction of the court that the situation giving rise to the lessor's certification under paragraph (1) did not exist or has been remedied-

(i) relief from the stay provided under subsection (a)(3) shall not be required to enable the lessor to proceed with the eviction; and

(ii) the clerk of the court shall immediately serve upon the lessor and the debtor a certified copy of the court's order upholding the lessor's certification.

(3) If the debtor fails to file, within 15 days, an objection under paragraph (2)(A)-

(A) subsection (b)(23) shall apply immediately upon such failure and relief from the stay provided under subsection (a)(3) shall not be required to enable the lessor to complete the process to recover full possession of the property; and

(B) the clerk of the court shall immediately serve upon the lessor and the debtor a certified copy of the docket indicating such failure.

(n)

(1) Except as provided in paragraph (2), subsection (a) does not apply in a case in which the debtor-

(A) is a debtor in a small business case pending at the time the petition is filed;

(B) was a debtor in a small business case that was dismissed for any reason by an order that became final in the 2-year period ending on the date of the order for relief entered

with respect to the petition;

(C) was a debtor in a small business case in which a plan was confirmed in the 2-year period ending on the date of the order for relief entered with respect to the petition; or

(D) is an entity that has acquired substantially all of the assets or business of a small business debtor described in subparagraph (A), (B), or (C), unless such entity establishes by a preponderance of the evidence that such entity acquired substantially all of the assets or business of such small business debtor in good faith and not for the purpose of evading this paragraph.

(2) Paragraph (1) does not apply-

(A) to an involuntary case involving no collusion by the debtor with creditors; or

(B) to the filing of a petition if-

(i) the debtor proves by a preponderance of the evidence that the filing of the petition resulted from circumstances beyond the control of the debtor not foreseeable at the time the case then pending was filed; and

(ii) it is more likely than not that the court will confirm a feasible plan, but not a liquidating plan, within a reasonable period of time.

(o) The exercise of rights not subject to the stay arising under subsection (a) pursuant to paragraph (6), (7), (17), or (27) of subsection (b) shall not be stayed by any order of a court or administrative agency in any proceeding under this title.

11 U.S.C. § 362

Pub. L. 95-598, Nov. 6, 1978, 92 Stat. 2570; Pub. L. 97-222, §3, July 27, 1982, 96 Stat. 235; Pub. L. 98-353, title III, §§304, 363(b), 392, 441, July 10, 1984, 98 Stat. 352, 363, 365, 371; Pub. L. 99-509, title V, §5001(a), Oct. 21, 1986, 100 Stat. 1911; Pub. L. 99-554, title II, §§257(j), 283(d), Oct. 27, 1986, 100 Stat. 3115, 3116; Pub. L. 101-311, title I, §102, title II, §202, June 25, 1990, 104 Stat. 267, 269; Pub. L. 101-508, title III, §3007(a)(1), Nov. 5, 1990, 104 Stat. 1388-28; Pub. L. 103-394, title I, §§101, 116, title II, §§204(a), 218(b), title III, §304(b), title IV, §401, title V, §501(b)(2), (d)(7), Oct. 22, 1994, 108 Stat. 4107, 4119, 4122, 4128, 4132, 4141, 4142, 4144; Pub. L. 105-277, div. I, title VI, §603, Oct. 21, 1998, 112 Stat. 2681-886; Pub. L. 109-8, title I, §106(f), title II, §§214, 224(b), title III, §§302, 303, 305(1), 311, 320, title IV, §§401(b), 441, 444, title VII, §§709, 718, title IX, §907(d), (o)(1), (2), title XI, §1106, title XII, §1225, Apr. 20, 2005, 119 Stat. 41, 54, 64, 75, 77, 79, 84, 94, 104, 114, 117, 127, 131, 176, 181, 182, 192, 199; Pub. L. 109-304, §17(b)(1), Oct. 6, 2006, 120 Stat. 1706; Pub. L. 109-390, §5(a)(2), Dec. 12, 2006, 120 Stat. 2696; Pub. L. 111-327, §2(a)(12), Dec. 22, 2010, 124 Stat. 3558.

HISTORICAL AND REVISION NOTES

LEGISLATIVE STATEMENTS*Section 362(a)(1) of the House amendment adopts the provision contained in the Senate amendment enjoining the commencement or continuation of a judicial, administrative, or other proceeding to recover a claim against the debtor that arose before the commencement of the case. The provision is beneficial and interacts with section 362(a)(6), which also covers assessment, to prevent harassment of the debtor with respect to pre-petition claims.Section 362(a)(7) contains a provision contained in H.R. 8200 as passed by the*

House. The differing provision in the Senate amendment was rejected. It is not possible that a debt owing to the debtor may be offset against an interest in the debtor.Section 362(a)(8) is new. The provision stays the commencement or continuation of any proceeding concerning the debtor before the U.S. Tax Court.Section 362(b)(4) indicates that the stay under section 362(a)(1) does not apply to affect the commencement or continuation of an action or proceeding by a governmental unit to enforce the governmental unit's police or regulatory power. This section is intended to be given a narrow construction in order to permit governmental units to pursue actions to protect the public health and safety and not to apply to actions by a governmental unit to protect a pecuniary interest in property of the debtor or property of the estate.Section 362(b)(6) of the House amendment adopts a provision contained in the Senate amendment restricting the exception to the automatic stay with respect to setoffs to permit only the setoff of mutual debts and claims. Traditionally, the right of setoff has been limited to mutual debts and claims and the lack of the clarifying term "mutual" in H.R. 8200 as passed by the House created an unintentional ambiguity. Section 362(b)(7) of the House amendment permits the issuance of a notice of tax deficiency. The House amendment rejects section 362(b)(7) in the Senate amendment. It would have permitted a particular governmental unit to obtain a pecuniary advantage without a hearing on the merits contrary to the exceptions contained in sections 362(b)(4) and (5).Section 362(d) of the House amendment represents a compromise between comparable provisions in the House bill and Senate amendment. Under section 362(d)(1) of the House amendment, the court may terminate, annul, modify, or condition the automatic stay for cause, including lack of adequate protection of an interest in property of a secured party. It is anticipated that the Rules of Bankruptcy Procedure will provide that those hearings will receive priority on the calendar. Under section 362(d)(2) the court may alternatively terminate, annul, modify, or condition the automatic stay for cause including inadequate protection for the creditor. The court shall grant relief from the stay if there is no equity and it is not necessary to an effective reorganization of the debtor.The latter requirement is contained in section 362(d)(2). This section is intended to solve the problem of real property mortgage foreclosures of property where the bankruptcy petition is filed on the eve of foreclosure. The section is not intended to apply if the business of the debtor is managing or leasing real property, such as a hotel operation, even though the debtor has no equity if the property is necessary to an effective reorganization of the debtor. Similarly, if the debtor does have an equity in the property, there is no requirement that the property be sold under section 363 of title 11 as would have been required by the Senate amendment.Section 362(e) of the House amendment represents a modification of provisions in H.R. 8200 as passed by the House and the Senate amendment to make clear that a final hearing must be commenced within 30 days after a preliminary hearing is held to determine whether a creditor will be entitled to relief from the automatic stay. In order to insure that those hearings will in fact occur within such 30-day period, it is anticipated that the rules of bankruptcy procedure provide that such final hearings receive priority on the court calendar.Section 362(g) places the burden of proof on the issue of the debtor's equity in collateral on the party requesting relief from the automatic stay and the burden on other issues on the debtor.An amendment has been made to section 362(b) to permit the Secretary of the Department of Housing and Urban Development to commence an action to foreclose a mortgage or deed of trust. The commencement of such an action is necessary for tax purposes. The section is not intended to permit the continuation of such an action after it is commenced nor is the section to be construed to entitle the Secretary to take possession in lieu of foreclosure.Automatic stay: Sections 362(b)(8) and (9) contained in the Senate amendment are largely deleted in the House amendment. Those provisions add to the list of actions not stayed (a) jeopardy assessments, (b) other assessments, and (c) the issuance of deficiency notices. In the House amendment, jeopardy assessments against property which ceases to be property of the estate is already authorized by section 362(c)(1). Other assessments are specifically stayed under section 362(a)(6), while the issuance of a deficiency notice is specifically permitted.

Stay of the assessment and the permission to issue a statutory notice of a tax deficiency will permit the debtor to take his personal tax case to the Tax Court, if the bankruptcy judge authorizes him to do so (as explained more fully in the discussion of section 505).

SENATE REPORT NO. 95-989*The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy.The action commenced by the party seeking relief from the stay is referred to as a motion to make it clear that at the expedited hearing under subsection (e), and at hearings on relief from the stay, the only issue will be the lack of adequate protection, the debtor's equity in the property, and the necessity of the property to an effective reorganization of the debtor, or the existence of other cause for relief from the stay. This hearing will not be the appropriate time at which to bring in other issues, such as counterclaims against the creditor, which, although relevant to the question of the amount of the debt, concern largely collateral or unrelated matters. This approach is consistent with that taken in cases such as In re Essex Properties, Ltd., 430 F.Supp. 1112 (N.D.Cal.1977), that an action seeking relief from the stay is not the assertion of a claim which would give rise to the right or obligation to assert counterclaims. Those counterclaims are not to be handled in the summary fashion that the preliminary hearing under this provision will be. Rather, they will be the subject of more complete proceedings by the trustee to recover property of the estate or to object to the allowance of a claim. However, this would not preclude the party seeking continuance of the stay from presenting evidence on the existence of claims which the court may consider in exercising its discretion. What is precluded is a determination of such collateral claims on the merits at the hearing.*

HOUSE REPORT NO. 95-595*Paragraph (7) [of subsec. (a)] stays setoffs of mutual debts and credits between the debtor and creditors. As with all other paragraphs of subsection (a), this paragraph does not affect the right of creditors. It simply stays its enforcement pending an orderly examination of the debtor's and creditors' rights.Subsection (c) governs automatic termination of the stay. Subsections (d) through (g) govern termination of the stay by the court on the request of a party in interest. Subsection (d) requires the court, on request of a party in interest, to grant relief from the stay, such as by terminating, annulling, modifying, or conditioning the stay, for cause. The lack of adequate protection of an interest in property of the party requesting relief from the stay is one cause for relief, but is not the only cause. As noted above, a desire to permit an action to proceed to completion in another tribunal may provide another cause. Other causes might include the lack of any connection with or interference with the pending bankruptcy case. For example, a divorce or child custody proceeding involving the debtor may bear no relation to the bankruptcy case. In that case, it should not be stayed. A probate proceeding in which the debtor is the executor or administrator of another's estate usually will not be related to the bankruptcy case, and should not be stayed. Generally, proceedings in which the debtor is a fiduciary, or involving postpetition activities of the debtor, need not be stayed because they bear no relationship to the purpose of the automatic stay, which is debtor protection from his creditors. The facts of each request will determine whether relief is appropriate under the circumstances.Subsection (e) provides a protection for secured creditors that is not available under present law. The subsection sets a time certain within which the bankruptcy court must rule on the adequacy of protection provided of the secured creditor's interest. If the court does not rule within 30 days from a request for relief from the stay, the stay is automatically terminated with respect to the property in question. In order to accommodate more complex cases, the subsection permits the court to make a preliminary ruling after a preliminary hearing. After a preliminary hearing, the court may continue the stay only if there is a reasonable likelihood that the party opposing relief from the stay will prevail at the final hearing. Because the stay is essentially an injunction, the three stages of the stay may be analogized to the three stages of an injunction. The filing of the petition which gives rise to the automatic stay is similar to a temporary restraining order. The*

preliminary hearing is similar to the hearing on a preliminary injunction, and the final hearing and order is similar to a permanent injunction. The main difference lies in which party must bring the issue before the court. While in the injunction setting, the party seeking the injunction must prosecute the action, in proceedings for relief from the automatic stay, the enjoined party must move. The difference does not, however, shift the burden of proof. Subsection (g) leaves that burden on the party opposing relief from the stay (that is, on the party seeking continuance of the injunction) on the issue of adequate protection.At the expedited hearing under subsection (e), and at all hearings on relief from the stay, the only issue will be the claim of the creditor and the lack of adequate protection or existence of other cause for relief from the stay. This hearing will not be the appropriate time at which to bring in other issues, such as counterclaims against the creditor on largely unrelated matters. Those counterclaims are not to be handled in the summary fashion that the preliminary hearing under this provision will be. Rather, they will be the subject of more complete proceedings by the trustees to recover property of the estate or to object to the allowance of a claim.

REFERENCES IN TEXT*Section 5(a)(3) of the Securities Investor Protection Act of 1970, referred to in subsecs. (a) and (b), is classified to section 78eee(a)(3) of Title 15, Commerce and Trade.The Social Security Act, referred to in subsec. (b)(2)(D) to (G), (28), is act Aug. 14, 1935, ch. 531, 49 Stat. 620. Titles IV, XI, and XVIII of the Act are classified generally to subchapters IV (§601 et seq.), XI (§1301 et seq.), and XVIII (§1395 et seq.), respectively, of chapter 7 of Title 42, The Public Health and Welfare. Sections 464, 466, and 1128B of the Act are classified to sections 664, 666, and 1320a-7b, respectively, of Title 42. For complete classification of this Act to the Code, see section 1305 of Title 42 and Tables.The National Housing Act, referred in subsec. (b)(8), is act June 27, 1934, ch. 847, 48 Stat. 1246, which is classified principally to chapter 13 (§1701 et seq.) of Title 12, Banks and Banking. For complete classification of this Act to the Code, see section 1701 of Title 12 and Tables.The Higher Education Act of 1965, referred to in subsec. (b)(16), is Pub. L. 89-329, Nov. 8, 1965, 79 Stat. 1219, which is classified generally to chapter 28 (§1001 et seq.) of Title 20, Education. Section 435(j) of the Act is classified to section 1085(j) of Title 20. For complete classification of this Act to the Code, see Short Title note set out under section 1001 of Title 20 and Tables.The Internal Revenue Code of 1986, referred to in subsec. (b)(19), is classified generally to Title 26, Internal Revenue Code.Section 408(b)(1) of the Employee Retirement Income Security Act of 1974, referred to in subsec. (b)(19)(A), is classified to section 1108(b)(1) of Title 29, Labor.*

AMENDMENTS2010*-Subsec. (a)(8). Pub. L. 111-327, §2(a)(12)(A), substituted "tax liability of a debtor that is a corporation" for "corporate debtor's tax liability".Subsec. (c)(3). Pub. L. 111-327, §2(a)(12)(B)(i), inserted "a" after "against" in introductory provisions.Subsec. (c)(4)(A)(i). Pub. L. 111-327, §2(a)(12)(B)(ii), inserted "under a chapter other than chapter 7 after dismissal" after "refiled".Subsec. (d)(4). Pub. L. 111-327, §2(a)(12)(C), substituted "hinder, or" for "hinder, and" in introductory provisions.Subsec. (l)(2). Pub. L. 111-327, §2(a)(12)(D), substituted "nonbankruptcy" for "nonbankrupcty".**2006****-Subsec. (b)(6), (7). Pub. L. 109-390, §5(a)(2)(A), added pars. (6) and (7) and struck out former pars. (6) and (7) which read as follows:"(6) under subsection (a) of this section, of the setoff by a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency of any mutual debt and claim under or in connection with commodity contracts, as defined in section 761 of this title, forward contracts, or securities contracts, as defined in section 741 of this title, that constitutes the setoff of a claim against the debtor for a margin payment, as defined in section 101, 741, or 761 of this title, or settlement payment, as defined in section 101 or 741 of this title, arising out of commodity contracts, forward contracts, or securities contracts against cash, securities, or other property held by, pledged to, under the control of, or due from such commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency to margin, guarantee, secure, or settle commodity contracts, forward contracts, or securities contracts;"(7) under subsection (a) of this section, of the setoff by a repo participant or financial participant, of any mutual debt and claim under*

*or in connection with repurchase agreements that constitutes the setoff of a claim against the debtor for a margin payment, as defined in section 741 or 761 of this title, or settlement payment, as defined in section 741 of this title, arising out of repurchase agreements against cash, securities, or other property held by, pledged to, under the control of, or due from such repo participant or financial participant to margin, guarantee, secure or settle repurchase agreements;".Subsec. (b)(12). Pub. L. 109-304, §17(b)(1)(A), substituted "chapter 537 of title 46 or section 109(h) of title 49" for "section 207 or title XI of the Merchant Marine Act, 1936".Subsec. (b)(13). Pub. L. 109-304, §17(b)(1)(B), substituted "chapter 537 of title 46" for "section 207 or title XI of the Merchant Marine Act, 1936".Subsec. (b)(17). Pub. L. 109-390, §5(a)(2)(B), added par. (17) and struck out former par. (17) which read as follows: "under subsection (a), of the setoff by a swap participant or financial participant of a mutual debt and claim under or in connection with one or more swap agreements that constitutes the setoff of a claim against the debtor for any payment or other transfer of property due from the debtor under or in connection with any swap agreement against any payment due to the debtor from the swap participant or financial participant under or in connection with any swap agreement or against cash, securities, or other property held by, pledged to, under the control of, or due from such swap participant or financial participant to margin, guarantee, secure, or settle any swap agreement;".Subsec. (b)(27). Pub. L. 109-390, §5(a)(2)(C), added par. (27) and struck out former par. (27) which read as follows: "under subsection (a), of the setoff by a master netting agreement participant of a mutual debt and claim under or in connection with one or more master netting agreements or any contract or agreement subject to such agreements that constitutes the setoff of a claim against the debtor for any payment or other transfer of property due from the debtor under or in connection with such agreements or any contract or agreement subject to such agreements against any payment due to the debtor from such master netting agreement participant under or in connection with such agreements or any contract or agreement subject to such agreements or against cash, securities, or other property held by, pledged to, under the control of, or due from such master netting agreement participant to margin, guarantee, secure, or settle such agreements or any contract or agreement subject to such agreements, to the extent that such participant is eligible to exercise such offset rights under paragraph (6), (7), or (17) for each individual contract covered by the master netting agreement in issue; and".**2005**-Subsec. (a)(8). Pub. L. 109-8, §709, substituted "a corporate debtor's tax liability for a taxable period the bankruptcy court may determine or concerning the tax liability of a debtor who is an individual for a taxable period ending before the date of the order for relief under this title" for "the debtor".Subsec. (b)(2). Pub. L. 109-8, §214, added par. (2) and struck out former par. (2) which read as follows: "under subsection (a) of this section-"(A) of the commencement or continuation of an action or proceeding for-"(i) the establishment of paternity; or"(ii) the establishment or modification of an order for alimony, maintenance, or support; or"(B) of the collection of alimony, maintenance, or support from property that is not property of the estate;".Subsec. (b)(6). Pub. L. 109-8, §907(d)(1)(A), (o) (1), substituted "financial institution, financial participant," for "financial institutions," in two places and inserted ", pledged to, under the control of," after "held by".Subsec. (b)(7). Pub. L. 109-8, §907(d)(1)(B), (o) (2), inserted "or financial participant" after "repo participant" in two places and ", pledged to, under the control of," after "held by".Subsec. (b)(17). Pub. L. 109-8, §907(d)(1)(C), added par. (17) and struck out former par. (17) which read as follows: "under subsection (a) of this section, of the setoff by a swap participant, of any mutual debt and claim under or in connection with any swap agreement that constitutes the setoff of a claim against the debtor for any payment due from the debtor under or in connection with any swap agreement against any payment due to the debtor from the swap participant under or in connection with any swap agreement or against cash, securities, or other property of the debtor held by or due from such swap participant to guarantee, secure or settle any swap agreement;".Subsec. (b)(18). Pub. L. 109-8, §1225, amended par. (18) generally. Prior to amendment, par. (18) read as follows: "under subsection (a) of the creation or perfection of a statutory lien for an ad valorem property tax imposed by the District of Columbia, or a political subdivision of a State, if such tax comes due after the filing of the petition;".Subsec. (b)(19). Pub. L. 109-8, §224(b), added par. (19).Subsec. (b)*

*(20), (21). Pub. L. 109-8, §303(b), added pars. (20) and (21).Subsec. (b)(22) to (24). Pub. L. 109-8, §311(a), added pars. (22) to (24).Subsec. (b)(25). Pub. L. 109-8, §401(b), added par. (25).Subsec. (b)(26). Pub. L. 109-8, §718, added par. (26).Subsec. (b)(27). Pub. L. 109-8, §907(d)(1)(D), added par. (27).Subsec. (b)(28). Pub. L. 109-8, §1106, added par. (28).Subsec. (c). Pub. L. 109-8, §305(1)(A), substituted "(e), (f), and (h)" for "(e), and (f)" in introductory provisions.Subsec. (c)(3), (4). Pub. L. 109-8, §302, added pars. (3) and (4).Subsec. (d). Pub. L. 109-8, §303(a), added par. (4) and concluding provisions.Subsec. (d)(3). Pub. L. 109-8, §444(1), inserted "or 30 days after the court determines that the debtor is subject to this paragraph, whichever is later" after "90-day period)" in introductory provisions.Subsec. (d)(3)(B). Pub. L. 109-8, §444(2), added subpar. (B) and struck out former subpar. (B) which read as follows: "the debtor has commenced monthly payments to each creditor whose claim is secured by such real estate (other than a claim secured by a judgment lien or by an unmatured statutory lien), which payments are in an amount equal to interest at a current fair market rate on the value of the creditor's interest in the real estate; or".Subsec. (e). Pub. L. 109-8, §320, designated existing provisions as par. (1) and added par. (2).Subsec. (h). Pub. L. 109-8, §305(1)(C), added subsec. (h). Former subsec. (h) redesignated (k).Subsecs. (i), (j). Pub. L. 109-8, §106(f), added subsecs. (i) and (j).Subsec. (k). Pub. L. 109-8, §441(1), designated existing provisions as par. (1), substituted "Except as provided in paragraph (2), an" for "An", and added par. (2). Pub. L. 109-8, §305(1)(B), redesignated subsec. (h) as (k).Subsecs. (l), (m). Pub. L. 109-8, §311(b), added subsecs. (l) and (m).Subsec. (n). Pub. L. 109-8, §441(2), added subsec. (n).Subsec. (o). Pub. L. 109-8, §907(d)(2), added subsec. (o).**1998**-Subsec. (b)(4), (5). Pub. L. 105-277 added par. (4) and struck out former pars. (4) and (5) which read as follows:"(4) under subsection (a)(1) of this section, of the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power;"(5) under subsection (a)(2) of this section, of the enforcement of a judgment, other than a money judgment, obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power;".**1994**-Subsecs. (a), (b). Pub. L. 103-394, §501(d)(7)(A), (B) (i), struck out "(15 U.S.C. 78ee e(a)(3))" after "Act of 1970" in introductory provisions.Subsec. (b)(2). Pub. L. 103-394, §304(b), amended par. (2) generally. Prior to amendment, par. (2) read as follows: "under subsection (a) of this section, of the collection of alimony, maintenance, or support from property that is not property of the estate;".Subsec. (b)(3). Pub. L. 103-394, §204(a), inserted ", or to maintain or continue the perfection of," after "to perfect".Subsec. (b)(6). Pub. L. 103-394, §501(b)(2)(A), substituted "section 761" for "section 761(4)", "section 741" for "section 741(7)", "section 101, 741, or 761" for "section 101(34), 741(5), or 761(15)", and "section 101 or 741" for "section 101(35) or 741(8)".Subsec. (b)(7). Pub. L. 103-394, §501(b)(2)(B), substituted "section 741 or 761" for "section 741(5) or 761(15)" and "section 741" for "section 741(8)".Subsec. (b)(9). Pub. L. 103-394, §116, amended par. (9) generally. Prior to amendment, par. (9) read as follows: "under subsection (a) of this section, of the issuance to the debtor by a governmental unit of a notice of tax deficiency;".Subsec. (b)(10). Pub. L. 103-394, §501(d)(7)(B)(ii), struck out "or" at end.Subsec. (b)(12). Pub. L. 103-394, §501(d)(7)(B)(iii), substituted "section 31325 of title 46" for "the Ship Mortgage Act, 1920 (46 App. U.S.C. 911 et seq.)" and struck out "(46 App. U.S.C. 1117 and 1271 et seq., respectively)" after "Act, 1936".Subsec. (b)(13). Pub. L. 103-394, §501(d)(7)(B)(iv), substituted "section 31325 of title 46" for "the Ship Mortgage Act, 1920 (46 App. U.S.C. 911 et seq.)" and struck out "(46 App. U.S.C. 1117 and 1271 et seq., respectively)" after "Act, 1936" and "or" at end.Subsec. (b)(14). Pub. L. 103-394, §501(d)(7)(B)(vii), amended par. (14) relating to the setoff by a swap participant of any mutual debt and claim under or in connection with a swap agreement by substituting "; or" for period at end, redesignating par. (14) as (17), and inserting it after par. (16).Subsec. (b)(15). Pub. L. 103-394, §501(d)(7)(B)(v), struck out "or" at end.Subsec. (b)(16). Pub. L. 103-394, §501(d)(7)(B)(vi), struck out "(20 U.S.C. 1001 et seq.)" after "Act of 1965" and substituted semicolon for period at end.Subsec. (b)(17). Pub. L. 103-394, §501(d)(7)(B)(vii)(II), (III), redesignated par. (14) relating to the setoff by a swap participant of any mutual debt and claim under or in connection with a swap agreement as (17) and inserted it after par. (16).Subsec. (b)(18). Pub. L. 103-394, §401,*

*added par. (18).Subsec. (d)(3). Pub. L. 103-394, §218(b), added par. (3).Subsec. (e). Pub. L. 103-394, §101, in last sentence substituted "concluded" for "commenced" and inserted before period at end ", unless the 30-day period is extended with the consent of the parties in interest or for a specific time which the court finds is required by compelling circumstances".**1990**-Subsec. (b)(6). Pub. L. 101-311, §202, inserted reference to sections 101(34) and 101(35) of this title.Subsec. (b)(12). Pub. L. 101-508, §3007(a)(1)(A), which directed the striking of "or" after "State law;", could not be executed because of a prior amendment by Pub. L. 101-311. See below. Pub. L. 101-311, §102(1), struck out "or" after "State law;".Subsec. (b)(13). Pub. L. 101-508, §3007(a)(1)(B), which directed the substitution of a semicolon for period at end, could not be executed because of a prior amendment by Pub. L. 101-311. See below. Pub. L. 101-311, §102(2), substituted "; or" for period at end.Subsec. (b)(14) to (16). Pub. L. 101-508, §3007(a)(1)(C), added pars. (14) to (16). Notwithstanding directory language adding pars. (14) to (16) immediately following par. (13), pars. (14) to (16) were added after par. (14), as added by Pub. L. 101-311 to reflect the probable intent of Congress. Pub. L. 101-311, §102(3), added par. (14) relating to the setoff by a swap participant of any mutual debt and claim under or in connection with a swap agreement. Notwithstanding directory language adding par. (14) at end of subsec. (b), par. (14) was added after par. (13) to reflect the probable intent of Congress.**1986**-Subsec. (b). Pub. L. 99-509 inserted sentence at end.Subsec. (b)(6). Pub. L. 99-554, §283(d)(1), substituted ", financial institutions" for "financial institution," in two places.Subsec. (b)(9). Pub. L. 99-554, §283(d)(2), (3), struck out "or" at end of first par. (9) and redesignated as par. (10) the second par. (9) relating to leases of nonresidential property, which was added by section 363(b) of Pub. L. 98-353.Subsec. (b)(10). Pub. L. 99-554, §283(d)(3), (4), redesignated as par. (10) the second par. (9) relating to leases of nonresidential property, added by section 363(b) of Pub. L. 99-353 and substituted "property; or" for "property.". Former par. (10) redesignated (11).Subsec. (b)(11). Pub. L. 99-554, §283(d)(3), redesignated former par. (10) as (11).Subsec. (b)(12), (13). Pub. L. 99-509 added pars. (12) and (13).Subsec. (c)(2)(C). Pub. L. 99-554, §257(j), inserted reference to chapter 12 of this title.**1984**-Subsec. (a)(1). Pub. L. 98-353, §441(a)(1), inserted "action or" after "other".Subsec. (a)(3). Pub. L. 98-353, §441(a)(2), inserted "or to exercise control over property of the estate".Subsec. (b)(3). Pub. L. 98-353, §441(b)(1), inserted "or to the extent that such act is accomplished within the period provided under section 547(e)(2)(A) of this title".Subsec. (b)(6). Pub. L. 98-353, §441(b)(2), inserted "or due from" after "held by" and "financial institution," after "stockbroker" in two places, and substituted "secure, or settle commodity contracts" for "or secure commodity contracts".Subsec. (b)(7) to (9). Pub. L. 98-353, §441(b)(3), (4), in par. (8) as redesignated by Pub. L. 98-353, §392, substituted "the" for "said" and struck out "or" the last place it appeared which probably meant "or" after "units;" that was struck out by Pub. L. 98-353, §363(b)(1); and, in par. (9), relating to notices of deficiencies, as redesignated by Pub. L. 98-353, §392, substituted a semicolon for the period.Pub. L. 98-353, §392, added par. (7) and redesignated former pars. (7) and (8) as (8) and (9), respectively.Pub. L. 98-353, §363(b), struck out "or" at end of par. (7), substituted "; or" for the period at end of par. (8), and added par. (9) relating to leases of nonresidential property.Subsec. (b)(10). Pub. L. 98-353, §441(b)(5), added par. (10).Subsec. (c)(2)(B). Pub. L. 98-353, §441(c), substituted "or" for "and".Subsec. (d)(2). Pub. L. 98-353, §441(d), inserted "under subsection (a) of this section" after "property".Subsec. (e). Pub. L. 98-353, §441(e), inserted "the conclusion of" after "pending" and substituted "The court shall order such stay continued in effect pending the conclusion of the final hearing under subsection (d) of this section if there is a reasonable likelihood that the party opposing relief from such stay will prevail at the conclusion of such final hearing. If the hearing under this subsection is a preliminary hearing, then such final hearing shall be commenced not later than thirty days after the conclusion of such preliminary hearing." for "If the hearing under this subsection is a preliminary hearing-"(1) the court shall order such stay so continued if there is a reasonable likelihood that the party opposing relief from such stay will prevail at the final hearing under subsection (d) of this section; and"(2) such final hearing shall be commenced within thirty days after such preliminary hearing."Subsec. (f). Pub. L. 98-353, §441(f), substituted "Upon request of a party in interest, the court, with or"*

*for "The court,".Subsec. (h). Pub. L. 98-353, §304, added subsec. (h).**1982**-Subsec. (a). Pub. L. 97-222, §3(a), inserted ", or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970 (15 U.S.C. 78ee e(a)(3))," after "this title" in provisions preceding par. (1).Subsec. (b). Pub. L. 97-222, §3(b), inserted ", or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970 (15 U.S.C. 78ee e(a)(3))," after "this title" in provisions preceding par. (1).Subsec. (b)(6). Pub. L. 97-222, §3(c), substituted provisions that the filing of a bankruptcy petition would not operate as a stay, under subsec. (a) of this section, of the setoff by a commodity broker, forward contract merchant, stockbroker, or securities clearing agency of any mutual debt and claim under or in connection with commodity, forward, or securities contracts that constitutes the setoff of a claim against the debtor for a margin or settlement payment arising out of commodity, forward, or securities contracts against cash, securities, or other property held by any of the above agents to margin, guarantee, or secure commodity, forward, or securities contracts, for provisions that such filing would not operate as a stay under subsection (a)(7) of this section, of the setoff of any mutual debt and claim that are commodity futures contracts, forward commodity contracts, leverage transactions, options, warrants, rights to purchase or sell commodity futures contracts or securities, or options to purchase or sell commodities or securities.*

***EFFECTIVE DATE OF 2006 AMENDMENT**Amendment by Pub. L. 109-390 not applicable to any cases commenced under this title or to appointments made under any Federal or State law, before Dec. 12, 2006, see section 7 of Pub. L. 109-390 set out as a note under section 101 of this title.*

***EFFECTIVE DATE OF 2005 AMENDMENT**Amendment by Pub. L. 109-8 effective 180 days after Apr. 20, 2005, and not applicable with respect to cases commenced under this title before such effective date, except as otherwise provided, see section 1501 of Pub. L. 109-8 set out as a note under section 101 of this title.*

***EFFECTIVE DATE OF 1994 AMENDMENT**Amendment by Pub. L. 103-394 effective Oct. 22, 1994, and not applicable with respect to cases commenced under this title before Oct. 22, 1994, see section 702 of Pub. L. 103-394 set out as a note under section 101 of this title.*

***EFFECTIVE DATE OF 1990 AMENDMENT** Pub. L. 101-508, title III, §3007(a)(3), Nov. 5, 1990, 104 Stat. 1388-28, provided that: "The amendments made by this subsection [amending this section and section 541 of this title] shall be effective upon date of enactment of this Act [Nov. 5, 1990]." Pub. L. 101-508, title III, §30083008,, 104 Stat. 1388-29, provided that the amendments made by subtitle A (§§3001-3008) of title III of Pub. L. 101-508 amending this section, sections 541 and 1328 of this title, and sections 1078, 1078-1, 1078-7, 1085, 1088, and 1091 of Title 20, Education, and provisions set out as a note under section 1078-1 of Title 20, were to cease to be effective Oct. 1, 1996, prior to repeal by Pub. L. 102-325, title XV, §15581558,, 106 Stat. 841.*

***EFFECTIVE DATE OF 1986 AMENDMENT**Amendment by section 257 of Pub. L. 99-554 effective 30 days after Oct. 27, 1986, but not applicable to cases commenced under this title before that date, see section 302(a), (c)(1) of Pub. L. 99-554 set out as a note under section 581 of Title 28, Judiciary and Judicial Procedure.Amendment by section 283 of Pub. L. 99-554 effective 30 days after Oct. 27, 1986, see section 302(a) of Pub. L. 99-554.Pub. L. 99-509, title V, §5001(b), Oct. 21, 1986, 100 Stat. 1912, provided that: "The amendments made by subsection (a) of this section [amending this section] shall apply only to petitions filed under section 362 of title 11, United States Code, which are made after August 1, 1986."*

***EFFECTIVE DATE OF 1984 AMENDMENT**Amendment by Pub. L. 98-353 effective with respect to cases filed 90 days after July 10, 1984, see section 552(a) of Pub. L. 98-353 set out as a note under section 101 of this title.*

REPORT TO CONGRESSIONAL COMMITTEES*Pub. L. 99-509, title V, §5001(a), Oct. 21, 1986, 100 Stat. 1911, directed Secretary of Transportation and Secretary of Commerce, before July 1, 1989, to submit reports to Congress on the effects of amendments to 11 U.S.C. 362 by this subsection.*

11 U.S.C. § 522

Section 522 - Exemptions

(a) In this section-

(1) "dependent" includes spouse, whether or not actually dependent; and

(2) "value" means fair market value as of the date of the filing of the petition or, with respect to property that becomes property of the estate after such date, as of the date such property becomes property of the estate.

(b)

(1) Notwithstanding section 541 of this title, an individual debtor may exempt from property of the estate the property listed in either paragraph (2) or, in the alternative, paragraph (3) of this subsection. In joint cases filed under section 302 of this title and individual cases filed under section 301 or 303 of this title by or against debtors who are husband and wife, and whose estates are ordered to be jointly administered under Rule 1015(b) of the Federal Rules of Bankruptcy Procedure, one debtor may not elect to exempt property listed in paragraph (2) and the other debtor elect to exempt property listed in paragraph (3) of this subsection. If the parties cannot agree on the alternative to be elected, they shall be deemed to elect paragraph (2), where such election is permitted under the law of the jurisdiction where the case is filed.

(2) Property listed in this paragraph is property that is specified under subsection (d), unless the State law that is applicable to the debtor under paragraph (3)(A) specifically does not so authorize.

(3) Property listed in this paragraph is-

(A) subject to subsections (o) and (p), any property that is exempt under Federal law, other than subsection (d) of this section, or State or local law that is applicable on the date of the filing of the petition to the place in which the debtor's domicile has been located for the 730 days immediately preceding the date of the filing of the petition or if the debtor's domicile has not been located in a single State for such 730-day period, the place in which the debtor's domicile was located for 180 days immediately preceding the 730-day period or for a longer portion of such 180-day period than in any other place;

(B) any interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest as a tenant by the entirety or joint tenant is exempt from process under applicable nonbankruptcy law; and

(C) retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986.

If the effect of the domiciliary requirement under subparagraph (A) is to render the debtor ineligible for any exemption, the debtor may elect to exempt property that is specified under subsection (d).

(4) For purposes of paragraph (3)(C) and subsection (d)(12), the following shall apply:

(A) If the retirement funds are in a retirement fund that has received a favorable determination under section 7805 of the Internal Revenue Code of 1986, and that determination is in effect as of the date of the filing of the petition in a case under this title, those funds shall be presumed to be exempt from the estate.

(B) If the retirement funds are in a retirement fund that has not received a favorable determination under such section 7805, those funds are exempt from the estate if the debtor demonstrates that-

(i) no prior determination to the contrary has been made by a court or the Internal Revenue Service; and

(ii)

(I) the retirement fund is in substantial compliance with the applicable requirements of the Internal Revenue Code of 1986; or

(II) the retirement fund fails to be in substantial compliance with the applicable requirements of the Internal Revenue Code of 1986 and the debtor is not materially responsible for that failure.

(C) A direct transfer of retirement funds from 1 fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986, under section 401(a)(31) of the Internal Revenue Code of 1986, or otherwise, shall not cease to qualify for exemption under paragraph (3)(C) or subsection (d)(12) by reason of such direct transfer.

(D)

(i) Any distribution that qualifies as an eligible rollover distribution within the meaning of section 402(c) of the Internal Revenue Code of 1986 or that is described in clause (ii) shall not cease to qualify for exemption under paragraph (3)(C) or subsection (d)(12) by reason of such distribution.

(ii) A distribution described in this clause is an amount that-

(I) has been distributed from a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986; and

(II) to the extent allowed by law, is deposited in such a fund or account not later than 60 days after the distribution of such amount.

(c) Unless the case is dismissed, property exempted under this section is not liable during or after the case for any debt of the debtor that arose, or that is determined under section 502 of this title as if such debt had arisen, before the commencement of the case, except-

(1) a debt of a kind specified in paragraph (1) or (5) of section 523(a) (in which case, notwithstanding any provision of applicable nonbankruptcy law to the contrary, such property shall be liable for a debt of a kind specified in such paragraph);

(2) a debt secured by a lien that is-

(A)

(i) not avoided under subsection (f) or (g) of this section or under section 544, 545, 547, 548, 549, or 724(a) of this title; and

(ii) not void under section 506(d) of this title; or

(B) a tax lien, notice of which is properly filed;

(3) a debt of a kind specified in section 523(a)(4) or 523(a)(6) of this title owed by an institution-affiliated party of an insured depository institution to a Federal depository institutions regulatory agency acting in its capacity as conservator, receiver, or liquidating agent for such institution; or

(4) a debt in connection with fraud in the obtaining or providing of any scholarship, grant, loan, tuition, discount, award, or other financial assistance for purposes of financing an education at an institution of higher education (as that term is defined in section 101 of the Higher Education Act of 1965 (20 U.S.C. 1001)).

(d) The following property may be exempted under subsection (b)(2) of this section:

(1) The debtor's aggregate interest, not to exceed $15,000 [1] in value, in real property or personal property that the debtor or a dependent of the debtor uses as a residence, in a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence, or in a burial plot for the debtor or a dependent of the debtor.

(2) The debtor's interest, not to exceed $2,400 [1] in value, in one motor vehicle.

(3) The debtor's interest, not to exceed $400 [1] in value in any particular item or $8,000 [1] in aggregate value, in household furnishings, household goods, wearing apparel, appliances, books, animals, crops, or musical instruments, that are held primarily for the personal, family, or household use of the debtor or a dependent of the debtor.

(4) The debtor's aggregate interest, not to exceed $1,000 [1] in value, in jewelry held primarily for the personal, family, or household use of the debtor or a dependent of the debtor.

(5) The debtor's aggregate interest in any property, not to exceed in value $800 [1] plus up to $7,500 [1] of any unused amount of the exemption provided under paragraph (1) of this subsection.

(6) The debtor's aggregate interest, not to exceed $1,500 [1] in value, in any implements, professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor.

(7) Any unmatured life insurance contract owned by the debtor, other than a credit life insurance contract.

(8) The debtor's aggregate interest, not to exceed in value $8,000 [1] less any amount of property of the estate transferred in the manner specified in section 542(d) of this title, in any accrued dividend or interest under, or loan value of, any unmatured life insurance contract owned by the debtor under which the insured is the debtor or an individual of whom the debtor is a dependent.

(9) Professionally prescribed health aids for the debtor or a dependent of the debtor.

(10) The debtor's right to receive-

(A) a social security benefit, unemployment compensation, or a local public assistance benefit;

(B) a veterans' benefit;

(C) a disability, illness, or unemployment benefit;

(D) alimony, support, or separate maintenance, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;

(E) a payment under a stock bonus, pension, profitsharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor, unless-

(i) such plan or contract was established by or under the auspices of an insider that employed the debtor at the time the debtor's rights under such plan or contract arose;

(ii) such payment is on account of age or length of service; and

(iii) such plan or contract does not qualify under section 401(a), 403(a), 403(b), or 408 of the Internal Revenue Code of 1986.

(11) The debtor's right to receive, or property that is traceable to-

(A) an award under a crime victim's reparation law;

(B) a payment on account of the wrongful death of an individual of whom the debtor was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;

(C) a payment under a life insurance contract that insured the life of an individual of whom the debtor was a dependent on the date of such individual's death, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;

(D) a payment, not to exceed $15,000,[1] on account of personal bodily injury, not including pain and suffering or compensation for actual pecuniary loss, of the debtor or an individual of whom the debtor is a dependent; or

(E) a payment in compensation of loss of future earnings of the debtor or an individual of whom the debtor is or was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor.

(12) Retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986.

(e) A waiver of an exemption executed in favor of a creditor that holds an unsecured claim against the debtor is unenforceable in a case under this title with respect to such claim against property that the debtor may exempt under subsection (b) of this section. A waiver by the debtor of a power under subsection (f) or (h) of this section to avoid a transfer, under subsection (g) or (i) of this section to exempt property, or under subsection (i) of this section to recover property or to preserve a transfer, is unenforceable in a case under this title.

(f)

(1) Notwithstanding any waiver of exemptions but subject to paragraph (3), the debtor may avoid the fixing of a lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled under subsection (b) of this section, if such lien is-

(A) a judicial lien, other than a judicial lien that secures a debt of a kind that is specified in section 523(a)(5); or

(B) a nonpossessory, nonpurchase-money security interest in any-

(i) household furnishings, household goods, wearing apparel, appliances, books, animals, crops, musical instruments, or jewelry that are held primarily for the personal, family, or household use of the debtor or a dependent of the debtor;

(ii) implements, professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor; or

(iii) professionally prescribed health aids for the debtor or a dependent of the debtor.

(2)

(A) For the purposes of this subsection, a lien shall be considered to impair an exemption to the extent that the sum of-

(i) the lien;

(ii) all other liens on the property; and

(iii) the amount of the exemption that the debtor could claim if there were no liens on the property;

exceeds the value that the debtor's interest in the property would have in the absence of any liens.

(B) In the case of a property subject to more than 1 lien, a lien that has been avoided shall not be considered in making the calculation under subparagraph (A) with respect to other liens.

(C) This paragraph shall not apply with respect to a judgment arising out of a mortgage foreclosure.

(3) In a case in which State law that is applicable to the debtor-

(A) permits a person to voluntarily waive a right to claim exemptions under subsection (d) or prohibits a debtor from claiming exemptions under subsection (d); and

(B) either permits the debtor to claim exemptions under State law without limitation in amount, except to the extent that the debtor has permitted the fixing of a consensual lien on any property or prohibits avoidance of a consensual lien on property otherwise eligible to be claimed as exempt property;
the debtor may not avoid the fixing of a lien on an interest of the debtor or a dependent of the debtor in property if the lien is a nonpossessory, nonpurchase-money security interest in implements, professional books, or tools of the trade of the debtor or a dependent of the debtor or farm animals or crops of the debtor or a dependent of the debtor to the extent the value of such implements, professional books, tools of the trade, animals, and crops exceeds $5,000.[1]

(4)

(A) Subject to subparagraph (B), for purposes of paragraph (1)(B), the term "household goods" means-

(i) clothing;

(ii) furniture;

(iii) appliances;

(iv) 1 radio;

(v) 1 television;

(vi) 1 VCR;

(vii) linens;

(viii) china;

(ix) crockery;

(x) kitchenware;

(xi) educational materials and educational equipment primarily for the use of minor dependent children of the debtor;

(xii) medical equipment and supplies;

(xiii) furniture exclusively for the use of minor children, or elderly or disabled dependents of the debtor;

(xiv) personal effects (including the toys and hobby equipment of minor dependent children and wedding rings) of the debtor and the dependents of the debtor; and

(xv) 1 personal computer and related equipment.

(B) The term "household goods" does not include-

(i) works of art (unless by or of the debtor, or any relative of the debtor);

(ii) electronic entertainment equipment with a fair market value of more than $500 [1] in the aggregate (except 1 television, 1 radio, and 1 VCR);

(iii) items acquired as antiques with a fair market value of more than $500 [1] in the aggregate;

(iv) jewelry with a fair market value of more than $500 [1] in the aggregate (except wedding rings); and

(v) a computer (except as otherwise provided for in this section), motor vehicle (including a tractor or lawn tractor), boat, or a motorized recreational device, conveyance, vehicle, watercraft, or aircraft.

(g) Notwithstanding sections 550 and 551 of this title, the debtor may exempt under subsection (b) of this section property that the trustee recovers under section 510(c)(2), 542, 543, 550, 551, or 553 of this title, to the extent that the debtor could have exempted such property under subsection (b) of this section if such property had not been transferred, if-

(1)

(A) such transfer was not a voluntary transfer of such property by the debtor; and

(B) the debtor did not conceal such property; or

(2) the debtor could have avoided such transfer under subsection (f)(1)(B) of this section.

(h) The debtor may avoid a transfer of property of the debtor or recover a setoff to the extent that the debtor could have exempted such property under subsection (g)(1) of this section if the trustee had avoided such transfer, if-

(1) such transfer is avoidable by the trustee under section 544, 545, 547, 548, 549, or 724(a) of this title or recoverable by the trustee under section 553 of this title; and

(2) the trustee does not attempt to avoid such transfer.

(i)

(1) If the debtor avoids a transfer or recovers a setoff under subsection (f) or (h) of this section, the debtor may recover in the manner prescribed by, and subject to the limitations of, section 550 of this title, the same as if the trustee had avoided such transfer, and may exempt any property so recovered under subsection (b) of this section.

(2) Notwithstanding section 551 of this title, a transfer avoided under section 544, 545, 547, 548, 549, or 724(a) of this title, under subsection (f) or (h) of this section, or property recovered under section 553 of this title, may be preserved for the benefit of the debtor to

the extent that the debtor may exempt such property under subsection (g) of this section or paragraph (1) of this subsection.

(j) Notwithstanding subsections (g) and (i) of this section, the debtor may exempt a particular kind of property under subsections (g) and (i) of this section only to the extent that the debtor has exempted less property in value of such kind than that to which the debtor is entitled under subsection (b) of this section.

(k) Property that the debtor exempts under this section is not liable for payment of any administrative expense except-

(1) the aliquot share of the costs and expenses of avoiding a transfer of property that the debtor exempts under subsection (g) of this section, or of recovery of such property, that is attributable to the value of the portion of such property exempted in relation to the value of the property recovered; and

(2) any costs and expenses of avoiding a transfer under subsection (f) or (h) of this section, or of recovery of property under subsection (i)(1) of this section, that the debtor has not paid.

(l) The debtor shall file a list of property that the debtor claims as exempt under subsection (b) of this section. If the debtor does not file such a list, a dependent of the debtor may file such a list, or may claim property as exempt from property of the estate on behalf of the debtor. Unless a party in interest objects, the property claimed as exempt on such list is exempt.

(m) Subject to the limitation in subsection (b), this section shall apply separately with respect to each debtor in a joint case.

(n) For assets in individual retirement accounts described in section 408 or 408A of the Internal Revenue Code of 1986, other than a simplified employee pension under section 408(k) of such Code or a simple retirement account under section 408(p) of such Code, the aggregate value of such assets exempted under this section, without regard to amounts attributable to rollover contributions under section 402(c), 402(e)(6), 403(a)(4), 403(a)(5), and 403(b)(8) of the Internal Revenue Code of 1986, and earnings thereon, shall not exceed $1,000,000 [1] in a case filed by a debtor who is an individual, except that such amount may be increased if the interests of justice so require.

(o) For purposes of subsection (b)(3)(A), and notwithstanding subsection (a), the value of an interest in-

(1) real or personal property that the debtor or a dependent of the debtor uses as a residence;

(2) a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence;

(3) a burial plot for the debtor or a dependent of the debtor; or

(4) real or personal property that the debtor or a dependent of the debtor claims as a homestead;

shall be reduced to the extent that such value is attributable to any portion of any property that the debtor disposed of in the 10-year period ending on the date of the filing of the petition with the intent to hinder, delay, or defraud a creditor and that the debtor could not exempt, or that portion that the debtor could not exempt, under subsection (b), if on such date the debtor had held the property so disposed of.

(p)

(1) Except as provided in paragraph (2) of this subsection and sections 544 and 548, as a result of electing under subsection (b)(3)(A) to exempt property under State or local law, a debtor may not exempt any amount of interest that was acquired by the debtor during the 1215-day period preceding the date of the filing of the petition that exceeds in the aggregate $125,000 [1] in value in-

(A) real or personal property that the debtor or a dependent of the debtor uses as a residence;

(B) a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence;

(C) a burial plot for the debtor or a dependent of the debtor; or

(D) real or personal property that the debtor or dependent of the debtor claims as a homestead.

(2)

(A) The limitation under paragraph (1) shall not apply to an exemption claimed under subsection (b)(3)(A) by a family farmer for the principal residence of such farmer.

(B) For purposes of paragraph (1), any amount of such interest does not include any interest transferred from a debtor's previous principal residence (which was acquired prior to the beginning of such 1215-day period) into the debtor's current principal residence, if the debtor's previous and current residences are located in the same State.

(q)

(1) As a result of electing under subsection (b)(3)(A) to exempt property under State or local law, a debtor may not exempt any amount of an interest in property described in subparagraphs (A), (B), (C), and (D) of subsection (p)(1) which exceeds in the aggregate $125,000 [1] if-

(A) the court determines, after notice and a hearing, that the debtor has been convicted of a felony (as defined in section 3156 of title 18), which under the circumstances, demonstrates that the filing of the case was an abuse of the provisions of this title; or

(B) the debtor owes a debt arising from-

(i) any violation of the Federal securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934), any State securities laws, or any regulation or order issued under Federal securities laws or State securities laws;

(ii) fraud, deceit, or manipulation in a fiduciary capacity or in connection with the purchase or sale of any security registered under section 12 or 15(d) of the Securities

Exchange Act of 1934 or under section 6 of the Securities Act of 1933;

(iii) any civil remedy under section 1964 of title 18; or

(iv) any criminal act, intentional tort, or willful or reckless misconduct that caused serious physical injury or death to another individual in the preceding 5 years.

(2) Paragraph (1) shall not apply to the extent the amount of an interest in property described in subparagraphs (A), (B), (C), and (D) of subsection (p)(1) is reasonably necessary for the support of the debtor and any dependent of the debtor.

[1] See Adjustment of Dollar Amounts notes below.

[1] Replaced by 22 U.S.C. 4060(c).

[2] Replaced by 46 U.S.C. 11108, 11109.

[3] Replaced by 5 U.S.C. 8346.

[4] Replaced by 45 U.S.C. 231m.

[5] Railroad unemployment benefits are covered by 45 U.S.C. 352(e).

[6] Veterans benefits generally are covered by 38 U.S.C. 3101 [now 5301].

[7] Replaced by 22 U.S.C. 4060(c).

[8] Replaced by 46 U.S.C. 11108, 11109.

[9] Replaced by 5 U.S.C. 8346.

[10] Replaced by 45 U.S.C. 231m.

[11] Railroad unemployment benefits are covered by 45 U.S.C. 352(e).

[12] Veterans benefits generally are covered by 38 U.S.C. 3101 [now 5301].

11 U.S.C. § 522

Pub. L. 95-598, Nov. 6, 1978, 92 Stat. 2586; Pub. L. 98-353, title III, §§306, 453, July 10, 1984, 98 Stat. 353, 375; Pub. L. 99-554, title II, §283(i), Oct. 27, 1986, 100 Stat. 3117; Pub. L. 101-647, title XXV, §2522(b), Nov. 29, 1990, 104 Stat. 4866; Pub. L. 103-394, title I, §108(d), title III, §§303, 304(d), 310, title V, §501(d)(12), Oct. 22, 1994, 108 Stat. 4112, 4132, 4133, 4137, 4145; Pub. L. 106-420, §4, Nov. 1, 2000, 114 Stat. 1868; Pub. L. 109-8, title II, §§216, 224 (1), title III, §§307, 308, 313(a), 322(a), Apr. 20, 2005, 119 Stat. 55, 62, 65, 81, 87, 96; Pub. L. 111-327, §2(a)(17), Dec. 22, 2010, 124 Stat. 3559.

HISTORICAL AND REVISION NOTES

LEGISLATIVE STATEMENTS*Section 522 of the House amendment represents a compromise on the issue of exemptions between the position taken in the House bill, and that taken in the Senate amendment. Dollar amounts specified in section 522(d) of the House bill have been reduced from amounts as contained in H.R. 8200 as passed by the House. The States may, by passing a law, determine whether the Federal exemptions will apply as an alternative to State exemptions in bankruptcy cases.Section 522(c)(1) tracks the House bill and provides that dischargeable tax claims may not be collected out of exempt property.Section 522(f)(2) is derived from the Senate*

amendment restricting the debtor to avoidance of nonpossessory, nonpurchase money security interests.Exemptions: Section 522(c)(1) of the House amendment adopts a provision contained in the House bill that dischargeable taxes cannot be collected from exempt assets. This changes present law, which allows collection of dischargeable taxes from exempt property, a rule followed in the Senate amendment. Nondischargeable taxes, however, will continue to the [be] collectable out of exempt property. It is anticipated that in the next session Congress will review the exemptions from levy currently contained in the Internal Revenue Code [title 26] with a view to increasing the exemptions to more realistic levels.

SENATE REPORT NO. 95-989*Subsection (a) of this section defines two terms: "dependent" includes the debtor's spouse, whether or not actually dependent; and "value" means fair market value as of the date of the filing of the petition.Subsection (b) tracks current law. It permits a debtor the exemptions to which he is entitled under other Federal law and the law of the State of his domicile. Some of the items that may be exempted under Federal laws other than title 11 include:Foreign Service Retirement and Disability payments, 22 U.S.C. 1104; [1]Social security payments, 42 U.S.C. 407;Injury or death compensation payments from war risk hazards, 42 U.S.C. 1717;Wages of fishermen, seamen, and apprentices, 46 U.S.C. 601; [2]Civil service retirement benefits, 5 U.S.C. 729, 2265; [3]Longshoremen's and Harbor Workers' Compensation Act death and disability benefits, 33 U.S.C. 916;Railroad Retirement Act annuities and pensions, 45 U.S.C. 228(L); [4]Veterans benefits, 45 U.S.C. 352(E); [5]Special pensions paid to winners of the Congressional Medal of Honor, 38 U.S.C. 3101; [6] andFederal homestead lands on debts contracted before issuance of the patent, 43 U.S.C. 175.He may also exempt an interest in property in which the debtor had an interest as a tenant by the entirety or joint tenant to the extent that interest would have been exempt from process under applicable nonbankruptcy law.Under proposed section 541, all property of the debtor becomes property of the estate, but the debtor is permitted to exempt certain property from property of the estate under this section. Property may be exempted even if it is subject to a lien, but only the unencumbered portion of the property is to be counted in computing the "value" of the property for the purposes of exemption.As under current law, the debtor will be permitted to convert nonexempt property into exempt property before filing a bankruptcy petition. The practice is not fraudulent as to creditors, and permits the debtor to make full use of the exemptions to which he is entitled under the law.Subsection (c) insulates exempt property from prepetition claims other than tax claims (whether or not dischargeable), and other than alimony, maintenance, or support claims that are excepted from discharge. The bankruptcy discharge does not prevent enforcement of valid liens. The rule of Long v. Bullard, 117 U.S. 617 (1886), is accepted with respect to the enforcement of valid liens on nonexempt property as well as on exempt property. Cf. Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 583 (1935).Subsection (c)(3) permits the collection of dischargeable taxes from exempt assets. Only assets exempted from levy under Section 6334 of the Internal Revenue Code [title 26] or under applicable state or local tax law cannot be applied to satisfy these tax claims. This rule applies to prepetition tax claims against the debtor regardless of whether the claims do or do not receive priority and whether they are dischargeable or nondischargeable. Thus, even if a tax is dischargeable vis-a-vis the debtor's after-acquired assets, it may nevertheless be collectible from exempt property held by the estate. (Taxes incurred by the debtor's estate which are collectible as first priority administrative expenses are not collectible from the debtor's estate which are collectible as first priority administrative expenses are not collectible from the debtor's exempt assets.)Subsection (d) protects the debtor's exemptions, either Federal or State, by making unenforceable in a bankruptcy case a waiver of exemptions or a waiver of the debtor's avoiding powers under the following subsections.Subsection (e) protects the debtor's exemptions, his discharge, and thus his fresh start by permitting him to avoid certain liens on exempt property. The debtor may avoid a judicial lien on any property to the extent that the property could have been exempted in the absence of the lien, and may similarly avoid a nonpurchase-money security interest in certain household and personal goods. The avoiding power is independent of any*

waiver of exemptions.Subsection (f) gives the debtor the ability to exempt property that the trustee recovers under one of the trustee's avoiding powers if the property was involuntarily transferred away from the debtor (such as by the fixing of a judicial lien) and if the debtor did not conceal the property. The debtor is also permitted to exempt property that the trustee recovers as the result of the avoiding of the fixing of certain security interests to the extent that the debtor could otherwise have exempted the property.Subsection (g) provides that if the trustee does not exercise an avoiding power to recover a transfer of property that would be exempt, the debtor may exercise it and exempt the property, if the transfer was involuntary and the debtor did not conceal the property. If the debtor wishes to preserve his right to pursue any action under this provision, then he must intervene in any action brought by the trustee based on the same cause of action. It is not intended that the debtor be given an additional opportunity to avoid a transfer or that the transferee should have to defend the same action twice. Rather, the section is primarily designed to give the debtor the rights the trustee could have, but has not, pursued. The debtor is given no greater rights under this provision than the trustee, and thus, the debtor's avoiding powers under proposed sections 544, 545, 547, and 548, are subject to proposed 546, as are the trustee's powers.These subsections are cumulative. The debtor is not required to choose which he will use to gain an exemption. Instead, he may use more than one in any particular instance, just as the trustee's avoiding powers are cumulative.Subsection (h) permits recovery by the debtor of property transferred by an avoided transfer from either the initial or subsequent transferees. It also permits preserving a transfer for the benefit of the debtor. In either event, the debtor may exempt the property recovered or preserved.Subsection (i) makes clear that the debtor may exempt property under the avoiding subsections (f) and (h) only to the extent he has exempted less property than allowed under subsection (b).Subsection (j) makes clear that the liability of the debtor's exempt property is limited to the debtor's aliquot share of the costs and expenses recovery of property that the trustee recovers and the debtor later exempts, and any costs and expenses of avoiding a transfer by the debtor that the debtor has not already paid.Subsection (k) requires the debtor to file a list of property that he claims as exempt from property of the estate. Absent an objection to the list, the property is exempted. A dependent of the debtor may file it and thus be protected if the debtor fails to file the list.Subsection (l) provides the rule for a joint case.

HOUSE REPORT NO. 95-595*Subsection (a) of this section defines two terms: "dependent" includes the debtor's spouse, whether or not actually dependent; and "value" means fair market value as of the date of the filing of the petition.Subsection (b), the operative subsection of this section, is a significant departure from present law. It permits an individual debtor in a bankruptcy case a choice between exemption systems. The debtor may choose the Federal exemptions prescribed in subsection (d), or he may choose the exemptions to which he is entitled under other Federal law and the law of the State of his domicile. If the debtor chooses the latter, some of the items that may be exempted under other Federal laws include:-Foreign Service Retirement and Disability payments, 22 U.S.C. 1104; [7]-Social security payments, 42 U.S.C. 407;-Injury or death compensation payments from war risk hazards, 42 U.S.C. 1717;-Wages of fishermen, seamen, and apprentices, 46 U.S.C. 601; [8]-Civil service retirement benefits, 5 U.S.C. 729, 2265; [9]-Longshoremen's and Harbor Workers' Compensation Act death and disability benefits, 33 U.S.C. 916;-Railroad Retirement Act annuities and pensions, 45 U.S.C. 228(l); [10]-Veterans benefits, 45 U.S.C. 352(E); [11]-Special pensions paid to winners of the Congressional Medal of Honor, 38 U.S.C. 3101; [12] and-Federal homestead lands on debts contracted before issuance of the patent, 43 U.S.C. 175.He may also exempt an interest in property in which the debtor had an interest as a tenant by the entirety or joint tenant to the extent that interest would have been exempt from process under applicable nonbankruptcy law. The Rules will provide for the situation where the debtor's choice of exemption, Federal or State, was improvident and should be changed, for example, where the court has ruled against the debtor with respect to a major exemption.Under proposed 11 U.S.C. 541, all property of the debtor becomes property of the estate, but the debtor is permitted to exempt certain property from property of the estate under this section. Property may be exempted even if it is*

subject to a lien, but only the unencumbered portion of the property is to be counted in computing the "value" of the property for the purposes of exemption. Thus, for example, a residence worth $30,000 with a mortgage of $25,000 will be exemptable [sic] to the extent of $5,000. This follows current law. The remaining value of the property will be dealt with in the bankruptcy case as is any interest in property that is subject to a lien.As under current law, the debtor will be permitted to convert nonexempt property into exempt property before filing a bankruptcy petition. See Hearings, pt. 3, at 1355-58. The practice is not fraudulent as to creditors and permits the debtor to make full use of the exemptions to which he is entitled under the law.Subsection (c) insulates exempt property from prepetition claims, except tax and alimony, maintenance, or support claims that are excepted from discharge. The bankruptcy discharge will not prevent enforcement of valid liens. The rule of Long v. Bullard, 117 U.S. 617 (1886) [6 S.Ct. 917, 29 L.Ed. 1004], is accepted with respect to the enforcement of valid liens on nonexempt property as well as on exempt property. Cf. Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 583 (1935) [55 S.Ct. 854].Subsection (d) specifies the Federal exemptions to which the debtor is entitled. They are derived in large part from the Uniform Exemptions Act, promulgated by the Commissioners of Uniform State Laws in August, 1976. Eleven categories of property are exempted. First is a homestead to the extent of $10,000, which may be claimed in real or personal property that the debtor or a dependent of the debtor uses as a residence. Second, the debtor may exempt a motor vehicle to the extent of $1500. Third, the debtor may exempt household goods, furnishings, clothing, and similar household items, held primarily for the personal, family, or household use of the debtor or a dependent of the debtor. "Animals" includes all animals, such as pets, livestock, poultry, and fish, if they are held primarily for personal, family or household use. The limitation for third category items is $300 on any particular item. The debtor may also exempt up to $750 of personal jewelry.Paragraph (5) permits the exemption of $500, plus any unused amount of the homestead exemption, in any property, in order not to discriminate against the nonhomeowner. Paragraph (6) grants the debtor up to $1000 in implements, professional books, or tools, of the trade of the debtor or a dependent. Paragraph (7) exempts a life insurance contract, other than a credit life insurance contract, owned by the debtor. This paragraph refers to the life insurance contract itself. It does not encompass any other rights under the contract, such as the right to borrow out the loan value. Because of this provision, the trustee may not surrender a life insurance contract, which remains property of the debtor if he chooses the Federal exemptions. Paragraph (8) permits the debtor to exempt up to $5000 in loan value in a life insurance policy owned by the debtor under which the debtor or an individual of whom the debtor is a dependent is the insured. The exemption provided by this paragraph and paragraph (7) will also include the debtor's rights in a group insurance certificate under which the insured is an individual of whom the debtor is a dependent (assuming the debtor has rights in the policy that could be exempted) or the debtor. A trustee is authorized to collect the entire loan value on every life insurance policy owned by the debtor as property of the estate. First, however, the debtor will choose which policy or policies under which the loan value will be exempted. The $5000 figure is reduced by the amount of any automatic premium loan authorized after the date of the filing of the petition under section 542(d). Paragraph (9) exempts professionally prescribed health aids.Paragraph (10) exempts certain benefits that are akin to future earnings of the debtor. These include social security, unemployment compensation, or public assistance benefits, veteran's benefits, disability, illness, or unemployment benefits, alimony, support, or separate maintenance (but only to the extent reasonably necessary for the support of the debtor and any dependents of the debtor), and benefits under a certain stock bonus, pension, profitsharing, annuity or similar plan based on illness, disability, death, age or length of service. Paragraph (11) allows the debtor to exempt certain compensation for losses. These include crime victim's reparation benefits, wrongful death benefits (with a reasonably necessary for support limitation), life insurance proceeds (same limitation), compensation for bodily injury, not including pain and suffering ($10,000 limitation), and loss of future earnings payments (support limitation). This provision in subparagraph (D)(11) is designed to cover payments in compensation of actual bodily injury, such as the loss of a limb, and is not intended to include

the attendant costs that accompany such a loss, such as medical payments, pain and suffering, or loss of earnings. Those items are handled separately by the bill.Subsection (e) protects the debtor's exemptions, either Federal or State, by making unenforceable in a bankruptcy case a waiver of exemptions or a waiver of the debtor's avoiding powers under the following subsections.Subsection (f) protects the debtor's exemptions, his discharge, and thus his fresh start by permitting him to avoid certain liens on exempt property. The debtor may avoid a judicial lien on any property to the extent that the property could have been exempted in the absence of the lien, and may similarly avoid a nonpurchase-money security interest in certain household and personal goods. The avoiding power is independent of any waiver of exemptions.Subsection (g) gives the debtor the ability to exempt property that the trustee recovers under one of the trustee's avoiding powers if the property was involuntarily transferred away from the debtor (such as by the fixing of a judicial lien) and if the debtor did not conceal the property. The debtor is also permitted to exempt property that the trustee recovers as the result of the avoiding of the fixing of certain security interests to the extent that the debtor could otherwise have exempted the property.If the trustee does not pursue an avoiding power to recover a transfer of property that would be exempt, the debtor may pursue it and exempt the property, if the transfer was involuntary and the debtor did not conceal the property. If the debtor wishes to preserve his right to pursue an action under this provision, then he must intervene in any action brought by the trustee based on the same cause of action. It is not intended that the debtor be given an additional opportunity to avoid a transfer or that the transferee have to defend the same action twice. Rather, the section is primarily designed to give the debtor the rights the trustee could have pursued if the trustee chooses not to pursue them. The debtor is given no greater rights under this provision than the trustee, and thus the debtor's avoiding powers under proposed 11 U.S.C. 544, 545, 547, and 548, are subject to proposed 11 U.S.C. 546, as are the trustee's powers.These subsections are cumulative. The debtor is not required to choose which he will use to gain an exemption. Instead, he may use more than one in any particular instance, just as the trustee's avoiding powers are cumulative.Subsection (i) permits recovery by the debtor of property transferred in an avoided transfer from either the initial or subsequent transferees. It also permits preserving a transfer for the benefit of the debtor. Under either case the debtor may exempt the property recovered or preserved.Subsection (k) makes clear that the debtor's aliquot share of the costs and expenses [for] recovery of property that the trustee recovers and the debtor later exempts, and any costs and expenses of avoiding a transfer by the debtor that the debtor has not already paid.Subsection (l) requires the debtor to file a list of property that he claims as exempt from property of the estate. Absent an objection to the list, the property is exempted. A dependent of the debtor may file it and thus be protected if the debtor fails to file the list.Subsection (m) requires the clerk of the bankruptcy court to give notice of any exemptions claimed under subsection (l), in order that parties in interest may have an opportunity to object to the claim.Subsection (n) provides the rule for a joint case: each debtor is entitled to the Federal exemptions provided under this section or to the State exemptions, whichever the debtor chooses.

REFERENCES IN TEXT*The Federal Rules of Bankruptcy Procedure, referred to in subsec. (b)(1), are set out in the Appendix to this title.The Internal Revenue Code of 1986, referred to in subsecs. (b)(3)(C), (4), (d)(10)(E)(iii), (12), and (n), is classified generally to Title 26, Internal Revenue Code.Sections 3(a)(47), 12, and 15(d) of the Securities Exchange Act of 1934, referred to in subsec. (q)(1)(B)(i), (ii), are classified to sections 78c(a)(47), 78l, and 78o(d), respectively, of Title 15, Commerce and Trade.Section 6 of the Securities Exchange Act of 1933, referred to in subsec. (q)(1)(B)(ii), is classified to section 77f of Title 15, Commerce and Trade.*

AMENDMENTS2010*-Subsec. (b)(3)(A). Pub. L. 111-327, §2(a)(17)(A), substituted "petition to the place" for "petition at the place" and "located in a single State" for "located at a single State".Subsec. (c)(1). Pub. L. 111-327, §2(a)(17)(B), substituted "such paragraph" for "section 523(a)(5)".**2005****-Subsec. (b). Pub. L. 109-8, §224(a)(1)(B)-(F), designated introductory provisions of subsec. (b) as par. (1), substituted "paragraph (3)" for "paragraph (2)" in two places and "paragraph (2)" for "paragraph (1)" wherever appearing, struck out "Such*

*property is-" after "case is filed.", and struck out former par. (1) which read: "property that is specified under subsection (d) of this section, unless the State law that is applicable to the debtor under paragraph (2)(A) of this subsection specifically does not so authorize; or, in the alternative,".Subsec. (b)(2). Pub. L. 109-8, §224(a)(1)(B), added par. (2). Former par. (2) redesignated (3).Subsec. (b)(2)(C). Pub. L. 109-8, §224(a)(1)(A)(i)-(iii), added subpar. (C).Subsec. (b)(3). Pub. L. 109-8, §307(2), inserted "If the effect of the domiciliary requirement under subparagraph (A) is to render the debtor ineligible for any exemption, the debtor may elect to exempt property that is specified under subsection (d)." at end. Pub. L. 109-8, §224(a)(1)(A)(iv), redesignated par. (2) as (3) and inserted introductory provisions.Subsec. (b)(3)(A). Pub. L. 109-8, §308(1), inserted "subject to subsections (o) and (p)," before "any property". Pub. L. 109-8, §307(1), substituted "730 days" for "180 days" and "or if the debtor's domicile has not been located at a single State for such 730-day period, the place in which the debtor's domicile was located for 180 days immediately preceding the 730-day period or for a longer portion of such 180-day period than in any other place" for ", or for a longer portion of such 180-day period than in any other place".Subsec. (b)(4). Pub. L. 109-8, §224(a)(1)(G), added par. (4).Subsec. (c)(1). Pub. L. 109-8, §216(1), added par. (1) and struck out former par. (1) which read as follows: "a debt of a kind specified in section 523(a)(1) or 523(a)(5) of this title;".Subsec. (d). Pub. L. 109-8, §224(a)(2)(A), substituted "subsection (b)(2)" for "subsection (b)(1)" in introductory provisions.Subsec. (d)(12). Pub. L. 109-8, §224(a)(2)(B), added par. (12).Subsec. (f)(1)(A). Pub. L. 109-8, §216(2), substituted "a debt of a kind that is specified in section 523(a)(5); or" for "a debt-"(i) to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for, or support of such spouse or child, in connection with a separation agreement, divorce decree or other order of a court of record, determination made in accordance with State or territorial law by a governmental unit, or property settlement agreement; and" (ii) to the extent that such debt-"(I) is not assigned to another entity, voluntarily, by operation of law, or otherwise; and"(II) includes a liability designated as alimony, maintenance, or support, unless such liability is actually in the nature of alimony, maintenance or support.; or".Subsec. (f)(4). Pub. L. 109-8, §313(a), added par. (4).Subsec. (g)(2). Pub. L. 109-8, §216(3), substituted "subsection (f)(1)(B)" for "subsection (f)(2)".Subsec. (n). Pub. L. 109-8, §224(e)(1), added subsec. (n).Subsec. (o). Pub. L. 109-8, §308(2), added subsec. (o).Subsecs. (p), (q). Pub. L. 109-8, §322(a), added subsecs. (p) and (q).**2000**-Subsec. (c)(4). Pub. L. 106-420 added par. (4).**1994**-Subsec. (b). Pub. L. 103-394, §501(d)(12)(A), substituted "Federal Rules of Bankruptcy Procedure" for "Bankruptcy Rules".Subsec. (d)(1) to (6). Pub. L. 103-394, §108(d)(1)-(6), substituted "$15,000" for "$7,500" in par. (1), "$2,400" for "$1,200" in par. (2), "$400" and "$8,000" for "$200" and "$4,000", respectively, in par. (3), "$1,000" for "$500" in par. (4), "$800" and "$7,500" for "$400" and "$3,750", respectively, in par. (5), and "$1,500" for "$750" in par. (6).Subsec. (d)(8). Pub. L. 103-394, §108(d)(7), substituted "$8,000" for "$4,000".Subsec. (d)(10)(E)(iii). Pub. L. 103-394, §501(d)(12)(B), substituted "or 408" for "408, or 409" and "Internal Revenue Code of 1986" for "Internal Revenue Code of 1954 (26 U.S.C. 401(a), 403(a), 403(b), 408, or 409)".Subsec. (d)(11)(D). Pub. L. 103-394, §108(d)(8), substituted "$15,000" for "$7,500".Subsec. (f)(1). Pub. L. 103-394, §§303(3), 310, designated existing provisions as par. (1) and inserted "but subject to paragraph (3)" after "waiver of exemptions" in introductory provisions. Former par. (1) redesignated subpar. (A) of par. (1).Subsec. (f)(1)(A). Pub. L. 103-394, §§303(2), 304, redesignated par. (1) as subpar. (A) of par. (1) and inserted ", other than a judicial lien that secures a debt-"(i) to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for, or support of such spouse or child, in connection with a separation agreement, divorce decree or other order of a court of record, determination made in accordance with State or territorial law by a governmental unit, or property settlement agreement; and"(ii) to the extent that such debt-"(I) is not assigned to another entity, voluntarily, by operation of law, or otherwise; and"(II) includes a liability designated as alimony, maintenance, or support, unless such liability is actually in the nature of alimony, maintenance or support."Subsec. (f)(1)(B). Pub. L. 103-394, §303(1), redesignated par. (2) as subpar. (B) of par. (1) and subpars. (A) to (C) of par. (2) as cls. (i) to (iii), respectively, of subpar. (B) of par. (1).Subsec. (f)(2). Pub. L. 103-394,*

*§303(4), added par. (2). Former par. (2) redesignated subpar. (B) of par. (1).Subsec. (f)(3). Pub. L. 103-394, §310(2), added par. (3).**1990**-Subsec. (c)(3). Pub. L. 101-647 added par. (3).**1986**-Subsec. (h)(1). Pub. L. 99-554, §283(i)(1), substituted "553 of this title" for "553 of this tittle".Subsec. (i)(2). Pub. L. 99-554, §283(i)(2), substituted "this" for "his" after "subsection (g) of".**1984**-Subsec. (a)(2). Pub. L. 98-353, §453(a), inserted "or, with respect to property that becomes property of an estate after such date, as of the date such property becomes property of the estate".Subsec. (b). Pub. L. 98-353, §306(a), inserted provision that in joint cases filed under section 302 of this title and individual cases filed under section 301 or 303 of this title by or against debtors who are husband and wife, and whose estates are ordered to be jointly administered under Rule 1015(b) of the Bankruptcy Rules, one debtor may not elect to exempt property listed in paragraph (1) and the other debtor elect to exempt property listed in paragraph (2) of this subsection, but that if the parties cannot agree on the alternative to be elected, they shall be deemed to elect paragraph (1), where such election is permitted under the law of the jurisdiction where the case is filed.Subsec. (c). Pub. L. 98-353, §453(b), amended subsec. (c) generally. Prior to amendment, subsec. (c) read as follows: "Unless the case is dismissed, property exempted under this section is not liable during or after the case for any debt of the debtor that arose, or that is determined under section 502 of this title as if such claim had arisen before the commencement of the case, except-"(1) a debt of a kind specified in section 523(a)(1) or section 523(a)(5) of this title; or"(2) a lien that is-"(A) not avoided under section 544, 545, 547, 548, 549, or 724(a) of this title;"(B) not voided under section 506(d) of this title; or"(C)(i) a tax lien, notice of which is properly filed; and"(ii) avoided under section 545(2) of this title."Subsec. (d)(3). Pub. L. 98-353, §306(b), inserted "or $4,000 in aggregate value".Subsec. (d)(5). Pub. L. 98-353, §306(c), amended par. (5) generally. Prior to amendment, par. (5) read as follows: "The debtor's aggregate interest, not to exceed in value $400 plus any unused amount of the exemption provided under paragraph (1) of this subsection, in any property."Subsec. (e). Pub. L. 98-353, §453(c), substituted "an exemption" for "exemptions".Subsec. (m). Pub. L. 98-353, §306(d), substituted "Subject to the limitation in subsection (b), this section shall apply separately with respect to each debtor in a joint case" for "This section shall apply separately with respect to each debtor in a joint case".*

***EFFECTIVE DATE OF 2005 AMENDMENT**Amendment by Pub. L. 109-8 effective 180 days after Apr. 20, 2005, with amendments by sections 216, 224(a), (e)(1), 307, and 313(a) of Pub. L. 109-8 not applicable with respect to cases commenced under this title before such effective date, except as otherwise provided, and amendments by sections 308 and 322(a) of Pub. L. 109-8 applicable with respect to cases commenced under this title on or after Apr. 20, 2005, see section 1501 of Pub. L. 109-8 set out as a note under section 101 of this title.*

***EFFECTIVE DATE OF 1994 AMENDMENT**Amendment by Pub. L. 103-394 effective Oct. 22, 1994, and not applicable with respect to cases commenced under this title before Oct. 22, 1994, see section 702 of Pub. L. 103-394 set out as a note under section 101 of this title.*

***EFFECTIVE DATE OF 1986 AMENDMENT**Amendment by Pub. L. 99-554 effective 30 days after Oct. 27, 1986, see section 302(a) of Pub. L. 99-554 set out as a note under section 581 of Title 28, Judiciary and Judicial Procedure.*

***EFFECTIVE DATE OF 1984 AMENDMENT**Amendment by Pub. L. 98-353 effective with respect to cases filed 90 days after July 10, 1984, see section 552(a) of Pub. L. 98-353 set out as a note under section 101 of this title.*

***ADJUSTMENT OF DOLLAR AMOUNTS**The dollar amounts specified in this section were adjusted by notices of the Judicial Conference of the United States pursuant to section 104 of this title as follows:By notice dated Feb. 5, 2019, 84 F.R. 3488, effective Apr. 1, 2019, in subsec. (d)(1), dollar amount "23,675" was adjusted to "25,150"; in subsec. (d)(2), dollar amount "3,775" was adjusted to "4,000"; in subsec. (d)(3), dollar amounts "600" and*

"12,625" were adjusted to "625" and "13,400", respectively; in subsec. (d)(4), dollar amount "1,600" was adjusted to "1,700"; in subsec. (d)(5), dollar amounts "1,250" and "11,850" were adjusted to "1,325" and "12,575", respectively; in subsec. (d)(6), dollar amount "2,375" was adjusted to "2,525"; in subsec. (d)(8), dollar amount "12,625" was adjusted to "13,400"; in subsec. (d)(11)(D), dollar amount "23,675" was adjusted to "25,150"; in subsec. (f)(3), dollar amount "6,425" was adjusted to "6,825"; in subsec. (f)(4), dollar amount "675" was adjusted to "725" each time it appeared; in subsec. (n), dollar amount "1,283,025" was adjusted to "1,362,800"; in subsec. (p), dollar amount "160,375" was adjusted to "170,350"; and, in subsec. (q), dollar amount "160,375" was adjusted to "170,350". See notice of the Judicial Conference of the United States set out as a note under section 104 of this title.By notice dated Feb. 16, 2016, 81 F.R. 8748, effective Apr. 1, 2016, in subsec. (d)(1), dollar amount "22,975" was adjusted to "23,675"; in subsec. (d)(2), dollar amount "3,675" was adjusted to "3,775"; in subsec. (d)(3), dollar amounts "575" and "12,250" were adjusted to "600" and "12,625", respectively; in subsec. (d)(4), dollar amount "1,550" was adjusted to "1,600"; in subsec. (d)(5), dollar amounts "1,225" and "11,500" were adjusted to "1,250" and "11,850", respectively; in subsec. (d)(6), dollar amount "2,300" was adjusted to "2,375"; in subsec. (d)(8), dollar amount "12,250" was adjusted to "12,625"; in subsec. (d)(11)(D), dollar amount "22,975" was adjusted to "23,675"; in subsec. (f)(3), dollar amount "6,225" was adjusted to "6,425"; in subsec. (f)(4), dollar amount "650" was adjusted to "675" each time it appeared; in subsec. (n), dollar amount "1,245,475" was adjusted to "1,283,025"; in subsec. (p), dollar amount "155,675" was adjusted to "160,375"; and, in subsec. (q), dollar amount "155,675" was adjusted to "160,375".By notice dated Feb. 12, 2013, 78 F.R. 12089, effective Apr. 1, 2013, in subsec. (d)(1), dollar amount "21,625" was adjusted to "22,975"; in subsec. (d)(2), dollar amount "3,450" was adjusted to "3,675"; in subsec. (d)(3), dollar amounts "550" and "11,525" were adjusted to "575" and "12,250", respectively; in subsec. (d)(4), dollar amount "1,450" was adjusted to "1,550"; in subsec. (d)(5), dollar amounts "1,150" and "10,825" were adjusted to "1,225" and "11,500", respectively; in subsec. (d)(6), dollar amount "2,175" was adjusted to "2,300"; in subsec. (d)(8), dollar amount "11,525" was adjusted to "12,250"; in subsec. (d)(11)(D), dollar amount "21,625" was adjusted to "22,975"; in subsec. (f)(3), dollar amount "5,850" was adjusted to "6,225"; in subsec. (f)(4), dollar amount "600" was adjusted to "650" each time it appeared; in subsec. (n), dollar amount "1,171,650" was adjusted to "1,245,475"; in subsec. (p), dollar amount "146,450" was adjusted to "155,675"; and, in subsec. (q), dollar amount "146,450" was adjusted to "155,675".By notice dated Feb. 19, 2010, 75 F.R. 8747, effective Apr. 1, 2010, in subsec. (d)(1), dollar amount "20,200" was adjusted to "21,625"; in subsec. (d)(2), dollar amount "3,225" was adjusted to "3,450"; in subsec. (d)(3), dollar amounts "525" and "10,775" were adjusted to "550" and "11,525", respectively; in subsec. (d)(4), dollar amount "1,350" was adjusted to "1,450"; in subsec. (d)(5), dollar amounts "1,075" and "10,125" were adjusted to "1,150" and "10,825", respectively; in subsec. (d)(6), dollar amount "2,025" was adjusted to "2,175"; in subsec. (d)(8), dollar amount "10,775" was adjusted to "11,525"; in subsec. (d)(11)(D), dollar amount "20,200" was adjusted to "21,625"; in subsec. (f)(3)(B), dollar amount "5,475" was adjusted to "5,850"; in subsec. (f)(4)(B), dollar amount "550" was adjusted to "600" each time it appeared; in subsec. (n), dollar amount "1,095,000" was adjusted to "1,171,650"; in subsec. (p)(1), dollar amount "136,875" was adjusted to "146,450"; and, in subsec. (q)(1), dollar amount "136,875" was adjusted to "146,450".By notice dated Feb. 7, 2007, 72 F.R. 7082, effective Apr. 1, 2007, in subsec. (d)(1), dollar amount "18,450" was adjusted to "20,200"; in subsec. (d)(2), dollar amount "2,950" was adjusted to "3,225"; in subsec. (d)(3), dollar amounts "475" and "9,850" were adjusted to "525" and "10,775", respectively; in subsec. (d)(4), dollar amount "1,225" was adjusted to "1,350"; in subsec. (d)(5), dollar amounts "975" and "9,250" were adjusted to "1,075" and "10,125", respectively; in subsec. (d)(6), dollar amount "1,850" was adjusted to "2,025"; in subsec. (d)(8), dollar amount "9,850" was adjusted to "10,775"; in subsec. (d)(11)(D), dollar amount "18,450" was adjusted to "20,200"; in subsec. (f)(3), dollar amount "5,000" was adjusted to "5,475"; in subsec. (f)(4), dollar amount "500" was adjusted to "550" each time it appeared; in subsec. (n), dollar amount "1,000,000" was adjusted to

"1,095,000"; in subsec. (p), dollar amount "125,000" was adjusted to "136,875"; and, in subsec. (q), dollar amount "125,000" was adjusted to "136,875".By notice dated Feb. 18, 2004, 69 F.R. 8482, effective Apr. 1, 2004, in subsec. (d)(1), dollar amount "17,425" was adjusted to "18,450"; in subsec. (d)(2), dollar amount "2,775" was adjusted to "2,950"; in subsec. (d)(3), dollar amounts "450" and "9,300" were adjusted to "475" and "9,850", respectively; in subsec. (d)(4), dollar amount "1,150" was adjusted to "1,225"; in subsec. (d)(5), dollar amounts "925" and "8,725" were adjusted to "975" and "9,250", respectively; in subsec. (d)(6), dollar amount "1,750" was adjusted to "1,850"; in subsec. (d)(8), dollar amount "9,300" was adjusted to "9,850"; and, in subsec. (d)(11)(D), dollar amount "17,425" was adjusted to "18,450".By notice dated Feb. 13, 2001, 66 F.R. 10910, effective Apr. 1, 2001, in subsec. (d)(1), dollar amount "16,150" was adjusted to "17,425"; in subsec. (d)(2), dollar amount "2,575" was adjusted to "2,775"; in subsec. (d)(3), dollar amounts "425" and "8,625" were adjusted to "450" and "9,300", respectively; in subsec. (d)(4), dollar amount "1,075" was adjusted to "1,150"; in subsec. (d)(5), dollar amounts "850" and "8,075" were adjusted to "925" and "8,725", respectively; in subsec. (d)(6), dollar amount "1,625" was adjusted to "1,750"; in subsec. (d)(8), dollar amount "8,625" was adjusted to "9,300"; and, in subsec. (d)(11)(D), dollar amount "16,150" was adjusted to "17,425".By notice dated Feb. 3, 1998, 63 F.R. 7179, effective Apr. 1, 1998, in subsec. (d)(1), dollar amount "15,000" was adjusted to "16,150"; in subsec. (d)(2), dollar amount "2,400" was adjusted to "2,575"; in subsec. (d)(3), dollar amounts "400" and "8,000" were adjusted to "425" and "8,625", respectively; in subsec. (d)(4), dollar amount "1,000" was adjusted to "1,075"; in subsec. (d)(5), dollar amounts "800" and "7,500" were adjusted to "850" and "8,075", respectively; in subsec. (d)(6), dollar amount "1,500" was adjusted to "1,625"; in subsec. (d)(8), dollar amount "8,000" was adjusted to "8,625"; and, in subsec. (d)(11)(D), dollar amount "15,000" was adjusted to "16,150".

11 U.S.C. § 523

Section 523 - Exceptions to discharge

(a) A discharge under section 727, 1141, 1192 [1] 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt-

(1) for a tax or a customs duty-

(A) of the kind and for the periods specified in section 507(a)(3) or 507(a)(8) of this title, whether or not a claim for such tax was filed or allowed;

(B) with respect to which a return, or equivalent report or notice, if required-

(i) was not filed or given; or

(ii) was filed or given after the date on which such return, report, or notice was last due, under applicable law or under any extension, and after two years before the date of the filing of the petition; or

(C) with respect to which the debtor made a fraudulent return or willfully attempted in any manner to evade or defeat such tax;

(2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by-

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;

(B) use of a statement in writing-

(i) that is materially false;

(ii) respecting the debtor's or an insider's financial condition;

(iii) on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied; and

(iv) that the debtor caused to be made or published with intent to deceive; or

(C)

(i) for purposes of subparagraph (A)-

(I) consumer debts owed to a single creditor and aggregating more than $500 [2] for luxury goods or services incurred by an individual debtor on or within 90 days before the order for relief under this title are presumed to be nondischargeable; and

(II) cash advances aggregating more than $750 [2] that are extensions of consumer credit under an open end credit plan obtained by an individual debtor on or within 70 days before the order for relief under this title, are presumed to be nondischargeable; and

(ii) for purposes of this subparagraph-

(I) the terms "consumer", "credit", and "open end credit plan" have the same meanings as in section 103 of the Truth in Lending Act; and

(II) the term "luxury goods or services" does not include goods or services reasonably necessary for the support or maintenance of the debtor or a dependent of the debtor;

(3) neither listed nor scheduled under section 521(a)(1) of this title, with the name, if known to the debtor, of the creditor to whom such debt is owed, in time to permit-

(A) if such debt is not of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim, unless such creditor had notice or actual knowledge of the case in time for such timely filing; or

(B) if such debt is of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim and timely request for a determination of dischargeability of such debt under one of such paragraphs, unless such creditor had notice or actual knowledge of the case in time for such timely filing and request;

(4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny;

(5) for a domestic support obligation;

(6) for willful and malicious injury by the debtor to another entity or to the property of another entity;

(7) to the extent such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss, other than a tax penalty-

(A) relating to a tax of a kind not specified in paragraph (1) of this subsection; or

(B) imposed with respect to a transaction or event that occurred before three years before the date of the filing of the petition;

(8) unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents, for-

(A)

(i) an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution; or

(ii) an obligation to repay funds received as an educational benefit, scholarship, or stipend; or

(B) any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual;

(9) for death or personal injury caused by the debtor's operation of a motor vehicle, vessel, or aircraft if such operation was unlawful because the debtor was intoxicated from using

alcohol, a drug, or another substance;

(10) that was or could have been listed or scheduled by the debtor in a prior case concerning the debtor under this title or under the Bankruptcy Act in which the debtor waived discharge, or was denied a discharge under section 727(a)(2), (3), (4), (5), (6), or (7) of this title, or under section 14c(1), (2), (3), (4), (6), or (7) of such Act;

(11) provided in any final judgment, unreviewable order, or consent order or decree entered in any court of the United States or of any State, issued by a Federal depository institutions regulatory agency, or contained in any settlement agreement entered into by the debtor, arising from any act of fraud or defalcation while acting in a fiduciary capacity committed with respect to any depository institution or insured credit union;

(12) for malicious or reckless failure to fulfill any commitment by the debtor to a Federal depository institutions regulatory agency to maintain the capital of an insured depository institution, except that this paragraph shall not extend any such commitment which would otherwise be terminated due to any act of such agency;

(13) for any payment of an order of restitution issued under title 18, United States Code;

(14) incurred to pay a tax to the United States that would be nondischargeable pursuant to paragraph (1);

(14A) incurred to pay a tax to a governmental unit, other than the United States, that would be nondischargeable under paragraph (1);

(14B) incurred to pay fines or penalties imposed under Federal election law;

(15) to a spouse, former spouse, or child of the debtor and not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, or a determination made in accordance with State or territorial law by a governmental unit;

(16) for a fee or assessment that becomes due and payable after the order for relief to a membership association with respect to the debtor's interest in a unit that has condominium ownership, in a share of a cooperative corporation, or a lot in a homeowners association, for as long as the debtor or the trustee has a legal, equitable, or possessory ownership interest in such unit, such corporation, or such lot, but nothing in this paragraph shall except from discharge the debt of a debtor for a membership association fee or assessment for a period arising before entry of the order for relief in a pending or subsequent bankruptcy case;

(17) for a fee imposed on a prisoner by any court for the filing of a case, motion, complaint, or appeal, or for other costs and expenses assessed with respect to such filing, regardless of an assertion of poverty by the debtor under subsection (b) or (f)(2) of section 1915 of title 28 (or a similar non-Federal law), or the debtor's status as a prisoner, as defined in section 1915(h) of title 28 (or a similar non-Federal law);

(18) owed to a pension, profit-sharing, stock bonus, or other plan established under section 401, 403, 408, 408A, 414, 457, or 501(c) of the Internal Revenue Code of 1986, under-

(A) a loan permitted under section 408(b)(1) of the Employee Retirement Income Security Act of 1974, or subject to section 72(p) of the Internal Revenue Code of 1986; or

(B) a loan from a thrift savings plan permitted under subchapter III of chapter 84 of title 5, that satisfies the requirements of section 8433(g) of such title;

but nothing in this paragraph may be construed to provide that any loan made under a governmental plan under section 414(d), or a contract or account under section 403(b), of the Internal Revenue Code of 1986 constitutes a claim or a debt under this title; or

(19) that-

(A) is for-

(i) the violation of any of the Federal securities laws (as that term is defined in section 3(a)(47) of the Securities Exchange Act of 1934), any of the State securities laws, or any regulation or order issued under such Federal or State securities laws; or

(ii) common law fraud, deceit, or manipulation in connection with the purchase or sale of any security; and

(B) results, before, on, or after the date on which the petition was filed, from-

(i) any judgment, order, consent order, or decree entered in any Federal or State judicial or administrative proceeding;

(ii) any settlement agreement entered into by the debtor; or

(iii) any court or administrative order for any damages, fine, penalty, citation, restitutionary payment, disgorgement payment, attorney fee, cost, or other payment owed by the debtor.

For purposes of this subsection, the term "return" means a return that satisfies the requirements of applicable nonbankruptcy law (including applicable filing requirements). Such term includes a return prepared pursuant to section 6020(a) of the Internal Revenue Code of 1986, or similar State or local law, or a written stipulation to a judgment or a final order entered by a nonbankruptcy tribunal, but does not include a return made pursuant to section 6020(b) of the Internal Revenue Code of 1986, or a similar State or local law.

(b) Notwithstanding subsection (a) of this section, a debt that was excepted from discharge under subsection (a)(1), (a)(3), or (a)(8) of this section, under section 17a(1), 17a(3), or 17a(5) of the Bankruptcy Act, under section 439A [3] of the Higher Education Act of 1965, or under section 733(g) [3] of the Public Health Service Act in a prior case concerning the debtor under this title, or under the Bankruptcy Act, is dischargeable in a case under this title unless, by the terms of subsection (a) of this section, such debt is not dischargeable in the case under this title.

(c)

(1) Except as provided in subsection (a)(3)(B) of this section, the debtor shall be discharged from a debt of a kind specified in paragraph (2), (4), or (6) of subsection (a) of this section, unless, on request of the creditor to whom such debt is owed, and after notice and a hearing, the court determines such debt to be excepted from discharge under paragraph (2), (4), or (6), as the case may be, of subsection (a) of this section.

(2) Paragraph (1) shall not apply in the case of a Federal depository institutions regulatory agency seeking, in its capacity as conservator, receiver, or liquidating agent for an insured depository institution, to recover a debt described in subsection (a)(2), (a)(4), (a)(6), or (a)(11) owed to such institution by an institution-affiliated party unless the receiver, conservator, or liquidating agent was appointed in time to reasonably comply, or for a Federal depository institutions regulatory agency acting in its corporate capacity as a successor to such receiver, conservator, or liquidating agent to reasonably comply, with subsection (a)(3)(B) as a creditor of such institution-affiliated party with respect to such debt.

(d) If a creditor requests a determination of dischargeability of a consumer debt under subsection (a)(2) of this section, and such debt is discharged, the court shall grant judgment in favor of the debtor for the costs of, and a reasonable attorney's fee for, the proceeding if the court finds that the position of the creditor was not substantially justified, except that the court shall not award such costs and fees if special circumstances would make the award unjust.

(e) Any institution-affiliated party of an insured depository institution shall be considered to be acting in a fiduciary capacity with respect to the purposes of subsection (a)(4) or (11).

[1] So in original. Probably should be followed by a comma.

[2] See Adjustment of Dollar Amounts notes below.

[3] See References in Text note below.

11 U.S.C. § 523

Pub. L. 95-598, Nov. 6, 1978, 92 Stat. 2590; Pub. L. 96-56, §3, Aug. 14, 1979, 93 Stat. 387; Pub. L. 97-35, title XXIII, §2334(b), Aug. 13, 1981, 95 Stat. 863; Pub. L. 98-353, title III, §§307, 371, 454, July 10, 1984, 98 Stat. 353, 364, 375; Pub. L. 99-554, title II, §§257(n), 281, 283(j), Oct. 27, 1986, 100 Stat. 3115-3117; Pub. L. 101-581, §2(a), Nov. 15, 1990, 104 Stat. 2865; Pub. L. 101-647, title XXV, §2522(a), title XXXI, §3102(a), title XXXVI, §3621, Nov. 29, 1990, 104 Stat. 4865, 4916, 4964; Pub. L. 103-322, title XXXII, §3209340934,, 108 Stat. 2135; Pub. L. 103-394, title II, §221, title III, §§304(e), (h)(3), 306, 309, title V, §501(d)(13), Oct. 22, 1994, 108 Stat. 4129, 4133-4135, 4137, 4145; Pub. L. 104-134, title I, §101 [(a)] [title VIII, §804(b)], Apr. 26, 1996, 110 Stat. 1321, 1321-74; renumbered title I, Pub. L. 104-140, §1(a), May 2, 1996, 110 Stat. 1327; Pub. L. 104-193, title III, §374(a), Aug. 22, 1996, 110 Stat. 2255; Pub. L. 105-244, title IX, §971(a), Oct. 7, 1998, 112 Stat. 1837; Pub. L. 107-204, title VIII, §803, July 30, 2002, 116 Stat. 801; Pub. L. 109-8, title II, §§215, 220, 224, title III, §§301, 310, 314(a), title IV, §412, title VII, §714, title XII, §§1209, 1235, title XIV, §1404(a), title XV, §1502(a)(2), Apr. 20, 2005, 119 Stat.

54, 59, 64, 75, 84, 88, 107, 128, 194, 204, 215, 216; Pub. L. 111-327, §2(a)(18), Dec. 22, 2010, 124 Stat. 3559; Pub. L. 116-54, §4(a)(8), Aug. 23, 2019, 133 Stat. 1086.

HISTORICAL AND REVISION NOTES

LEGISLATIVE STATEMENTS*Section 523(a)(1) represents a compromise between the position taken in the House bill and the Senate amendment. Section 523(a)(2) likewise represents a compromise between the position taken in the House bill and the Senate amendment with respect to the false financial statement exception to discharge. In order to clarify that a "renewal of credit" includes a "refinancing of credit", explicit reference to a refinancing of credit is made in the preamble to section 523(a)(2). A renewal of credit or refinancing of credit that was obtained by a false financial statement within the terms of section 523(a)(2) is nondischargeable. However, each of the provisions of section 523(a)(2) must be proved. Thus, under section 523(a)(2)(A) a creditor must prove that the debt was obtained by false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition. Subparagraph (A) is intended to codify current case law e.g., Neal v. Clark, 95 U.S. 704 (1887) [24 L. Ed. 586], which interprets "fraud" to mean actual or positive fraud rather than fraud implied in law. Subparagraph (A) is mutually exclusive from subparagraph (B). Subparagraph (B) pertains to the so-called false financial statement. In order for the debt to be nondischargeable, the creditor must prove that the debt was obtained by the use of a statement in writing (i) that is materially false; (ii) respecting the debtor's or an insider's financial condition; (iii) on which the creditor to whom the debtor is liable for obtaining money, property, services, or credit reasonably relied; (iv) that the debtor caused to be made or published with intent to deceive. Section 523(a)(2)(B)(iv) is not intended to change from present law since the statement that the debtor causes to be made or published with the intent to deceive automatically includes a statement that the debtor actually makes or publishes with an intent to deceive. Section 523(a)(2)(B) is explained in the House report. Under section 523(a)(2)(B)(i) a discharge is barred only as to that portion of a loan with respect to which a false financial statement is materially false.In many cases, a creditor is required by state law to refinance existing credit on which there has been no default. If the creditor does not forfeit remedies or otherwise rely to his detriment on a false financial statement with respect to existing credit, then an extension, renewal, or refinancing of such credit is nondischargeable only to the extent of the new money advanced; on the other hand, if an existing loan is in default or the creditor otherwise reasonably relies to his detriment on a false financial statement with regard to an existing loan, then the entire debt is nondischargeable under section 523(a)(2)(B). This codifies the reasoning expressed by the second circuit in In re Danns, 558 F.2d 114 (2d Cir. 1977).Section 523(a)(3) of the House amendment is derived from the Senate amendment. The provision is intended to overrule Birkett v. Columbia Bank, 195 U.S. 345 (1904) [25 S.Ct. 38, 49 L.Ed. 231, 12 Am.Bankr.Rep. 691].Section 523(a)(4) of the House amendment represents a compromise between the House bill and the Senate amendment.Section 523(a)(5) is a compromise between the House bill and the Senate amendment. The provision excepts from discharge a debt owed to a spouse, former spouse or child of the debtor, in connection with a separation agreement, divorce decree, or property settlement agreement, for alimony to, maintenance for, or support of such spouse or child but not to the extent that the debt is assigned to another entity. If the debtor has assumed an obligation of the debtor's spouse to a third party in connection with a separation agreement, property settlement agreement, or divorce proceeding, such debt is dischargeable to the extent that payment of the debt by the debtor is not actually in the nature of alimony, maintenance, or support of debtor's spouse, former spouse, or child.Section 523(a)(6) adopts the position taken in the House bill and rejects the alternative suggested in the Senate amendment. The phrase "willful and malicious injury" covers a willful and malicious conversion.Section 523(a)(7) of the House amendment adopts the position taken in the Senate amendment and rejects the position taken in the House bill. A penalty relating to a tax cannot be nondischargeable unless the tax itself is nondischargeable.Section 523(a)(8) represents a compromise between the House bill and the Senate amendment*

regarding educational loans. This provision is broader than current law which is limited to federally insured loans. Only educational loans owing to a governmental unit or a nonprofit institution of higher education are made nondischargeable under this paragraph.Section 523(b) is new. The section represents a modification of similar provisions contained in the House bill and the Senate amendment.Section 523(c) of the House amendment adopts the position taken in the Senate amendment.Section 523(d) represents a compromise between the position taken in the House bill and the Senate amendment on the issue of attorneys' fees in false financial statement complaints to determine dischargeability. The provision contained in the House bill permitting the court to award damages is eliminated. The court must grant the debtor judgment or a reasonable attorneys' fee unless the granting of judgment would be clearly inequitable.Nondischargeable debts: The House amendment retains the basic categories of nondischargeable tax liabilities contained in both bills, but restricts the time limits on certain nondischargeable taxes. Under the amendment, nondischargeable taxes cover taxes entitled to priority under section 507(a)(6) of title 11 and, in the case of individual debtors under chapters 7, 11, or 13, tax liabilities with respect to which no required return had been filed or as to which a late return had been filed if the return became last due, including extensions, within 2 years before the date of the petition or became due after the petition or as to which the debtor made a fraudulent return, entry or invoice or fraudulently attempted to evade or defeat the tax.In the case of individuals in liquidation under chapter 7 or in reorganization under chapter 11 of title 11, section 1141(d)(2) incorporates by reference the exceptions to discharge continued in section 523. Different rules concerning the discharge of taxes where a partnership or corporation reorganizes under chapter 11, apply under section 1141.The House amendment also deletes the reduction rule contained in section 523(e) of the Senate amendment. Under that rule, the amount of an otherwise nondischargeable tax liability would be reduced by the amount which a governmental tax authority could have collected from the debtor's estate if it had filed a timely claim against the estate but which it did not collect because no such claim was filed. This provision is deleted in order not to effectively compel a tax authority to file claim against the estate in "no asset" cases, along with a dischargeability petition. In no-asset cases, therefore, if the tax authority is not potentially penalized by failing to file a claim, the debtor in such cases will have a better opportunity to choose the prepayment forum, bankruptcy court or the Tax Court, in which to litigate his personal liability for a nondischargeable tax.The House amendment also adopts the Senate amendment provision limiting the nondischargeability of punitive tax penalties, that is, penalties other than those which represent collection of a principal amount of tax liability through the form of a "penalty." Under the House amendment, tax penalties which are basically punitive in nature are to be nondischargeable only if the penalty is computed by reference to a related tax liability which is nondischargeable or, if the amount of the penalty is not computed by reference to a tax liability, the transaction or event giving rise to the penalty occurred during the 3-year period ending on the date of the petition.

SENATE REPORT NO. 95-989*This section specifies which of the debtor's debts are not discharged in a bankruptcy case, and certain procedures for effectuating the section. The provision in Bankruptcy Act §17c [section 35(c) of former title 11] granting the bankruptcy courts jurisdiction to determine dischargeability is deleted as unnecessary, in view of the comprehensive grant of jurisdiction prescribed in proposed 28 U.S.C. 1334(b), which is adequate to cover the full jurisdiction that the bankruptcy courts have today over dischargeability and related issues under Bankruptcy Act §17c. The Rules of Bankruptcy Procedure will specify, as they do today, who may request determinations of dischargeability, subject, of course, to proposed 11 U.S.C. 523(c), and when such a request may be made. Proposed 11 U.S.C. 350, providing for reopening of cases, provides one possible procedure for a determination of dischargeability and related issues after a case is closed.Subsection (a) lists nine kinds of debts excepted from discharge. Taxes that are excepted from discharge are set forth in paragraph (1). These include claims against the debtor which receive priority in the second, third and sixth categories (§507(a)(3)(B) and (c) and (6)). These categories include taxes for which the tax authority failed*

to file a claim against the estate or filed its claim late. Whether or not the taxing authority's claim is secured will also not affect the claim's nondischargeability if the tax liability in question is otherwise entitled to priority.Also included in the nondischargeable debts are taxes for which the debtor had not filed a required return as of the petition date, or for which a return had been filed beyond its last permitted due date (§523(a)(1)(B)). For this purpose, the date of the tax year to which the return relates is immaterial. The late return rule applies, however, only to the late returns filed within three years before the petition was filed, and to late returns filed after the petition in title 11 was filed. For this purpose, the taxable year in question need not be one or more of the three years immediately preceding the filing of the petition.Tax claims with respect to which the debtor filed a fraudulent return, entry or invoice, or fraudulently attempted to evade or defeat any tax (§523(a)(1)(C)) are included. The date of the taxable year with regard to which the fraud occurred is immaterial.Also included are tax payments due under an agreement for deferred payment of taxes, which a debtor had entered into with the Internal Revenue Service (or State or local tax authority) before the filing of the petition and which relate to a prepetition tax liability (§523(a)(1)(D)) are also nondischargeable. This classification applies only to tax claims which would have received priority under section 507(a) if the taxpayer had filed a title 11 petition on the date on which the deferred payment agreement was entered into. This rule also applies only to installment payments which become due during and after the commencement of the title 11 case. Payments which had become due within one year before the filing of the petition receive sixth priority, and will be nondischargeable under the general rule of section 523(a)(1)(A).The above categories of nondischargeability apply to customs duties as well as to taxes.Paragraph (2) provides that as under Bankruptcy Act §17a(2) [section 35(a)(2) of former title 11], a debt for obtaining money, property, services, or a refinancing extension or renewal of credit by false pretenses, a false representation, or actual fraud, or by use of a statement in writing respecting the debtor's financial condition that is materially false, on which the creditor reasonably relied, and which the debtor made or published with intent to deceive, is excepted from discharge. This provision is modified only slightly from current section 17a(2). First, "actual fraud" is added as a ground for exception from discharge. Second, the creditor must not only have relied on a false statement in writing, but the reliance must have been reasonable. This codifies case law construing present section 17a(2). Third, the phrase "in any manner whatsoever" that appears in current law after "made or published" is deleted as unnecessary, the word "published" is used in the same sense that it is used in defamation cases.Unscheduled debts are excepted from discharge under paragraph (3). The provision, derived from section 17a(3) [section 35(a)(3) of former title 11], follows current law, but clarifies some uncertainties generated by the case law construing 17a(3). The debt is excepted from discharge if it was not scheduled in time to permit timely action by the creditor to protect his rights, unless the creditor had notice or actual knowledge of the case.Paragraph (4) excepts debts for fraud incurred by the debtor while acting in a fiduciary capacity or for defalcation, embezzlement, or misappropriation.Paragraph (5) provides that debts for willful and malicious conversion or injury by the debtor to another entity or the property of another entity are nondischargeable. Under this paragraph "willful" means deliberate or intentional. To the extent that Tinker v. Colwell, 139 U.S. 473 (1902), held that a less strict standard is intended, and to the extent that other cases have relied on Tinker to apply a "reckless disregard" standard, they are overruled.Paragraph (6) excepts from discharge debts to a spouse, former spouse, or child of the debtor for alimony to, maintenance for, or support of the spouse or child. This language, in combination with the repeal of section 456(b) of the Social Security Act (42 U.S.C. 656(b)) by section 326 of the bill, will apply to make nondischargeable only alimony, maintenance, or support owed directly to a spouse or dependent. What constitutes alimony, maintenance, or support, will be determined under the bankruptcy law, not State law. Thus, cases such as In re Waller, 494 F.2d 447 (6th Cir. 1974), are overruled, and the result in cases such as Fife v. Fife, 1 Utah 2d 281, 265 P.2d 642 (1952) is followed. The proviso, however, makes nondischargeable any debts resulting from an agreement by the debtor to hold the debtor's spouse harmless on joint debts, to the extent that the agreement is in payment of alimony, maintenance, or support of the spouse, as

determined under bankruptcy law considerations as to whether a particular agreement to pay money to a spouse is actually alimony or a property settlement.Paragraph (7) makes nondischargeable certain liabilities for penalties including tax penalties if the underlying tax with respect to which the penalty was imposed is also nondischargeable (sec. 523(a)(7)). These latter liabilities cover those which, but are penal in nature, as distinct from so-called "pecuniary loss" penalties which, in the case of taxes, involve basically the collection of a tax under the label of a "penalty." This provision differs from the bill as introduced, which did not link the nondischarge of a tax penalty with the treatment of the underlying tax. The amended provision reflects the existing position of the Internal Revenue Service as to tax penalties imposed by the Internal Revenue Code (Rev.Rul. 68-574, 1968-2 C.B. 595).Paragraph (8) follows generally current law and excerpts from discharge student loans until such loans have been due and owing for five years. Such loans include direct student loans as well as insured and guaranteed loans. This provision is intended to be self-executing and the lender or institution is not required to file a complaint to determine the nondischargeability of any student loan.Paragraph (9) excepts from discharge debts that the debtor owed before a previous bankruptcy case concerning the debtor in which the debtor was denied a discharge other than on the basis of the six-year bar.Subsection (b) of this section permits discharge in a bankruptcy case of an unscheduled debt from a prior case. This provision is carried over from Bankruptcy Act §17b [section 35(b) of former title 11]. The result dictated by the subsection would probably not be different if the subsection were not included. It is included nevertheless for clarity.Subsection (c) requires a creditor who is owed a debt that may be excepted from discharge under paragraph (2), (4), or (5), (false statements, defalcation or larceny misappropriation, or willful and malicious injury) to initiate proceedings in the bankruptcy court for an exception to discharge. If the creditor does not act, the debt is discharged. This provision does not change current law.Subsection (d) is new. It provides protection to a consumer debtor that dealt honestly with a creditor who sought to have a debt excepted from discharge on the ground of falsity in the incurring of the debt. The debtor may be awarded costs and a reasonable attorney's fee for the proceeding to determine the dischargeability of a debt under subsection (a)(2), if the court finds that the proceeding was frivolous or not brought by its creditor in good faith.The purpose of the provision is to discourage creditors from initiating proceedings to obtaining a false financial statement exception to discharge in the hope of obtaining a settlement from an honest debtor anxious to save attorney's fees. Such practices impair the debtor's fresh start and are contrary to the spirit of the bankruptcy laws.

HOUSE REPORT NO. 95-595*Subsection (a) lists eight kinds of debts excepted from discharge. Taxes that are entitled to priority are excepted from discharge under paragraph (1). In addition, taxes with respect to which the debtor made a fraudulent return or willfully attempted to evade or defeat, or with respect to which a return (if required) was not filed or was not filed after the due date and after one year before the bankruptcy case are excepted from discharge. If the taxing authority's claim has been disallowed, then it would be barred by the more modern rules of collateral estoppel from reasserting that claim against the debtor after the case was closed. See Plumb, The Tax Recommendations of the Commission on the Bankruptcy Laws: Tax Procedures, 88 Harv.L.Rev. 1360, 1388 (1975).As under Bankruptcy Act §17a(2) [section 35(a)(2) of former title 11], debt for obtaining money, property, services, or an extension or renewal of credit by false pretenses, a false representation, or actual fraud, or by use of a statement in writing respecting the debtor's financial condition that is materially false, on which the creditor reasonably relied, and that the debtor made or published with intent to deceive, is excepted from discharge. This provision is modified only slightly from current section 17a(2). First, "actual fraud" is added as a grounds for exception from discharge. Second, the creditor must not only have relied on a false statement in writing, the reliance must have been reasonable. This codifies case law construing this provision. Third, the phrase "in any manner whatsoever" that appears in current law after "made or published" is deleted as unnecessary. The word "published" is used in the same sense that it is used in slander actions.Unscheduled debts*

are excepted from discharge under paragraph (3). The provision, derived from section 17a(3) [section 35(a)(3) of former title 11], follows current law, but clarifies some uncertainties generated by the case law construing 17a(3). The debt is excepted from discharge if it was not scheduled in time to permit timely action by the creditor to protect his rights, unless the creditor had notice or actual knowledge of the case.Paragraph (4) excepts debts for embezzlement or larceny. The deletion of willful and malicious conversion from §17a(2) of the Bankruptcy Act [section 35(a)(2) of former title 11] is not intended to effect a substantive change. The intent is to include in the category of non-dischargeable debts a conversion under which the debtor willfully and maliciously intends to borrow property for a short period of time with no intent to inflict injury but on which injury is in fact inflicted.Paragraph (5) excepts from discharge debts to a spouse, former spouse, or child of the debtor for alimony to, maintenance for, or support of, the spouse or child. This language, in combination with the repeal of section 456(b) of the Social Security Act (42 U.S.C. 656(b)) by section 327 of the bill, will apply to make nondischargeable only alimony, maintenance, or support owed directly to a spouse or dependent. See Hearings, pt. 2, at 942. What constitutes alimony, maintenance, or support, will be determined under the bankruptcy laws, not State law. Thus, cases such as In re Waller, 494 F.2d 447 (6th Cir. 1974); Hearings, pt. 3, at 1308-10, are overruled, and the result in cases such as Fife v. Fife, 1 Utah 2d 281, 265 P.2d 642 (1952) is followed. This provision will, however, make nondischargeable any debts resulting from an agreement by the debtor to hold the debtor's spouse harmless on joint debts, to the extent that the agreement is in payment of alimony, maintenance, or support of the spouse, as determined under bankruptcy law considerations that are similar to considerations of whether a particular agreement to pay money to a spouse is actually alimony or a property settlement. See Hearings, pt. 3, at 1287-1290.Paragraph (6) excepts debts for willful and malicious injury by the debtor to another person or to the property of another person. Under this paragraph, "willful" means deliberate or intentional. To the extent that Tinker v. Colwell, 193 U.S. 473 (1902) [24 S.Ct. 505, 48 L.Ed. 754, 11 Am.Bankr.Rep. 568], held that a looser standard is intended, and to the extent that other cases have relied on Tinker to apply a "reckless disregard" standard, they are overruled.Paragraph (7) excepts from discharge a debt for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, that is not compensation for actual pecuniary loss.Paragraph (8) [enacted as (9)] excepts from discharge debts that the debtor owed before a previous bankruptcy case concerning the debtor in which the debtor was denied a discharge other than on the basis of the six-year bar.Subsection (d) is new. It provides protection to a consumer debtor that dealt honestly with a creditor who sought to have a debt excepted from discharge on grounds of falsity in the incurring of the debt. The debtor is entitled to costs of and a reasonable attorney's fee for the proceeding to determine the dischargeability of a debt under subsection (a)(2), if the creditor initiated the proceeding and the debt was determined to be dischargeable. The court is permitted to award any actual pecuniary loss that the debtor may have suffered as a result of the proceeding (such as loss of a day's pay). The purpose of the provision is to discourage creditors from initiating false financial statement exception to discharge actions in the hopes of obtaining a settlement from an honest debtor anxious to save attorney's fees. Such practices impair the debtor's fresh start.

EDITORIAL NOTES

REFERENCES IN TEXT*The Internal Revenue Code of 1986, referred to in subsec. (a), is classified generally to Title 26, Internal Revenue Code.Section 103 of the Truth in Lending Act, referred to in subsec. (a)(2)(C)(ii)(I), is classified to section 1602 of Title 15, Commerce and Trade.The Bankruptcy Act, referred to in subsecs. (a)(10) and (b), is act July 1, 1898, ch. 541, 30 Stat. 544, as amended, which was classified generally to former Title 11. Sections 14c and 17a of the Bankruptcy Act were classified to sections 32(c) and 35(a) of former Title 11.Section 408(b)(1) of the Employee Retirement Income Security Act of 1974, referred to in subsec. (a)(18)(A), is classified to section 1108(b)(1) of Title 29, Labor.Section 3(a)(47) of the Securities Exchange Act of 1934, referred to in*

subsec. (a)(19)(A)(i), is classified to section 78c(a)(47) of Title 15, Commerce and Trade.Section 439A of the Higher Education Act of 1965, referred to in subsec. (b), was classified to section 1087-3 of Title 20, Education, and was repealed by Pub. L. 95-598, title III, §317, Nov. 6, 1978, 92 Stat. 2678.Section 733(g) of the Public Health Service Act, referred to in subsec. (b), was repealed by Pub. L. 95-598, title III, §327, Nov. 6, 1978, 92 Stat. 2679. A subsec. (g), containing similar provisions, was added to section 733 by Pub. L. 97-35, title XXVII, §2730, Aug. 13, 1981, 95 Stat. 919. Section 733 was subsequently omitted in the general revision of subchapter V of chapter 6A of Title 42, The Public Health and Welfare, by Pub. L. 102-408, title I, §102, Oct. 13, 1992, 106 Stat. 1994. See section 292f(g) of Title 42.

***AMENDMENTS2019**-Subsec. (a). Pub. L. 116-54 inserted "1192" after "1141," in introductory provisions.**2010**-Subsec. (a)(2)(C)(ii)(II). Pub. L. 111-327, §2(a)(18)(A), substituted semicolon for period at end.Subsec. (a)(3). Pub. L. 111-327, §2(a)(18)(B), substituted "521(a)(1)" for "521(1)" in introductory provisions.**2005**- Pub. L. 109-8, §1209(1), transferred par. (15) and inserted it after subsec. (a)(14A). See 1994 Amendments note below. Pub. L. 109-8, §215(3), in par. (15), inserted "to a spouse, former spouse, or child of the debtor and" before "not of the kind" and "or" after "court of record," and substituted a semicolon for "unless-"(A) the debtor does not have the ability to pay such debt from income or property of the debtor not reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor and, if the debtor is engaged in a business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business; or"(B) discharging such debt would result in a benefit to the debtor that outweighs the detrimental consequences to a spouse, former spouse, or child of the debtor;".Subsec. (a). Pub. L. 109-8, §714(2), inserted at end "For purposes of this subsection, the term 'return' means a return that satisfies the requirements of applicable nonbankruptcy law (including applicable filing requirements). Such term includes a return prepared pursuant to section 6020(a) of the Internal Revenue Code of 1986, or similar State or local law, or a written stipulation to a judgment or a final order entered by a nonbankruptcy tribunal, but does not include a return made pursuant to section 6020(b) of the Internal Revenue Code of 1986, or a similar State or local law."Subsec. (a)(1)(A). Pub. L. 109-8, §1502(a)(2), substituted "507(a)(3)" for "507(a)(2)".Subsec. (a)(1)(B). Pub. L. 109-8, §714(1)(A), inserted "or equivalent report or notice," after "a return," in introductory provisions.Subsec. (a)(1)(B)(i). Pub. L. 109-8, §714(1)(B), inserted "or given" after "filed".Subsec. (a)(1)(B)(ii). Pub. L. 109-8, §714(1)(C), inserted "or given" after "filed" and ", report, or notice" after "return".Subsec. (a)(2)(C). Pub. L. 109-8, §310, amended subpar. (C) generally. Prior to amendment, subpar. (C) read as follows: "for purposes of subparagraph (A) of this paragraph, consumer debts owed to a single creditor and aggregating more than $1,000 for 'luxury goods or services' incurred by an individual debtor on or within 60 days before the order for relief under this title, or cash advances aggregating more than $1,000 that are extensions of consumer credit under an open end credit plan obtained by an individual debtor on or within 60 days before the order for relief under this title, are presumed to be nondischargeable; 'luxury goods or services' do not include goods or services reasonably acquired for the support or maintenance of the debtor or a dependent of the debtor; an extension of consumer credit under an open end credit plan is to be defined for purposes of this subparagraph as it is defined in the Consumer Credit Protection Act;".Subsec. (a)(5). Pub. L. 109-8, §215(1)(A), added par. (5) and struck out former par. (5) which read as follows: "to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for, or support of such spouse or child, in connection with a separation agreement, divorce decree or other order of a court of record, determination made in accordance with State or territorial law by a governmental unit, or property settlement agreement, but not to the extent that-"(A) such debt is assigned to another entity, voluntarily, by operation of law, or otherwise (other than debts assigned pursuant to section 408(a)(3) of the Social Security Act, or any such debt which has been assigned to the Federal Government or to a State or any political subdivision of such State); or"(B) such debt includes a liability designated as alimony, maintenance, or support, unless such liability is actually in the nature*

*of alimony, maintenance, or support;"Subsec. (a)(8). Pub. L. 109-8, §220, added par. (8) and struck out former par. (8) which read as follows: "for an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution, or for an obligation to repay funds received as an educational benefit, scholarship or stipend, unless excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents;".Subsec. (a)(9). Pub. L. 109-8, §1209(2), substituted "motor vehicle, vessel, or aircraft" for "motor vehicle".Subsec. (a)(14A). Pub. L. 109-8, §314(a), added par. (14A).Subsec. (a)(14B). Pub. L. 109-8, §1235, added par. (14B).Subsec. (a)(16). Pub. L. 109-8, §412, struck out "dwelling" after "debtor's interest in a" and "housing" after "share of a cooperative" and substituted "ownership," for "ownership or" and "or a lot in a homeowners association, for as long as the debtor or the trustee has a legal, equitable, or possessory ownership interest in such unit, such corporation, or such lot," for "but only if such fee or assessment is payable for a period during which-"(A) the debtor physically occupied a dwelling unit in the condominium or cooperative project; or" (B) the debtor rented the dwelling unit to a tenant and received payments from the tenant for such period,".Subsec. (a)(17). Pub. L. 109-8, §301, substituted "on a prisoner by any court" for "by a court" and "subsection (b) or (f)(2) of section 1915" for "section 1915(b) or (f)" and inserted "(or a similar non-Federal law)" after "title 28" in two places.Subsec. (a)(18). Pub. L. 109-8, §224(c), added par. (18). Pub. L. 109-8, §215(1)(B), struck out par. (18) which read as follows: "owed under State law to a State or municipality that is-" (A) in the nature of support, and"(B) enforceable under part D of title IV of the Social Security Act (42 U.S.C. 601 et seq.); or".Subsec. (a)(19)(B). Pub. L. 109-8, §1404(a), inserted ", before, on, or after the date on which the petition was filed," after "results" in introductory provisions.Subsec. (c)(1). Pub. L. 109-8, §215(2), substituted "or (6)" for "(6), or (15)" in two places.Subsec. (e). Pub. L. 109-8, §1209(3), substituted "an insured" for "a insured".**2002**-Subsec. (a)(19). Pub. L. 107-204 added par. (19).**1998**-Subsec. (a)(8). Pub. L. 105-244 substituted "stipend, unless" for "stipend, unless-" and struck out "(B)" before "excepting such debt" and subpar. (A) which read as follows: "such loan, benefit, scholarship, or stipend overpayment first became due more than 7 years (exclusive of any applicable suspension of the repayment period) before the date of the filing of the petition; or".**1996**-Subsec. (a)(5)(A). Pub. L. 104-193, §374(a)(4), substituted "section 408(a)(3)" for "section 402(a)(26)".Subsec. (a)(17). Pub. L. 104-134 added par. (17).Subsec. (a)(18). Pub. L. 104-193, §374(a)(1)-(3), added par. (18).**1994**-Par. (15). Pub. L. 103-394, §304(e) [(1)], amended this section by adding par. (15) at the end. See 2005 Amendment note above.Subsec. (a). Pub. L. 103-394, §501(d)(13)(A)(i), substituted "1141," for "1141,," in introductory provisions.Subsec. (a)(1)(A). Pub. L. 103-394, §304(h)(3), substituted "507(a)(8)" for "507(a)(7)".Subsec. (a)(2)(C). Pub. L. 103-394, §§306, 501, substituted "$1,000 for" for "$500 for", "60" for "forty" after "incurred by an individual debtor on or within", and "60" for "twenty" after "obtained by an individual debtor on or within", and struck out "(15 U.S.C. 1601 et seq.)" after "Protection Act".Subsec. (a)(11). Pub. L. 103-322, §320934(1), struck out "or" after semicolon at end.Subsec. (a)(12). Pub. L. 103-322, §320934(2), which directed the substitution of "; or" for a period at end of par. (12), could not be executed because a period did not appear at end.Subsec. (a)(13). Pub. L. 103-394, §221(1), substituted semicolon for period at end. Pub. L. 103-322, §320934(3), added par. (13).Subsec. (a)(14). Pub. L. 103-394, §221(2), added par. (14).Subsec. (a)(16). Pub. L. 103-394, §309, added par. (16).Subsec. (b). Pub. L. 103-394, §501(d)(13)(B), struck out "(20 U.S.C. 1087-3)" after "Act of 1965" and "(42 U.S.C. 294f)" after "Service Act".Subsec. (c)(1). Pub. L. 103-394, §304(e)(2), substituted "(6), or (15)" for "or (6)" in two places.Subsec. (e). Pub. L. 103-394, §501(d)(13)(C), substituted "insured depository institution" for "depository institution or insured credit union".**1990**-Subsec. (a)(8). Pub. L. 101-647, §3621, substituted "for an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution, or for an obligation to repay funds received as an educational benefit, scholarship or stipend, unless" for "for an educational loan made, insured, or guaranteed by a governmental unit, or made under any program*

*funded in whole or in part by a governmental unit or a nonprofit institution, unless" in introductory provisions and amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: "such loan first became due before five years (exclusive of any applicable suspension of the repayment period) before the date of the filing of the petition; or".Subsec. (a)(9). Pub. L. 101-581 and Pub. L. 101-647, §3102(a), identically amended par. (9) generally. Prior to amendment, par. (9) read as follows: "to any entity, to the extent that such debt arises from a judgment or consent decree entered in a court of record against the debtor wherein liability was incurred by such debtor as a result of the debtor's operation of a motor vehicle while legally intoxicated under the laws or regulations of any jurisdiction within the United States or its territories wherein such motor vehicle was operated and within which such liability was incurred; or".Subsec. (a)(11), (12). Pub. L. 101-647, §2522(a)(1), added pars. (11) and (12).Subsec. (c). Pub. L. 101-647, §2522(a)(3), designated existing provisions as par. (1) and added par. (2).Subsec. (e). Pub. L. 101-647, §2522(a)(2), added subsec. (e).**1986**-Subsec. (a). Pub. L. 99-554, §257(n), inserted reference to sections 1228(a) and 1228(b) of this title.Subsec. (a)(1)(A). Pub. L. 99-554, §283(j)(1)(A), substituted "507(a)(7)" for "507(a)(6)".Subsec. (a)(5). Pub. L. 99-554, §281, struck out the comma after "decree" and inserted ", determination made in accordance with State or territorial law by a governmental unit," after "record".Subsec. (a)(9), (10). Pub. L. 99-554, §283(j)(1)(B), redesignated par. (9) relating to debts incurred by persons driving while intoxicated, added by Pub. L. 98-353 as (10).Subsec. (b). Pub. L. 99-554, §283(j)(2), substituted "Service" for "Services".**1984**-Subsec. (a)(2). Pub. L. 98-353, §454(a)(1), in provisions preceding subpar. (A), struck out "obtaining" after "for", and substituted "refinancing of credit, to the extent obtained" for "refinance of credit,".Subsec. (a)(2)(A). Pub. L. 98-353, §307(a)(1), struck out "or" at end.Subsec. (a)(2)(B). Pub. L. 98-353, §307(a)(2), inserted "or" at end.Subsec. (a)(2)(B)(iii). Pub. L. 98-353, §454(a)(1)(A), struck out "obtaining" before "such".Subsec. (a)(2)(C). Pub. L. 98-353, §307(a)(3), added subpar. (C).Subsec. (a)(5). Pub. L. 98-353, §454(b)(1), inserted "or other order of a court of record" after "divorce decree," in provisions preceding subpar. (A).Subsec. (a)(5)(A). Pub. L. 98-353, §454(b)(2), inserted ", or any such debt which has been assigned to the Federal Government or to a State or any political subdivision of such State".Subsec. (a)(8). Pub. L. 98-353, §§371(1), 454, struck out "of higher education" after "a nonprofit institution of" and struck out "or" at end.Subsec. (a)(9). Pub. L. 98-353, §371(2), added the par. (9) relating to debts incurred by persons driving while intoxicated.Subsec. (c). Pub. L. 98-353, §454(c), inserted "of a kind" after "debt".Subsec. (d). Pub. L. 98-353, §307(b), substituted "the court shall grant judgment in favor of the debtor for the costs of, and a reasonable attorney's fee for, the proceeding if the court finds that the position of the creditor was not substantially justified, except that the court shall not award such costs and fees if special circumstances would make the award unjust" for "the court shall grant judgment against such creditor and in favor of the debtor for the costs of, and a reasonable attorney's fee for, the proceeding to determine dischargeability, unless such granting of judgment would be clearly inequitable".**1981**-Subsec. (a)(5)(A). Pub. L. 97-35 substituted "law, or otherwise (other than debts assigned pursuant to section 402(a)(26) of the Social Security Act);" for "law, or otherwise;".**1979**-Subsec. (a)(8). Pub. L. 96-56 substituted "for an educational loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or a nonprofit institution of higher education" for "to a governmental unit, or a nonprofit institution of higher education, for an educational loan" in the provisions preceding subpar. (A) and inserted "(exclusive of any applicable suspension of the repayment period)" after "before five years" in subpar. (A).*

STATUTORY NOTES AND RELATED SUBSIDIARIES

EFFECTIVE DATE OF 2019 AMENDMENT*Amendment by Pub. L. 116-54 effective 180 days after Aug. 23, 2019, see section 5 of Pub. L. 116-54 set out as a note under section 101 of this title.*

EFFECTIVE DATE OF 2005 AMENDMENT *Pub. L. 109-8, title XIV, §1404(b), Apr. 20, 2005, 119 Stat. 215, provided that: "The amendment made by subsection (a) [amending this section] is effective beginning July 30, 2002."Amendment by sections 215, 220, 224(c), 301, 310, 314(a), 412, 714, 1209, 1235, and 1502(a)(2) of Pub. L. 109-8 effective 180 days after Apr. 20, 2005, and not applicable with respect to cases commenced under this title before such effective date, except as otherwise provided, see section 1501 of Pub. L. 109-8 set out as a note under section 101 of this title.*

EFFECTIVE DATE OF 1998 AMENDMENT *Pub. L. 105-244, title IX, §971(b), Oct. 7, 1998, 112 Stat. 1837, provided that: "The amendment made by subsection (a) [amending this section] shall apply only with respect to cases commenced under title 11, United States Code, after the date of enactment of this Act [Oct. 7, 1998]."*

EFFECTIVE DATE OF 1996 AMENDMENT *Pub. L. 104-193, title III, §374(c), Aug. 22, 1996, 110 Stat. 2256, provided that: "The amendments made by this section [amending this section and section 656 of Title 42, The Public Health and Welfare] shall apply only with respect to cases commenced under title 11 of the United States Code after the date of the enactment of this Act [Aug. 22, 1996]."For provisions relating to effective date of title III of Pub. L. 104-193 see section 395(a)-(c) of Pub. L. 104-193 set out as a note under section 654 of Title 42, The Public Health and Welfare.*

EFFECTIVE DATE OF 1994 AMENDMENT*Amendment by Pub. L. 103-394 effective Oct. 22, 1994, and not applicable with respect to cases commenced under this title before Oct. 22, 1994, see section 702 of Pub. L. 103-394 set out as a note under section 101 of this title.*

EFFECTIVE DATE OF 1990 AMENDMENT *Pub. L. 101-647, title XXXI, §31043104,, 104 Stat. 4916, provided that:"(a) EFFECTIVE DATE.-This title and the amendments made by this title [amending this section and section 1328 of this title and enacting provisions set out as a note under section 101 of this title] shall take effect on the date of the enactment of this Act [Nov. 29, 1990]."(b) APPLICATION OF AMENDMENTS.-The amendments made by this title [amending this section and section 1328 of this title] shall not apply with respect to cases commenced under title 11 of the United States Code before the date of the enactment of this Act."Amendment by section 3621 of Pub. L. 101-647 effective 180 days after Nov. 29, 1990, see section 3631 of Pub. L. 101-647 set out as an Effective Date note under section 3001 of Title 28, Judiciary and Judicial Procedure. Pub. L. 101-581, §4, Nov. 15, 1990, 104 Stat. 2865, provided that:"(a) EFFECTIVE DATE.-This Act and the amendments made by this Act [amending this section and section 1328 of this title and enacting provisions set out as a note under section 101 of this title] shall take effect on the date of the enactment of this Act [Nov. 15, 1990]."(b) APPLICATION OF AMENDMENTS.-The amendments made by this Act [amending this section and section 1328 of this title] shall not apply with respect to cases commenced under title 11 of the United States Code before the date of the enactment of this Act."*

EFFECTIVE DATE OF 1986 AMENDMENT*Amendment by section 257 of Pub. L. 99-554 effective 30 days after Oct. 27, 1986, but not applicable to cases commenced under this title before that date, see section 302(a), (c)(1) of Pub. L. 99-554 set out as a note under section 581 of Title 28, Judiciary and Judicial Procedure.Amendment by sections 281 and 283 of Pub. L. 99-554 effective 30 days after Oct. 27, 1986, see section 302(a) of Pub. L. 99-554.*

EFFECTIVE DATE OF 1984 AMENDMENT*Amendment by Pub. L. 98-353 effective with respect to cases filed 90 days after July 10, 1984, see section 552(a) of Pub. L. 98-353 set out as a note under section 101 of this title.*

EFFECTIVE DATE OF 1981 AMENDMENT*Amendment by Pub. L. 97-35 effective Aug. 13, 1981, see section 2334(c) of Pub. L. 97-35 set out as a note under section 656 of Title 42, The Public Health and Welfare.*

COURT RULES AND JUDICIAL DOCUMENTS

ADJUSTMENT OF DOLLAR AMOUNTS*The dollar amounts specified in this section were adjusted by notices of the Judicial Conference of the United States pursuant to section 104 of this title as follows:By notice dated Feb. 5, 2019, 84 F.R. 3488, effective Apr. 1, 2019, in subsec. (a)(2)(C)(i)(I), dollar amount "675" was adjusted to "725" and, in subsec. (a)(2)(C)(i)(II), dollar amount "950" was adjusted to "1,000". See notice of the Judicial Conference of the United States set out as a note under section 104 of this title.By notice dated Feb. 16, 2016, 81 F.R. 8748, effective Apr. 1, 2016, in subsec. (a)(2)(C)(i)(I), dollar amount "650" was adjusted to "675" and, in subsec. (a)(2)(C)(i)(II), dollar amount "925" was adjusted to "950".By notice dated Feb. 12, 2013, 78 F.R. 12089, effective Apr. 1, 2013, in subsec. (a)(2)(C)(i)(I), dollar amount "600" was adjusted to "650" and, in subsec. (a)(2)(C)(i)(II), dollar amount "875" was adjusted to "925".By notice dated Feb. 19, 2010, 75 F.R. 8747, effective Apr. 1, 2010, in subsec. (a)(2)(C)(i)(I), dollar amount "550" was adjusted to "600" and, in subsec. (a)(2)(C)(i)(II), dollar amount "825" was adjusted to "875".By notice dated Feb. 7, 2007, 72 F.R. 7082, effective Apr. 1, 2007, in subsec. (a)(2)(C)(i)(I), dollar amount "500" was adjusted to "550" and, in subsec. (a)(2)(C)(i)(II), dollar amount "750" was adjusted to "825".[Pub. L. 109-8 amended subsec. (a)(2)(C) generally. See 2005 Amendment note above.]By notice dated Feb. 18, 2004, 69 F.R. 8482, effective Apr. 1, 2004, in subsec. (a)(2)(C), dollar amount "1,150" was adjusted to "1,225" each time it appeared.By notice dated Feb. 13, 2001, 66 F.R. 10910, effective Apr. 1, 2001, in subsec. (a)(2)(C), dollar amount "1,075" was adjusted to "1,150" each time it appeared.By notice dated Feb. 3, 1998, 63 F.R. 7179, effective Apr. 1, 1998, in subsec. (a)(2)(C), dollar amount "1,000" was adjusted to "1,075" each time it appeared.*

11 U.S.C. § 541

Section 541 - Property of the estate

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is-

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date-

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

(b) Property of the estate does not include-

(1) any power that the debtor may exercise solely for the benefit of an entity other than the debtor;

(2) any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease before the commencement of the case under this title, and ceases to include any interest of the debtor as a lessee

under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease during the case;

(3) any eligibility of the debtor to participate in programs authorized under the Higher Education Act of 1965 (20 U.S.C. 1001 et seq.; 42 U.S.C. 2751 et seq.),[1] or any accreditation status or State licensure of the debtor as an educational institution;

(4) any interest of the debtor in liquid or gaseous hydrocarbons to the extent that-

(A)

(i) the debtor has transferred or has agreed to transfer such interest pursuant to a farmout agreement or any written agreement directly related to a farmout agreement; and

(ii) but for the operation of this paragraph, the estate could include the interest referred to in clause (i) only by virtue of section 365 or 544(a)(3) of this title; or

(B)

(i) the debtor has transferred such interest pursuant to a written conveyance of a production payment to an entity that does not participate in the operation of the property from which such production payment is transferred; and

(ii) but for the operation of this paragraph, the estate could include the interest referred to in clause (i) only by virtue of section 365 or 542 of this title;

(5) funds placed in an education individual retirement account (as defined in section 530(b)(1) of the Internal Revenue Code of 1986) not later than 365 days before the date of the filing of the petition in a case under this title, but-

(A) only if the designated beneficiary of such account was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were placed in such account;

(B) only to the extent that such funds-

(i) are not pledged or promised to any entity in connection with any extension of credit; and

(ii) are not excess contributions (as described in section 4973(e) of the Internal Revenue Code of 1986); and

(C) in the case of funds placed in all such accounts having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $5,000; [2]

(6) funds used to purchase a tuition credit or certificate or contributed to an account in accordance with section 529(b)(1)(A) of the Internal Revenue Code of 1986 under a qualified State tuition program (as defined in section 529(b)(1) of such Code) not later than 365 days before the date of the filing of the petition in a case under this title, but-

(A) only if the designated beneficiary of the amounts paid or contributed to such tuition program was a child, stepchild, grandchild, or stepgrandchild of the debtor for the

taxable year for which funds were paid or contributed;

(B) with respect to the aggregate amount paid or contributed to such program having the same designated beneficiary, only so much of such amount as does not exceed the total contributions permitted under section 529(b)(6) of such Code with respect to such beneficiary, as adjusted beginning on the date of the filing of the petition in a case under this title by the annual increase or decrease (rounded to the nearest tenth of 1 percent) in the education expenditure category of the Consumer Price Index prepared by the Department of Labor; and

(C) in the case of funds paid or contributed to such program having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $5,000; [2]

(7) any amount-

(A) withheld by an employer from the wages of employees for payment as contributions-

(i) to-

(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;

(II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or

(III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986;

except that such amount under this subparagraph shall not constitute disposable income as defined in section 1325(b)(2); or

(ii) to a health insurance plan regulated by State law whether or not subject to such title; or

(B) received by an employer from employees for payment as contributions-

(i) to-

(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;

(II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or

(III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986;

except that such amount under this subparagraph shall not constitute disposable income, as defined in section 1325(b)(2); or

(ii) to a health insurance plan regulated by State law whether or not subject to such title;

(8) subject to subchapter III of chapter 5, any interest of the debtor in property where the debtor pledged or sold tangible personal property (other than securities or written or printed evidences of indebtedness or title) as collateral for a loan or advance of money given by a person licensed under law to make such loans or advances, where-

(A) the tangible personal property is in the possession of the pledgee or transferee;

(B) the debtor has no obligation to repay the money, redeem the collateral, or buy back the property at a stipulated price; and

(C) neither the debtor nor the trustee have exercised any right to redeem provided under the contract or State law, in a timely manner as provided under State law and section 108(b);

(9) any interest in cash or cash equivalents that constitute proceeds of a sale by the debtor of a money order that is made-

(A) on or after the date that is 14 days prior to the date on which the petition is filed; and

(B) under an agreement with a money order issuer that prohibits the commingling of such proceeds with property of the debtor (notwithstanding that, contrary to the agreement, the proceeds may have been commingled with property of the debtor), unless the money order issuer had not taken action, prior to the filing of the petition, to require compliance with the prohibition; or

(10) funds placed in an account of a qualified ABLE program (as defined in section 529A(b) of the Internal Revenue Code of 1986) not later than 365 days before the date of the filing of the petition in a case under this title, but-

(A) only if the designated beneficiary of such account was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were placed in such account;

(B) only to the extent that such funds-

(i) are not pledged or promised to any entity in connection with any extension of credit; and

(ii) are not excess contributions (as described in section 4973(h) of the Internal Revenue Code of 1986); and

(C) in the case of funds placed in all such accounts having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $6,225.[2]

Paragraph (4) shall not be construed to exclude from the estate any consideration the debtor retains, receives, or is entitled to receive for transferring an interest in liquid or gaseous hydrocarbons pursuant to a farmout agreement.

(c)

(1) Except as provided in paragraph (2) of this subsection, an interest of the debtor in property becomes property of the estate under subsection (a)(1), (a)(2), or (a)(5) of this section notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law-

(A) that restricts or conditions transfer of such interest by the debtor; or

(B) that is conditioned on the insolvency or financial condition of the debtor, on the commencement of a case under this title, or on the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement, and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property.

(2) A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.

(d) Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such a mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

(e) In determining whether any of the relationships specified in paragraph (5)(A) or (6)(A) of subsection (b) exists, a legally adopted child of an individual (and a child who is a member of an individual's household, if placed with such individual by an authorized placement agency for legal adoption by such individual), or a foster child of an individual (if such child has as the child's principal place of abode the home of the debtor and is a member of the debtor's household) shall be treated as a child of such individual by blood.

(f) Notwithstanding any other provision of this title, property that is held by a debtor that is a corporation described in section 501(c)(3) of the Internal Revenue Code of 1986 and exempt from tax under section 501(a) of such Code may be transferred to an entity that is not such a corporation, but only under the same conditions as would apply if the debtor had not filed a case under this title.

[1] See References in Text note below.

[2] See Adjustment of Dollar Amounts notes below.

11 U.S.C. § 541

Pub. L. 95-598, Nov. 6, 1978, 92 Stat. 2594; Pub. L. 98-353, title III, §§363(a), 456, July 10, 1984, 98 Stat. 363, 376; Pub. L. 101-508, title III, §3007(a)(2), Nov. 5, 1990, 104 Stat. 1388-28; Pub. L. 102-486, title XXX, §3017(b), Oct. 24, 1992, 106 Stat. 3130; Pub. L. 103-394, title II, §§208(b), Oct. 22, 1994, 223, Oct. 22, 1994, 108 Stat. 4124, 4129; Pub. L. 109-8, title II, §225(a), title III, §323, title XII, §§1212, 1221(c), 1230, Apr. 20, 2005, 119 Stat. 65, 97, 194, 196, 201; Pub. L. 111-327, §2(a)(22), Dec. 22, 2010, 124 Stat. 3560; Pub. L. 113-295, div. B, title I, §104(a), Dec. 19, 2014, 128 Stat. 4063.

HISTORICAL AND REVISION NOTES

LEGISLATIVE STATEMENTS*Section 541(a)(7) is new. The provision clarifies that any interest in property that the estate acquires after the commencement of the case is property of the estate; for example, if the estate enters into a contract, after the commencement of the case, such a contract would be property of the estate. The addition of this provision by the House amendment merely clarifies that section 541(a) is an all-embracing definition which includes charges on property, such as liens held by the debtor on property of a third party, or beneficial rights and interests that the debtor may have in property of another. However, only the debtor's interest in such property becomes property of the estate. If the debtor holds bare legal title or holds property in trust for another, only those rights which the debtor would have otherwise had emanating from such interest pass to the estate under section 541. Neither this section nor section 545 will affect various statutory provisions that give a creditor a lien that is valid both inside and outside bankruptcy against a bona fide purchaser of property from the debtor, or that creates a trust fund for the benefit of creditors meeting similar criteria. See Packers and Stockyards Act §206, 7 U.S.C. 196 (1976).Section 541(c)(2) follows the position taken in the House bill and rejects the position taken in the Senate amendment with respect to income limitations on a spend-thrift trust.Section 541(d) of the House amendment is derived from section 541(e) of the Senate amendment and reiterates the general principle that where the debtor holds bare legal title without any equitable interest, that the estate acquires bare legal title without any equitable interest in the property. The purpose of section 541(d) as applied to the secondary mortgage market is identical to the purpose of section 541(e) of the Senate amendment and section 541(d) will accomplish the same result as would have been accomplished by section 541(e). Even if a mortgage seller retains for purposes of servicing legal title to mortgages or interests in mortgages sold in the secondary mortgage market, the trustee would be required by section 541(d) to turn over the mortgages or interests in mortgages to the purchaser of those mortgages.The seller of mortgages in the secondary mortgage market will often retain the original mortgage notes and related documents and the seller will not endorse the notes to reflect the sale to the purchaser. Similarly, the purchaser will often not record the purchaser's ownership of the mortgages or interests in mortgages under State recording statutes. These facts are irrelevant and the seller's retention of the mortgage documents and the purchaser's decision not to record do not change the trustee's obligation to turn the mortgages or interests in mortgages over to the purchaser. The application of section 541(d) to secondary mortgage market transactions will not be affected by the terms of the servicing agreement between the mortgage servicer and the purchaser of the mortgages. Under section 541(d), the trustee is required to recognize the purchaser's title to the mortgages or interests in mortgages and to turn this property over to the purchaser. It makes no difference whether the servicer and the purchaser characterize their relationship as one of trust, agency, or independent contractor.The purpose of section 541(d) as applied to the secondary mortgage market is therefore to make certain that secondary mortgage market sales as they are currently structured are not subject to challenge by bankruptcy trustees and that purchasers of mortgages will be able to obtain the mortgages or interests in mortgages which they have purchased from trustees without the trustees asserting that a sale of mortgages is a loan from the purchaser to the seller.Thus, as section 541(a)(1) clearly states, the estate is comprised of all legal or equitable interests of the debtor in property as of the commencement of the case. To the extent such an interest is limited in the hands of the debtor, it is equally limited in the hands of the estate except to the extent that defenses which are personal against the debtor are not effective against the estate.Property of the estate: The Senate amendment provided that property of the estate does not include amounts held by the debtor as trustee and any taxes withheld or collected from others before the commencement of the case. The House amendment removes these two provisions. As to property held by the debtor as a trustee, the House amendment provides that property of the estate will include whatever interest the debtor held in the property at the commencement of the case. Thus, where the debtor held only legal title to the property and the beneficial interest in that property belongs to*

another, such as exists in the case of property held in trust, the property of the estate includes the legal title, but not the beneficial interest in the property.As to withheld taxes, the House amendment deletes the rule in the Senate bill as unnecessary since property of the estate does not include the beneficial interest in property held by the debtor as a trustee. Under the Internal Revenue Code of 1954 (section 7501) [26 U.S.C. 7501], the amounts of withheld taxes are held to be a special fund in trust for the United States. Where the Internal Revenue Service can demonstrate that the amounts of taxes withheld are still in the possession of the debtor at the commencement of the case, then if a trust is created, those amounts are not property of the estate. Compare In re Shakesteers Coffee Shops, 546 F.2d 821 (9th Cir. 1976) with In re Glynn Wholesale Building Materials, Inc. (S.D. Ga. 1978) and In re Progress Tech Colleges, Inc., 42 Aftr 2d 78-5573 (S.D. Ohio 1977).Where it is not possible for the Internal Revenue Service to demonstrate that the amounts of taxes withheld are still in the possession of the debtor at the commencement of the case, present law generally includes amounts of withheld taxes as property of the estate. See, e.g., United States v. Randall, 401 U.S. 513 (1973) [91 S. Ct. 991, 28 L.Ed.2d 273] and In re Tamasha Town and Country Club, 483 F.2d 1377 (9th Cir. 1973). Nonetheless, a serious problem exists where "trust fund taxes" withheld from others are held to be property of the estate where the withheld amounts are commingled with other assets of the debtor. The courts should permit the use of reasonable assumptions under which the Internal Revenue Service, and other tax authorities, can demonstrate that amounts of withheld taxes are still in the possession of the debtor at the commencement of the case. For example, where the debtor had commingled that amount of withheld taxes in his general checking account, it might be reasonable to assume that any remaining amounts in that account on the commencement of the case are the withheld taxes. In addition, Congress may consider future amendments to the Internal Revenue Code [title 26] making clear that amounts of withheld taxes are held by the debtor in a trust relationship and, consequently, that such amounts are not property of the estate.

SENATE REPORT NO. 95-989*This section defines property of the estate, and specifies what property becomes property of the estate. The commencement of a bankruptcy case creates an estate. Under paragraph (1) of subsection (a), the estate is comprised of all legal or equitable interest of the debtor in property, wherever located, as of the commencement of the case. The scope of this paragraph is broad. It includes all kinds of property, including tangible or intangible property, causes of action (see Bankruptcy Act §70a(6) [section 110(a)(6) of former title 11]), and all other forms of property currently specified in section 70a of the Bankruptcy Act §70a [section 110(a) of former title 11], as well as property recovered by the trustee under section 542 of proposed title 11, if the property recovered was merely out of the possession of the debtor, yet remained "property of the debtor." The debtor's interest in property also includes "title" to property, which is an interest, just as are a possessory interest, or lease-hold interest, for example. The result of Segal v. Rochelle, 382 U.S. 375 (1966), is followed, and the right to a refund is property of the estate.Though this paragraph will include choses in action and claims by the debtor against others, it is not intended to expand the debtor's rights against others more than they exist at the commencement of the case. For example, if the debtor has a claim that is barred at the time of the commencement of the case by the statute of limitations, then the trustee would not be able to pursue that claim, because he too would be barred. He could take no greater rights than the debtor himself had. But see proposed 11 U.S.C. 108, which would permit the trustee a tolling of the statute of limitations if it had not run before the date of the filing of the petition.Paragraph (1) has the effect of overruling Lockwood v. Exchange Bank, 190 U.S. 294 (1903), because it includes as property of the estate all property of the debtor, even that needed for a fresh start. After the property comes into the estate, then the debtor is permitted to exempt it under proposed 11 U.S.C. 522, and the court will have jurisdiction to determine what property may be exempted and what remains as property of the estate. The broad jurisdictional grant in proposed 28 U.S.C. 1334 would have the effect of overruling Lockwood independently of the change made by this provision.Paragraph (1) also has the effect of overruling Lines v. Frederick, 400 U.S. 18 (1970).Situations occasionally arise where property ostensibly belonging to the*

debtor will actually not be property of the debtor, but will be held in trust for another. For example, if the debtor has incurred medical bills that were covered by insurance, and the insurance company had sent the payment of the bills to the debtor before the debtor had paid the bill for which the payment was reimbursement, the payment would actually be held in a constructive trust for the person to whom the bill was owed. This section and proposed 11 U.S.C. 545 also will not affect various statutory provisions that give a creditor of the debtor a lien that is valid outside as well as inside bankruptcy, or that creates a trust fund for the benefit of a creditor of the debtor. See Packers and Stockyards Act §206, 7 U.S.C. 196.Bankruptcy Act §8 [section 26 of former title 11] has been deleted as unnecessary. Once the estate is created, no interests in property of the estate remain in the debtor. Consequently, if the debtor dies during the case, only property exempted from property of the estate or acquired by the debtor after the commencement of the case and not included as property of the estate will be available to the representative of the debtor's probate estate. The bankruptcy proceeding will continue in rem with respect to property of the state, and the discharge will apply in personam to relieve the debtor, and thus his probate representative, of liability for dischargeable debts.The estate also includes the interests of the debtor and the debtor's spouse in community property, subject to certain limitations; property that the trustee recovers under the avoiding powers; property that the debtor acquires by bequest, devise, inheritance, a property settlement agreement with the debtor's spouse, or as the beneficiary of a life insurance policy within 180 days after the petition; and proceeds, product, offspring, rents, and profits of or from property of the estate, except such as are earning from services performed by an individual debtor after the commencement of the case. Proceeds here is not used in a confining sense, as defined in the Uniform Commercial Code, but is intended to be a broad term to encompass all proceeds of property of the estate. The conversion in form of property of the estate does not change its character as property of the estate.Subsection (b) excludes from property of the estate any power, such as a power of appointment, that the debtor may exercise solely for the benefit of an entity other than the debtor. This changes present law which excludes powers solely benefiting other persons but not other entities.Subsection (c) invalidates restrictions on the transfer of property of the debtor, in order that all of the interests of the debtor in property will become property of the estate. The provisions invalidated are those that restrict or condition transfer of the debtor's interest, and those that are conditioned on the insolvency or financial condition of the debtor, on the commencement of a bankruptcy case, or on the appointment of a custodian of the debtor's property. Paragraph (2) of subsection (c), however, preserves restrictions on a transfer of a spendthrift trust that the restriction is enforceable nonbankruptcy law to the extent of the income reasonably necessary for the support of a debtor and his dependents.Subsection (d) [enacted as (e)], derived from section 70c of the Bankruptcy Act [section 110(c) of former title 11], gives the estate the benefit of all defenses available to the debtor as against an entity other than the estate, including such defenses as statutes of limitations, statutes of frauds, usury, and other personal defenses, and makes waiver by the debtor after the commencement of the case ineffective to bind the estate.Section 541(e) [enacted as (d)] confirms the current status under the Bankruptcy Act [former title 11] of bona fide secondary mortgage market transactions as the purchase and sale of assets. Mortgages or interests in mortgages sold in the secondary market should not be considered as part of the debtor's estate. To permit the efficient servicing of mortgages or interests in mortgages the seller often retains the original mortgage notes and related documents, and the purchaser records under State recording statutes the purchaser's ownership of the mortgages or interests in mortgages purchased. Section 541(e) makes clear that the seller's retention of the mortgage documents and the purchaser's decision not to record do not impair the asset sale character of secondary mortgage market transactions. The committee notes that in secondary mortgage market transactions the parties may characterize their relationship as one of trust, agency, or independent contractor. The characterization adopted by the parties should not affect the statutes in bankruptcy on bona fide secondary mortgage market purchases and sales.

REFERENCES IN TEXT*The Higher Education Act of 1965, referred to in subsec. (b)(3), is Pub. L. 89-329, Nov. 8, 1965, 79 Stat. 1219, which is classified generally to chapter 28 (§1001 et seq.) of Title 20, Education. Part C of title IV of the Act was formerly classified to part C (§2751 et seq.) of subchapter I of chapter 34 of Title 42, The Public Health and Welfare, prior to transfer to part C (§1087-51 et seq.) of subchapter IV of chapter 28 of Title 20. For complete classification of this Act to the Code, see Short Title note set out under section 1001 of Title 20 and Tables.The Internal Revenue Code of 1986, referred to in subsecs. (b)(5) to (7), (10) and (f), is classified generally to Title 26, Internal Revenue Code.The Employee Retirement Income Security Act of 1974, referred to in subsec. (b)(7)(A)(i)(I), (B)(i)(I), is Pub. L. 93-406, Sept. 2, 1974, 88 Stat. 829, as amended. Title I of the Act is classified generally to subchapter I (§1001 et seq.) of chapter 18 of Title 29, Labor. For complete classification of this Act to the Code, see Short Title note set out under section 1001 of Title 29 and Tables.*

AMENDMENTS2014*-Subsec. (b)(10). Pub. L. 113-295 added par. (10).****2010****-Subsec. (b)(6)(B). Pub. L. 111-327 substituted "section 529(b)(6)" for "section 529(b)(7)".****2005****-Subsec. (b)(4). Pub. L. 109-8, §225(a)(1)(A), struck out "or" at end.Subsec. (b)(4)(B)(ii). Pub. L. 109-8, §1212, inserted "365 or" before "542".Subsec. (b)(5), (6). Pub. L. 109-8, §225(a)(1)(C), added pars. (5) and (6). Former par. (5) redesignated (9).Subsec. (b)(7). Pub. L. 109-8, §323, added par. (7).Subsec. (b)(8). Pub. L. 109-8, §1230, added par. (8).Subsec. (b)(9). Pub. L. 109-8, §225(a)(1)(B), redesignated par. (5) as (9).Subsec. (e). Pub. L. 109-8, §225(a)(2), added subsec. (e).Subsec. (f). Pub. L. 109-8, §1221(c), added subsec. (f).****1994****-Subsec. (b)(4). Pub. L. 103-394, §208(b), designated existing provisions of subpar. (A) as cl. (i) of subpar. (A), redesignated subpar. (B) as cl. (ii) of subpar. (A), substituted "the interest referred to in clause (i)" for "such interest", substituted "; or" for period at end of cl. (ii), and added subpar. (B). Pub. L. 103-394, §223(2), which directed the amendment of subsec. (b)(4) by striking out period at end and inserting "; or", was executed by inserting "or" after semicolon at end of subsec. (b)(4)(B)(ii), as added by Pub. L. 103-394, §208(b)(3), to reflect the probable intent of Congress.Subsec. (b)(5). Pub. L. 103-394, §223, added par. (5).****1992****-Subsec. (b). Pub. L. 102-486 added par. (4) and closing provisions.****1990****-Subsec. (b)(3). Pub. L. 101-508 added par. (3).****1984****-Subsec. (a). Pub. L. 98-353, §456(a)(1), (2), struck out "under" after "under" and inserted "and by whomever held" after "located".Subsec. (a)(3). Pub. L. 98-353, §456(a)(3), inserted "329(b), 363(n),".Subsec. (a)(5). Pub. L. 98-353, §456(a)(4), substituted "Any" for "An".Subsec. (a)(6). Pub. L. 98-353, §456(a)(5), substituted "or profits" for "and profits".Subsec. (b). Pub. L. 98-353, §363(a), amended subsec. (b) generally. Prior to amendment, subsec. (b) read as follows: "Property of the estate does not include any power that the debtor may only exercise solely for the benefit of an entity other than the debtor."Subsec. (c)(1). Pub. L. 98-353, §456(b)(1), inserted "in an agreement, transfer, instrument, or applicable nonbankruptcy law".Subsec. (c)(1)(B). Pub. L. 98-353, §456(b)(2), substituted "taking" for "the taking", and inserted "before such commencement" after "custodian".Subsec. (d). Pub. L. 98-353, §456(c), inserted "(1) or (2)" after "(a)".Subsec. (e). Pub. L. 98-353, §456(d), struck out subsec. (e) which read as follows: "The estate shall have the benefit of any defense available to the debtor as against an entity other than the estate, including statutes of limitation, statutes of frauds, usury, and other personal defenses. A waiver of any such defense by the debtor after the commencement of the case does not bind the estate."*

EFFECTIVE DATE OF 2014 AMENDMENT*Amendment by Pub. L. 113-295 applicable with respect to cases commenced under this title on or after Dec. 19, 2014, see section 104(d) of Pub. L. 113-295 set out as a note under section 521 of this title.*

EFFECTIVE DATE OF 2005 AMENDMENT*Amendment by section 1221(c) of Pub. L. 109-8 applicable to cases pending under this title on Apr. 20, 2005, or filed under this title on or after Apr. 20, 2005, with certain exceptions, see section 1221(d) of Pub. L. 109-8 set out as a note under section 363 of this title.Amendment by*

sections 225(a), 323, 1212, and 1230 of Pub. L. 109-8 effective 180 days after Apr. 20, 2005, and not applicable with respect to cases commenced under this title before such effective date, except as otherwise provided, see section 1501 of Pub. L. 109-8 set out as a note under section 101 of this title.

EFFECTIVE DATE OF 1994 AMENDMENT*Amendment by Pub. L. 103-394 effective Oct. 22, 1994, and not applicable with respect to cases commenced under this title before Oct. 22, 1994, see section 702 of Pub. L. 103-394 set out as a note under section 101 of this title.*

EFFECTIVE DATE OF 1992 AMENDMENT*Amendment by Pub. L. 102-486 effective Oct. 24, 1992, but not applicable with respect to cases commenced under this title before Oct. 24, 1992, see section 3017(c) of Pub. L. 102-486 set out as a note under section 101 of this title.*

EFFECTIVE DATE OF 1984 AMENDMENT*Amendment by Pub. L. 98-353 effective with respect to cases filed 90 days after July 10, 1984, see section 552(a) of Pub. L. 98-353 set out as a note under section 101 of this title.*

ADJUSTMENT OF DOLLAR AMOUNTS*The dollar amounts specified in this section were adjusted by notices of the Judicial Conference of the United States pursuant to section 104 of this title as follows:By notice dated Feb. 5, 2019, 84 F.R. 3488, effective Apr. 1, 2019, in subsec. (b)(5)(C), (6)(C), (10)(C), dollar amount "6,425" was adjusted to "6,825". See notice of the Judicial Conference of the United States set out as a note under section 104 of this title.By notice dated Feb. 16, 2016, 81 F.R. 8748, effective Apr. 1, 2016, in subsec. (b)(5)(C), (6)(C), dollar amount "6,225" was adjusted to "6,425".By notice dated Feb. 12, 2013, 78 F.R. 12089, effective Apr. 1, 2013, in subsec. (b)(5)(C), (6)(C), dollar amount "5,850" was adjusted to "6,225".By notice dated Feb. 19, 2010, 75 F.R. 8747, effective Apr. 1, 2010, in subsec. (b)(5)(C), (6)(C), dollar amount "5,475" was adjusted to "5,850".By notice dated Feb. 7, 2007, 72 F.R. 7082, effective Apr. 1, 2007, in subsec. (b)(5)(C), (6)(C), dollar amount "5,000" was adjusted to "5,475".*

N.Y. C.P.L.R. § 5205

Section 5205 - Personal property exempt from application to the satisfaction of money judgments

(a) Exemption for personal property. The following personal property when owned by any person is exempt from application to the satisfaction of a money judgment except where the judgment is for the purchase price of the exempt property or was recovered by a domestic, laboring person or mechanic for work performed by that person in such capacity:

1. all stoves and home heating equipment kept for use in the judgment debtor's dwelling house and necessary fuel therefor for one hundred twenty days; one sewing machine with its appurtenances;

2. religious texts, family pictures and portraits, and school books used by the judgment debtor or in the family; and other books, not exceeding five hundred dollars in value, kept and used as part of the family or judgment debtor's library;

3. a seat or pew occupied by the judgment debtor or the family in a place of public worship;

4. domestic animals with the necessary food for those animals for one hundred twenty days, provided that the total value of such animals and food does not exceed one thousand dollars; all necessary food actually provided for the use of the judgment debtor or his family for one hundred twenty days;

5. all wearing apparel, household furniture, one mechanical, gas or electric refrigerator, one radio receiver, one television set, one computer and associated equipment, one cellphone, crockery, tableware and cooking utensils necessary for the judgment debtor and the family; all prescribed health aids;

6. a wedding ring; a watch, jewelry and art not exceeding one thousand dollars in value;

7. tools of trade, necessary working tools and implements, including those of a mechanic, farm machinery, team, professional instruments, furniture and library, not exceeding three thousand dollars in value, together with the necessary food for the team for one hundred twenty days, provided, however, that the articles specified in this paragraph are necessary to the carrying on of the judgment debtor's profession or calling;

8. one motor vehicle not exceeding four thousand dollars in value above liens and encumbrances of the debtor; if such vehicle has been equipped for use by a disabled debtor, then ten thousand dollars in value above liens and encumbrances of the debtor; provided, however, that this exemption for one motor vehicle shall not apply if the debt enforced is for child support, spousal support, maintenance, alimony or equitable distribution, or if the state of New York or any of its agencies or any municipal corporation is the judgment creditor; and

9. if no homestead exemption is claimed, then one thousand dollars in personal property, bank account or cash.

(b) Exemption of cause of action and damages for taking or injuring exempt personal property. A cause of action, to recover damages for taking or injuring personal property exempt from application to the satisfaction of a money judgment, is exempt from application to the satisfaction of a money judgment. A money judgment and its proceeds arising out of such a cause of action is exempt, for one year after the collection thereof, from application to the satisfaction of a money judgment.

(c) Trust exemption.

1. Except as provided in paragraphs four and five of this subdivision, all property while held in trust for a judgment debtor, where the trust has been created by, or the fund so held in trust has proceeded from, a person other than the judgment debtor, is exempt from application to the satisfaction of a money judgment.

2. For purposes of this subdivision, all trusts, custodial accounts, annuities, insurance contracts, monies, assets or interests established as part of, and all payments from, either any trust or plan, which is qualified as an individual retirement account under section four hundred eight or section four hundred eight A of the United States Internal Revenue Code of 1986, as amended, a Keogh (HR-10), retirement or other plan established by a corporation, which is qualified under section 401 of the United States Internal Revenue Code of 1986, as amended, or created as a result of rollovers from such plans pursuant to sections 402 (a) (5), 403 (a) (4), 408 (d) (3) or 408A of the Internal Revenue Code of 1986, as amended, or a plan that satisfies the requirements of section 457 of the Internal Revenue Code of 1986, as amended, shall be considered a trust which has been created by or which has proceeded from a person other than the judgment debtor, even though such judgment debtor is (i) in the case of an individual retirement account plan, an individual who is the settlor of and depositor to such account plan, or (ii) a self-employed individual, or (iii) a partner of the entity sponsoring the Keogh (HR-10) plan, or (iv) a shareholder of the corporation sponsoring the retirement or other plan or (v) a participant in a section 457 plan.

3. All trusts, custodial accounts, annuities, insurance contracts, monies, assets, or interests described in paragraph two of this subdivision shall be conclusively presumed to be spendthrift trusts under this section and the common law of the state of New York for all purposes, including, but not limited to, all cases arising under or related to a case arising under sections one hundred one to thirteen hundred thirty of title eleven of the United States Bankruptcy Code, as amended.

4. This subdivision shall not impair any rights an individual has under a qualified domestic relations order as that term is defined in section 414(p) of the United States Internal Revenue Code of 1986, as amended or under any order of support, alimony or maintenance of any court of competent jurisdiction to enforce arrears/past due support whether or not such arrears/past due support have been reduced to a money judgment.

5. Additions to an asset described in paragraph two of this subdivision shall not be exempt from application to the satisfaction of a money judgment if (i) made after the date that is ninety days before the interposition of the claim on which such judgment was entered, or (ii) deemed to be voidable transactions under article ten of the debtor and creditor law.

(d) Income exemptions. The following personal property is exempt from application to the satisfaction of a money judgment, except such part as a court determines to be unnecessary for the reasonable requirements of the judgment debtor and his dependents:

1. ninety per cent of the income or other payments from a trust the principal of which is exempt under subdivision (c); provided, however, that with respect to any income or payments made from trusts, custodial accounts, annuities, insurance contracts, monies, assets or interest established as part of an individual retirement account plan or as part of a Keogh (HR-10), retirement or other plan described in paragraph two of subdivision (c) of this section, the exception in this subdivision for such part as a court determines to be unnecessary for the reasonable requirements of the judgment debtor and his dependents shall not apply, and the ninety percent exclusion of this paragraph shall become a one hundred percent exclusion;

2. ninety per cent of the earnings of the judgment debtor for his personal services rendered within sixty days before, and at any time after, an income execution is delivered to the sheriff or a motion is made to secure the application of the judgment debtor's earnings to the satisfaction of the judgment; and

3. payments pursuant to an award in a matrimonial action, for the support of a wife, where the wife is the judgment debtor, or for the support of a child, where the child is the judgment debtor; where the award was made by a court of the state, determination of the extent to which it is unnecessary shall be made by that court.

(e) Exemptions to members of armed forces. The pay and bounty of a non-commissioned officer, musician or private in the armed forces of the United States or the state of New York; a land warrant, pension or other reward granted by the United States, or by a state, for services in the armed forces; a sword, horse, medal, emblem or device of any kind presented as a testimonial for services rendered in the armed forces of the United States or a state; and the uniform, arms and equipments which were used by a person in the service, are exempt from application to the satisfaction of a money judgment; provided, however, that the provisions of this subdivision shall not apply to the satisfaction of any order or money judgment for the support of a person's child, spouse, or former spouse.

(f) Exemption for unpaid milk proceeds. Ninety per cent of any money or debt due or to become due to the judgment debtor for the sale of milk produced on a farm operated by him and delivered for his account to a milk dealer licensed pursuant to article twenty-one of the agriculture and markets law is exempt from application to the satisfaction of a money judgment.

(g) Security deposit exemption. Money deposited as security for the rental of real property to be used as the residence of the judgment debtor or the judgment debtor's family; and money deposited as security with a gas, electric, water, steam, telegraph or telephone

corporation, or a municipality rendering equivalent utility services, for services to judgment debtor's residence or the residence of judgment debtor's family, are exempt from application to the satisfaction of a money judgment.

(h) The following personal property is exempt from application to the satisfaction of money judgment, except such part as a court determines to be unnecessary for the reasonable requirements of the judgment debtor and his dependents:

1. any and all medical and dental accessions to the human body and all personal property or equipment that is necessary or proper to maintain or assist in sustaining or maintaining one or more major life activities or is utilized to provide mobility for a person with a permanent disability; and

2. any guide dog, service dog or hearing dog, as those terms are defined in section one hundred eight of the agriculture and markets law, or any animal trained to aid or assist a person with a permanent disability and actually being so used by such person, together with any and all food or feed for any such dog or other animal.

(i) Exemption for life insurance policies. The right of a judgment debtor to accelerate payment of part or all of the death benefit or special surrender value under a life insurance policy, as authorized by paragraph one of subsection (a) of section one thousand one hundred thirteen of the insurance law, or to enter into a viatical settlement pursuant to the provisions of article seventy-eight of the insurance law, is exempt from application to the satisfaction of a money judgment.

(j) Exemption for New York state college choice tuition savings program trust fund payment monies. Monies in an account created pursuant to article fourteen-A of the education law are exempt from application to the satisfaction of a money judgment as follows:

1. one hundred percent of monies in an account established in connection with a scholarship program established pursuant to such article is exempt;

2. one hundred percent of monies in an account is exempt where the judgment debtor is the account owner and designated beneficiary of such account and is a minor; and

3. an amount not exceeding ten thousand dollars in an account, or in the aggregate for more than one account, is exempt where the judgment debtor is the account owner of such account or accounts.

For purposes of this subdivision, the terms "account owner" and "designated beneficiary" shall have the meanings ascribed to them in article fourteen-A of the education law.

(k) Notwithstanding any other provision of law to the contrary, where the judgment involves funds of a convicted person as defined in paragraph (c) of subdivision one of section six hundred thirty-two-a of the executive law, and all or a portion of such funds represent compensatory damages awarded by judgment to a convicted person in a separate action, a judgment obtained pursuant to such section six hundred thirty-two-a shall not be subject to execution or enforcement against the first ten percent of the portion of such funds that represents compensatory damages in the convicted person's action; provided, however,

that this exemption from execution or enforcement shall not apply to judgments obtained by a convicted person prior to the effective date of the chapter of the laws of two thousand one which added this sentence or to any amendment to such judgment where such amendment was obtained on or after the effective date of this subdivision. For the purpose of determining the amount of a judgment which is not subject to execution or enforcement pursuant to this subdivision:

(i) the court shall deduct attorney's fees from that portion of the judgment that represents compensatory damages and multiply the remainder of compensatory damages by ten percent; and

(ii) when the judgment includes compensatory and punitive damages, attorney's fees shall be pro rated among compensatory and punitive damages in the same proportion that all attorney's fees bear to all damages recovered.

(l) Exemption of banking institution accounts into which statutorily exempt payments are made electronically or by direct deposit.

1. If direct deposit or electronic payments reasonably identifiable as statutorily exempt payments were made to the judgment debtor's account in any banking institution during the forty-five day period preceding the date a restraining notice was served on the banking institution or an execution was served upon the banking institution by a marshal or sheriff, then two thousand five hundred dollars in the judgment debtor's account is exempt from application to the satisfaction of a money judgment. Nothing in this subdivision shall be construed to limit a creditor's rights under 42 U.S.C. § 659 or 38 U.S.C. § 5301 or to enforce a child support, spousal support, alimony or maintenance obligation. Nothing in this subdivision shall alter the exempt status of funds that are protected from execution, levy, attachment, garnishment or other legal process, pursuant to this section or under any other provision of state or federal law, or shall affect the right of a judgment debtor to claim such exemption.

2. For purposes of this article, "statutorily exempt payments" means any personal property exempt from application to the satisfaction of a money judgment under any provision of state or federal law. Such term shall include, but not be limited to, payments from any of the following sources: social security, including retirement, survivors' and disability benefits, supplemental security income or child support payments; veterans administration benefits; public assistance; workers' compensation; unemployment insurance; public or private pensions; railroad retirement; and black lung benefits.

3.

(i) Beginning on April first, two thousand twelve, and at each three-year interval ending on April first thereafter, the dollar amount of the exemption provided in this section, subdivisions (e) and (h) of section fifty-two hundred twenty-two, subdivision (a) of section fifty-two hundred thirty and subdivision (e) of section fifty-two hundred thirty-two of this article in effect immediately before that date shall be adjusted as provided in subparagraph (ii) of this paragraph.

(ii) The superintendent of financial services shall determine the amount of the adjustment based on the change in the Consumer Price Index for All Urban Consumers, New York-Northern New Jersey-Long Island, NY-NJ-CT-PA, published by the U.S. Department of Labor, Bureau of Labor Statistics, for the most recent three-year period ending on December thirty-first preceding the adjustment, with each adjusted amount rounded to the nearest twenty-five dollars.

(iii) Beginning on April first, two thousand twelve, and at each three-year interval ending on April first thereafter, the superintendent of financial services shall publish the current dollar amount of the exemption provided in this section, subdivisions (e) and (h) of section fifty-two hundred twenty-two, subdivision (a) of section fifty-two hundred thirty and subdivision (e) of section fifty-two hundred thirty-two of this chapter, together with the date of the next scheduled adjustment. The publication shall be substantially in the form set below:
CURRENT DOLLAR AMOUNT OF EXEMPTION FROM ENFORCEMENT OF JUDGMENT UNDER NEW YORK CIVIL PRACTICE LAW AND RULES Sections 5205(l), 5222(e), 5222(h), 5230(a), and 5232(e)

The following is the current dollar amount of exemption from enforcement of money judgments under CPLR sections 5205(l), 5222(e), 5222(h), 5230(a), and 5232(e), as required by CPLR section 5205(l)(3):

(Amount)

This amount is effective on April 1, (year) and shall not apply to cases commenced before April 1, (year). The next adjustment is scheduled for April 1, (year).

(iv) Adjustments made under subparagraph (i) of this paragraph shall not apply with respect to restraining notices served or executions effected before the date of the adjustment.

(m) Nothing in subdivision (l) of this section limits the judgment debtor's exemption rights in this section or under any other law.
(n) Notwithstanding any other provision of law to the contrary, the term "banking institution" when used in this article shall mean and include all banks, trust companies, savings banks, savings and loan associations, credit unions, foreign banking corporations incorporated, chartered, organized or licensed under the laws of this state, foreign banking corporations maintaining a branch in this state, and nationally chartered banks.
(o) The provisions of subdivisions (l), (m) and (n) of this section do not apply when the state of New York, or any of its agencies or municipal corporations is the judgment creditor, or if the debt enforced is for child support, spousal support, maintenance or alimony, provided that the restraining notice or execution contains a legend at the top thereof, above the caption, in sixteen point bold type with the following language: "The judgment creditor is the state of New York, or any of its agencies or municipal corporations, AND/OR the debt enforced is for child support, spousal support, maintenance or alimony.".

N.Y. C.P.L.R. Law § 5205

Amended by New York Laws 2019, ch. 580,Sec. 3, eff. 4/4/2020.
See New York Laws 2019, ch. 580, Sec. 7.

N.Y. C.P.L.R. § 5206

Section 5206 - Real property exempt from application to the satisfaction of money judgments

(a) Exemption of homestead. Property of one of the following types, not exceeding one hundred fifty thousand dollars for the counties of Kings, Queens, New York, Bronx, Richmond, Nassau, Suffolk, Rockland, Westchester and Putnam; one hundred twenty-five thousand dollars for the counties of Dutchess, Albany, Columbia, Orange, Saratoga and Ulster; and seventy-five thousand dollars for the remaining counties of the state in value above liens and encumbrances, owned and occupied as a principal residence, is exempt from application to the satisfaction of a money judgment, unless the judgment was recovered wholly for the purchase price thereof:

1. a lot of land with a dwelling thereon,

2. shares of stock in a cooperative apartment corporation,

3. units of a condominium apartment, or

4. a mobile home.

But no exempt homestead shall be exempt from taxation or from sale for non-payment of taxes or assessments.

(b) Homestead exemption after owner's death. The homestead exemption continues after the death of the person in whose favor the property was exempted for the benefit of the surviving spouse and surviving children until the majority of the youngest surviving child and until the death of the surviving spouse.

(c) Suspension of occupation as affecting homestead. The homestead exemption ceases if the property ceases to be occupied as a residence by a person for whose benefit it may so continue, except where the suspension of occupation is for a period not exceeding one year, and occurs in consequence of injury to, or destruction of, the dwelling house upon the premises.

(d) Exemption of homestead exceeding one hundred fifty thousand dollars in value for the counties of Kings, Queens, New York, Bronx, Richmond, Nassau, Suffolk, Rockland, Westchester and Putnam; one hundred twenty-five thousand dollars for the counties of Dutchess, Albany, Columbia, Orange, Saratoga and Ulster; and seventy-five thousand dollars for the remaining counties of the state. The exemption of a homestead is not void because the value of the property exceeds one hundred fifty thousand dollars for the counties of Kings, Queens, New York, Bronx, Richmond, Nassau, Suffolk, Rockland, Westchester and Putnam; one hundred twenty-five thousand dollars for the counties of Dutchess, Albany, Columbia, Orange, Saratoga and Ulster; and seventy-five thousand dollars for the remaining counties of the state but the lien of a judgment attaches to the surplus.

(e) Sale of homestead exceeding one hundred fifty thousand dollars for the counties of Kings, Queens, New York, Bronx, Richmond, Nassau, Suffolk, Rockland, Westchester and Putnam; one hundred twenty-five thousand dollars for the counties of Dutchess, Albany,

Columbia, Orange, Saratoga and Ulster; and seventy-five thousand dollars for the remaining counties of the state in value. A judgment creditor may commence a special proceeding in the county in which the homestead is located against the judgment debtor for the sale, by a sheriff or receiver, of a homestead exceeding one hundred fifty thousand dollars for the counties of Kings, Queens, New York, Bronx, Richmond, Nassau, Suffolk, Rockland, Westchester and Putnam; one hundred twenty-five thousand dollars for the counties of Dutchess, Albany, Columbia, Orange, Saratoga and Ulster; and seventy-five thousand dollars for the remaining counties of the state in value. The court may direct that the notice of petition be served upon any other person. The court, if it directs such a sale, shall so marshal the proceeds of the sale that the right and interest of each person in the proceeds shall correspond as nearly as may be to his right and interest in the property sold. Money, not exceeding one hundred fifty thousand dollars for the counties of Kings, Queens, New York, Bronx, Richmond, Nassau, Suffolk, Rockland, Westchester and Putnam; one hundred twenty-five thousand dollars for the counties of Dutchess, Albany, Columbia, Orange, Saratoga and Ulster; and seventy-five thousand dollars for the remaining counties of the state, paid to a judgment debtor, as representing his interest in the proceeds, is exempt for one year after the payment, unless, before the expiration of the year, he acquires an exempt homestead, in which case, the exemption ceases with respect to so much of the money as was not expended for the purchase of that property; and the exemption of the property so acquired extends to every debt against which the property sold was exempt. Where the exemption of property sold as prescribed in this subdivision has been continued after the judgment debtor's death, or where he dies after the sale and before payment to him of his portion of the proceeds of the sale, the court may direct that portion of the proceeds which represents his interest be invested for the benefit of the person or persons entitled to the benefit of the exemption, or be otherwise disposed of as justice requires.

(f) Exemption of burying ground. Land, set apart as a family or private burying ground, is exempt from application to the satisfaction of a money judgment, upon the following conditions only:

1. a portion of it must have been actually used for that purpose;

2. it must not exceed in extent one-fourth of an acre; and

3. it must not contain any building or structure, except one or more vaults or other places of deposit for the dead, or mortuary monuments.

N.Y. C.P.L.R. Law § 5206

STRATEGIC PLANNING WHEN CONFRONTED WITH OVERWHELMING DEBT: PART 1.

March 3, 2020

Author: Andrew M. Thaler, Esq.

Faced with a problem, the stress of not knowing what to do can be debilitating and result in procrastination and indecision. In the world of debt, knowledge is power. An understanding of debtor and creditor rights enables one to not only know what is likely to happen in the future but to take proactive measures to alter, to your benefit, what might otherwise happen if nothing is done. Developing a strategy to tackle worrying debt can lead to a fresh start, and financial stability. On the other hand, putting one's head in the sand is usually a poor option because doing nothing leaves everything to chance.

The first step is to identify that there is a problem. The second step is to deal with the problem head on by getting proper and timely advice on how to solve the problem. Unfortunately many people wait too long, or never seek the advice they need in order to make good life choices. As they say, an ounce of prevention is worth a pound of cure. This is the first in a series of articles that illustrate how having pertinent knowledge can drastically affect the outcome.

Consider the following facts and scenarios:

Facts: Debtor, let's call him Mike, is 55 years old:

- owes $100,000 on credit card debts.
- has no savings other than an IRA account with $100,000
- owns a house with his wife that has $200,000 in equity but no other significant assets
- makes $55,000 a year
- uses one credit card to pay another card's minimum monthly payment
- can no longer obtain new credit cards and is now unable to make monthly minimum payments
- receives dunning letters and has been served with lawsuits
- has poor health insurance coverage with high deductibles and has a heart condition that while stable could flare up at any time

Scenario One:

Mike, does not seek advice from a bankruptcy attorney. Mike panics and withdraws $50,000 from his IRA and uses the bulk of the money to pay creditors putting the most pressure on him. Shortly thereafter Mike incurs out of pocket medical costs of $15,000 due to his heart condition (which causes him to miss 4 weeks of work) thereby eliminating his ability to pay the minimum monthly amounts on the remaining $50,000 in credit card debts. More lawsuits are filed. Judgments are placed against his house, his wages are garnished 10% by a judgment creditor that also seizes his bank account with what is left of the IRA money. At this point Mike decides to talk to a bankruptcy attorney. The attorney advises Mike that the withdrawal of the IRA money has made him ineligible to file bankruptcy at this time because the additional income made him fail bankruptcy's "Means Test". If Mike wants to file chapter 7 bankruptcy, he will have to wait 4- 6 months to be eligible. Mike will have to spend time and money trying to avoid the entry of additional judgments being entered against him which will become liens against his house. Mike will only then be eligible to file bankruptcy. His wife is not happy about all this. Mike is miserable.

Scenario Two:

Upon realizing that he simply does not have enough money to pay back his creditors Mike talks to a bankruptcy attorney to discuss his options. The bankruptcy attorney tells Mike that his IRA is protected from the reach of the credit card companies and that he should not withdraw any of the money to pay them as he planned. Mike is also told that if he withdraws money from the IRA to pay debts, including his medical bills, it will affect his eligibility to file chapter 7 bankruptcy. (A case in the E.D.N.Y holds that IRA withdrawals are included in calculation of "current monthly income" for Means Testing purposes. Courts in other jurisdictions have not agreed.) Mike is told that his share of the $200,000 equity in the marital home is exempt from the credit card creditors and no judgment liens will be filed against the house if he acts quickly. Mike is told that he should not consider obtaining a home equity loan to pay his debts because if he files chapter 7 bankruptcy those debts will be permanently discharged. Additionally Mike is told that on the filing of bankruptcy there is an automatic stay that will stop the dunning letters, the lawsuits and the filing of judgments against the house. Mike is told bankruptcy will discharge of all of his credit card debts and that he will be able to keep all of his assets. Mike is relieved that he did not follow advice from others and use his retirement money and equity in the marital home to try and pay his debts.

The above scenarios illustrate that based on the same facts there can be two diametrically opposed outcomes. One is favorable to Mike (he saves his IRA, can file bankruptcy immediately to discharge all his debts, does not tap into the equity in his house and avoids judgments against his house) and the other is a disaster (he loses $50,000 in his IRA, cannot file bankruptcy now, has to deal with creditors who might file judgments against his house and a very unhappy spouse etc.).

In short, a failure to obtain information on debtor and creditor rights can be disastrous. I tell clients that not consulting with an attorney in these situations is like crossing a highway blindfolded late

at night thinking that there is no way they will get hit by a car. You might reach the other side in one piece or you might get hit. In scenario one Mike was hit and hurt bad. In scenario two Mike had his eyes wide open and only crossed the highway after he knew the path was safe. Mike came out unscathed.

The bottom line is that when faced with debt that keeps you up at night, seek advice from a qualified bankruptcy professional. Property that might otherwise be lost can often be protected. Debts that don't seem will ever go away might be discharged. Every case is different. Bankruptcy or other appropriate options for dealing with debt may be available. An education is essential to making an informed decision.

Andrew M. Thaler is founding partner of Thaler Law Firm PLLC, a panel Chapter 7 Bankruptcy Trustee E.D.N.Y. He is rated "AV Preeminent" by Martindale-Hubbell, the highest professional excellence, and selected to the Super Lawyers list in the category bankruptcy & creditor/debtor rights in the NY Metro area.

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What Happens at and How to Prepare for a Bankruptcy Meeting of Creditors

Author: Andrew M. Thaler Esq.*

Upon the filing of an individual chapter 7 bankruptcy petition the court schedules a meeting of creditors. The meeting, by statute, must be held between 21 and 40 days from the filing date. The debtor will receive a notice from the court shortly after the filing notifying him to appear for the examination. The meeting of creditors affords the trustee, creditors and parties in interest with the opportunity to question the debtor with regard to his or her property and debts. The debtor is required to file Bankruptcy Schedules and Statement of Financial Affairs with their Petition. Those documents provide a road map that outlines the Debtor's property and debts as of the filing date, and discloses certain financial transactions that took place in various time periods prior thereto. The trustee will read those documents before the meeting. They documents are publically available and may be read by creditors and parties in interest. The trustee will ask questions at the meeting of creditors which are designed to uncover assets that might not be disclosed in the Schedules and Statement of Financial Affairs. Those assets are typically previously owned real property, prior business interests, prior or future litigation and generally any asset that might have a value large enough to potentially make a distribution to creditors.

Creditors seldom appear at meeting of creditors but when they do they usually have an agenda. A creditor might (i) ask the debtor about an asset that has not been disclosed; (ii) seek to find out if the debtor intends to reaffirm an obligation such as a car loan; or (iii) ask questions designed to support a complaint objecting to the debtor's discharge.

The meeting of creditors is usually held at the courthouse but could be held elsewhere. A judge does not preside at the meeting which ordinarily is not held in a courtroom but a meeting room. The trustee will usually be assigned a case load of up to about 15 cases an hour. The trustee will examine each debtor. The actual examination in a simple case might last as little as 3-5 minutes. In a more complicated case it could last up to an hour or more. Accordingly a debtor must be prepared to spend a half day or more for the examination as there is no guarantee that all the examinations will conclude quickly.

When serving as debtor's counsel I prepare the client in advance to comfortably and truthfully respond to these questions. Both attorney and client want to minimize the time spent answering the trustee’s questions and avoid unnecessary extra scrutiny into the debtor’s affairs. Keep in mind that a trustee may be assigned upwards of a thousand cases each year. Most of those cases have no assets to distribute to creditors, but the trustee will not know that a case has no assets without some level of investigation. The volume of cases assigned to a trustee provides motivation to review and close cases as quickly and efficiently as possible. It therefore makes sense to provide the trustee what he needs to know about the case. This will avoid follow up letters for the debtor to supply documents or the debtor having to appear for examination at an adjourned meeting of creditors. Accordingly, prior to the meeting it is best practice to send the trustee copies of all the documents the trustee might ask be produced at the meeting of creditors (deeds, bank statements etc.) so the trustee can review them in advance and hopefully close the examination right then and there. Counsel should also bring extra copies for the trustee in the event he does not have his copies readily available.

When not representing debtors and serving in my capacity as a chapter 7 Trustee I ask the questions listed below. The questions are designed to try and uncover assets. The responses received may lead to follow up questions. Here are the basic questions I ask in every case which a debtor must be able to answer accurately.

- Have you ever owned a home, house, co-op, condo or real property of any type?
- Does anyone owe you any money?
- Are you presently suing anyone?
- Do you have any claims where you could sue someone and recover money such as a car accident or malpractice case?
- Have you ever been self-employed or been engaged in your own business?
- In the last 6 years have you sold or transferred any asset that you owned or had an interest in that had a value of $5,000 or more?
- In the last year have you paid or transferred any money or property to a family member or business associate on account of a debt?
- Do you now own any stocks or bonds?
- Have you sold or transferred any stocks or bonds in the last 2 years?
- At any one time in the last year have you had $5,000 or more in cash and banks?
- Has anyone died in the past and left you anything?
- Do you expect to inherit anything in the next 6 months?
-
- Have you paid college tuition for an adult child in the past 6 years?
- I will also ask any specific questions that need to be asked that arise from reading the Schedules and Statement of Financial Affairs or questions that creditors might bring to my attention.

Proper preparation for the meeting of creditors can reduce debtor's stress, manage expectations and save everyone a lot of time.

Andrew M. Thaler is a founding member of Thaler Law Firm PLLC. The firm which focuses on bankruptcy, debtor and creditor rights, mediation and trustee representation.

In Bankruptcy Timing is Everything and Planning Essential (The Means Test)
5-29-18

Author: Andrew M. Thaler

Individuals often seek chapter 7 bankruptcy relief to obtain a "fresh start" to discharge debts they have difficulty satisfying. In most chapter 7 cases "eligible" debtors discharge most if not all of their debts and keep most if not all of their property. If they do not properly plan however, they could be shut out of chapter 7, where debts can be discharged in as little as 3 months. Instead, the only alternative may be a choice between a chapter 13 bankruptcy (where creditors are paid all or a portion of their debts from the debtor's future income over three to five years), or not filing at all. As soon as financial trouble appears on the horizon it is critical to consult with a qualified bankruptcy professional so proper planning can occur.

Timing comes into play in numerous aspects of bankruptcy planning. One example is in application of the "Means Test" for debtors with consumer debt.

The "Means Test" is a calculation of a person's income over the full six month period prior to the filing of the bankruptcy petition from just about all sources (social security income however is excluded). Married couples must include both spouses income even if one spouse is not filing for bankruptcy and is not otherwise responsible for their spouse's debts. Individuals with income above the median income where they live will be subject to the "Means Test".

Bottom line, the "Means Test" is nothing more than an eligibility test. The test has nothing to do with the "present" income of the debtor notwithstanding that (i) the average of the prior 6 months income is called that person's "current monthly income" and (ii) that number multiplied by 12 is used to determine yearly income for eligibility purposes.

Fixed Local and National Expense Standards, secured debts on which payments are currently being made, limited other expenses and in some cases special circumstance expenses are deducted from the "current monthly income" amount. The difference between the "current monthly income" and allowable expenses equals that person's disposable income. If the disposable income is over a certain amount, the individual will be ineligible for chapter 7 relief. That leaves the options of not filing bankruptcy at all or to file under some other chapter where disposable income will be paid to creditors over time. Oftentimes an individual who does not pass the "Means Test" will balk at filing a chapter 13 wage earner plan because their actual expenses exceed the Local and National Standard expenses thus leaving them with higher disposable income on paper than they really have in their pocket at the end of each month. Many debtors are not prepared to change their lifestyle to make a chapter 13 plan work. For example, the boat, family vacations and child's college expenses are not allowed expenses in a chapter 13.

A person earning more that the median income during the 6 month look back period but who is presently underemployed, unemployed with no earnings, or declared permanently disabled and unable to work, will not pass the Means Test. Whether fair or not, they must wait until their "current monthly income" is below the Means Test median income amount or their disposable income low enough to pass the Means Test. In the meantime collection activity and lawsuits will not be stayed and assets that otherwise might be exempt from the reach of creditors in bankruptcy can be seized and lost.

A more common scenario is where an individual has spiraled downward financially over a period of time from job loss or reduction in income and decides to file bankruptcy only after they have gotten back on their feet and secured employment or higher income. If they wait too long to file bankruptcy they may be subject to the Means Test or not pass the Means Test thereby foreclosing the ability to discharge debts in a chapter 7 case – something that might have been possible had they filed when they had little or no income. The result is that they may have assets seized or have to pay money to creditors in a chapter 13 reorganization from their disposable income that they could have otherwise discharged. If no bankruptcy is filed they will have to deal with continued creditor collection efforts. Individuals who do not learn their rights and plan appropriately often find out that they used assets that would be exempt in bankruptcy to pay debts that could have been discharged – precious money that could have been saved or used to obtain proper legal advice.

When money is tight people think that they cannot afford to file bankruptcy or even a nominal bankruptcy consultation fee. The exact opposite is often true – they cannot afford to not file bankruptcy or not get proper advice. The reality is that early intervention, education, planning and proactive action will provide peace of mind and better outcomes for most people.

GMAC Mtge., LLC v Coombs
2020 NY Slip Op 07039
Decided on November 25, 2020
Appellate Division, Second Department
Miller, J.
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Decided on November 25, 2020 SUPREME COURT OF THE STATE OF NEW YORK
Appellate Division, Second Judicial Department
SHERI S. ROMAN, J.P.
ROBERT J. MILLER
JOSEPH J. MALTESE
ANGELA G. IANNACCI, JJ.

2017-08030
(Index No. 29971/08)

[*1]GMAC Mortgage, LLC, respondent,

v

Winsome Coombs, appellant, et al., defendants.

APPEAL by the defendant Winsome Coombs, in an action to foreclose a mortgage, from an order of the Supreme Court (Noach Dear, J.), dated June 19, 2017, and entered in Kings County. The order granted the plaintiff's motion for leave to reargue its prior motion, inter alia, for summary judgment on the complaint insofar as asserted against that defendant, which had been denied in an order of the same court (Yvonne Lewis, J.) dated December 18, 2013, and upon reargument, in effect, vacated the determination in the order dated December 18, 2013, denying the plaintiff's prior motion, and thereupon granted the prior motion.

Chidi Eze, Brooklyn, NY, for appellant.

Ras Boriskin, LLC, Westbury, NY, for respondent.

MILLER, J.

OPINION & ORDER

This appeal requires us to address a new statute, RPAPL 1302-a (as added by L 2019, ch 739, § 1), and consider its impact on the affirmative defense of lack of standing and the operation of the waiver provisions contained in CPLR 3211(e). We conclude that, in this case, the Supreme Court should have permitted the defendant to raise the affirmative defense of lack of standing and to amend his answer to include that defense, even though he failed to affirmatively plead it in his answer. However, since the plaintiff nevertheless established its entitlement to summary judgment on the issue of standing and on the complaint, we affirm the order appealed from.

In February 2007, the defendant Winsome Coombs (hereinafter the defendant) executed a note in the sum of $419,225 in favor of Quicken Loans, Inc. The note was secured by a mortgage on residential property in Brooklyn. In November 2008, the plaintiff commenced this action against the defendant, among others, to foreclose the mortgage. The defendant interposed a verified answer, but did not assert that the plaintiff lacked standing to commence this action.

In October 2012, the defendant moved to dismiss the complaint, inter alia, on the ground that the plaintiff lacked standing to commence this action. The plaintiff separately moved, among other things, for summary judgment on the complaint insofar as asserted against the defendant.

In an order dated December 18, 2013, the Supreme Court denied the defendant's motion and the plaintiff's motion. The plaintiff subsequently moved for leave to reargue its prior motion. The defendant opposed the plaintiff's motion for leave to reargue, contending, among other things, that the plaintiff lacked standing to commence this action.

In an order dated June 19, 2017, the Supreme Court granted the plaintiff's motion for leave to reargue and, upon reargument, granted the plaintiff's prior motion. The court did not [*2]address the merits of the standing defense that had been raised by the defendant in opposition to the plaintiff's motion for leave to reargue, finding that the defense had been waived by the defendant's failure to include it in the verified answer. The defendant appeals from the order dated June 19, 2017. We affirm.

"CPLR 3018, which governs responsive pleadings, draws a distinction between denials and affirmative defenses" (*US Bank N.A. v Nelson*, 169 AD3d 110, 113). "Denials generally relate to allegations setting forth the essential elements that must be proved in order to sustain the particular cause of action" and "[t]hus, a mere denial of one or more elements of the cause of action will suffice to place them in issue" (*id.* at 113).

Conversely, a defendant must plead, as an affirmative defense, "all matters which if not pleaded would be likely to take the adverse party by surprise or would raise issues of fact not appearing on the face of a prior pleading" (CPLR 3018[b]; *see US Bank N.A. v Nelson*, 169 AD3d at 113). Accordingly, where a defendant seeks to inject into the litigation "matters [that] are not the plaintiff's burden to prove as part of the cause of action," those matters must be affirmatively pleaded as defenses (Siegel & Connors, NY Prac § 223 [6th ed July 2020 Update]; *see* CPLR 3014; *US Bank N.A. v Nelson*, 169 AD3d at 113; *see also* 5 Weinstein-Korn-Miller, NY Civ Prac: CPLR ¶ 3018.02).

"Failure to plead a defense that must be pleaded affirmatively under CPLR 3018(b) is a waiver of that defense, unless it is raised by a motion under CPLR 3211(a)" (5 Weinstein-Korn-Miller, NY Civ Prac: CPLR ¶ 3018.18; *see Munson v New York Seed Improvement Coop.*, 64 NY2d 985, 986-987; *DeLuca v Pecoraro*, 109 AD3d 636, 637; *Rooney v Slomowitz*, 11 AD3d 864, 867; *Counties of Warren & Washington Indus. Dev. Agency v Boychuck*, 109 AD2d 1024, 1026; *De Lisa v Amica Mut. Ins. Co.*, 59 AD2d 380, 382; *A. A. Sutain, Ltd. v Montgomery Ward & Co.*, 22 AD2d 607, 609-610, *affd* 17 NY2d 776). However, "[s]uch a waiver can be retracted by amendment of the answer" so as to include the omitted defense (*Surlak v Surlak*, 95 AD2d 371, 383; *see* CPLR 3025; *cf. Furlo v Cheek*, 20 AD2d 939, 940; *see generally* 5 Weinstein-Korn-Miller, NY Civ Prac: CPLR ¶ 3018.18).

If a defendant fails to amend the answer within the time prescribed by CPLR 3025(a), the defendant may amend the answer to include a new defense pursuant to CPLR 3025(b) "at any time by leave of court or by stipulation of all parties" (CPLR 3025[b]). The statute directs

that "[l]eave shall be freely given upon such terms as may be just including the granting of costs and continuances" (CPLR 3025[b]; *see Murray v City of New York*, 43 NY2d 400, 404-406).

CPLR 3211(e), however, places important limitations on a defendant's ability to retract a waiver of certain affirmative defenses through the amendment of an answer pursuant to CPLR 3025(b) (*see generally* Siegel, NY Prac § 275 at 473 [5th ed]). Although this subdivision uses the same term — "waived" —in three separate sentences, the various types of waivers occasioned by CPLR 3211(e) are not uniformly applied. Indeed, as the case law illustrates, the effect of such a waiver may vary depending on the nature of the defense that was waived.

For example, CPLR 3211(e) provides that

> "[a]n objection based upon a ground specified in [CPLR 3211(a)(8) or (9)] is waived if a party moves on any of the grounds set forth in [CPLR 3211(a)] without raising such objection or if, having made no objection under [CPLR 3211(a)], he or she does not raise such objection in the responsive pleading."

CPLR 3211(a)(8) and (9) include defenses relating to personal and in rem jurisdiction.

The Court of Appeals has held that once a jurisdictional defense listed in CPLR 3211(a)(8) or (9) has been "waived" under CPLR 3211(e), the resulting waiver may not be retracted through subsequent amendment to the answer pursuant to CPLR 3025(b) (*see Addesso v Shemtob*, 70 NY2d 689, 690; *Boulay v Olympic Flame*, 165 AD2d 191, 194; *cf. Iacovangelo v Shepherd*, 5 NY3d 184, 186; *Ficorp, Ltd. v Gourian*, 263 AD2d 392, 392-393). Accordingly, "[w]hile permission to amend an answer is to be freely given pursuant to CPLR 3025(b), the waiver of a *jurisdictional* defense [listed in CPLR 3211(a)(8) or (9)] cannot be nullified by a subsequent amendment to a pleading adding the missing affirmative defense" (*McGowan v Hoffmeister*, 15 AD3d 297, 297; *see Addesso v Shemtob*, 70 NY2d at 690).

The "objections of personal or *[in] rem* jurisdiction . . . are deemed so fundamental" that they are irretrievably waived if the defendant makes a motion pursuant to CPLR 3211(a) without [*3]raising those threshold jurisdictional defenses (Siegel & Connors, NY Prac § 274 [6th ed]; *see* CPLR 3211[e]; *Competello v Giordano*, 51 NY2d 904, 905). Indeed, "[t]he purpose of [this] waiver provision of [CPLR 3211(e)] is to prevent the defendant from wasting both the 'court's or the plaintiff's time on any 3211 motion on any ground at all unless

on that motion [she or] he joins [those] jurisdictional [defenses]'" (*Competello v Giordano*, 51 NY2d at 905, quoting David D. Siegel, Practice Commentaries, McKinney's Cons Laws of NY, Book 7B, CPLR C3211:59 at 63). The purpose underlying that provision would obviously be frustrated if a defendant could retract a waiver of these jurisdictional defenses "at any time" by amending its answer to include them (CPLR 3025[b]).

Similarly, another provision of CPLR 3211(e) provides that

> "an objection that the summons and complaint . . . was not properly served is waived if, having raised such an objection in a pleading, the objecting party does not move for judgment on that ground within sixty days after serving the pleading, unless the court extends the time upon the ground of undue hardship" (*cf. Goldenberg v Westchester County Health Care Corp.*, 16 NY3d 323, 327).

The purpose of the 1996 amendment to CPLR 3211(e), which added the 60-day time limit, was "'to require a party with a genuine objection to service to deal with the issue promptly and at the outset of the action . . . ferret out unjustified objections and . . . provide for the prompt resolution of those that have merit'" (*Wade v Byung Yang Kim*, 250 AD2d 323, 325, quoting Senate Introducer's Mem in Support, Bill Jacket, L 1996, ch 501 at 5; *see U.S. Bank N.A. v Roque*, 172 AD3d 948, 951; *Deutsche Bank Natl. Trust Co. v Acevedo*, 157 AD3d 859, 861).

In contrast to the two provisions noted above, a third waiver provision contained in CPLR 3211(e) provides that "[a]ny objection or defense based upon a ground set forth in [CPLR 3211(a)(1), (3), (4), (5), and (6)] is waived unless raised either by such motion or in the responsive pleading" (*see McLean v Sachem Cent. Sch. Dist.*, 186 AD3d 470; *M & E 73-75, LLC v 57 Fusion LLC*, ____ AD3d ____, 2020 NY Slip Op 04372 [1st Dept]; *Bonanni v Horizons Invs. Corp.*, 179 AD3d 995, 1001; *Pace v Perk*, 81 AD2d 444, 461-462). The specifically enumerated defenses that are subject to this portion of the subdivision include "legal capacity" (CPLR 3211[a][3]), "arbitration and award, collateral estoppel, discharge in bankruptcy, infancy or other disability of the moving party, payment, release, res judicata, statute of limitations, [and] statute of frauds" (CPLR 3211[a][5]).

Unlike a waiver of the jurisdictional defenses listed in CPLR 3211(a)(8) and (9), which cannot be retracted through amendment to the pleadings (*see Addesso v Shemtob*, 70 NY2d at 690; *McGowan v Hoffmeister*, 15 AD3d at 297), a waiver of the defenses listed in CPLR 3211(a)(1), (3), (4), (5), and (6) may generally be retracted through amendment to the answer

pursuant to CPLR 3025 to include the waived defense (*see e.g. Barrett v Kasco Constr. Co.*, 56 NY2d 830, 831; *Fahey v County of Ontario*, 44 NY2d 934, 935; Congregation B'nai Jehuda v Hiyee Realty Corp., 35 AD3d 311, 313; *Town of Webster v Village of Webster*, 280 AD2d 931, 932-933; *Henderson v Gulati*, 270 AD2d 308, 309; *Ficorp, Ltd. v Gourian*, 263 AD2d at 392; *Endicott Johnson Corp. v Konik Indus.*, 249 AD2d 744, 744-745; *Marks v Macchiarola*, 221 AD2d 217, 218; *Armstrong v Peat, Marwick, Mitchell & Co.*, 150 AD2d 189, 190; *A. J. Pegno Constr. Corp. v City of New York*, 95 AD2d 655, 656; *Pace v Perk*, 81 AD2d at 461-462).

A waiver under this portion of CPLR 3211(e) is therefore consistent with the general waiver that results from a failure to affirmatively plead a defense in accordance with CPLR 3018(b), which, as already observed, may generally be retracted through amendment to the pleadings (*see* CPLR 3025; *Surlak v Surlak*, 95 AD2d at 383; *see generally* 5 Weinstein-Korn-Miller, NY Civ Prac: CPLR ¶ 3018.18). A waiver of these defenses may also be retracted by raising the defense in a motion for summary judgment, or in opposition to a motion for summary judgment, under which circumstances a court may, in the provident exercise of its discretion, "deem[ ] [the] defendant's answer amended to include the affirmative defense . . . on [the] motion for summary judgment" (*Barrett v Kasco Constr. Co.*, 56 NY2d at 831; *see Seaboard Sur. Co. v Nigro Bros.*, 222 AD2d 574, 574; *Adsit v Quantum Chem. Corp.*, 199 AD2d 899, 900; *Creary v Davie*, 188 AD2d 1033, 1033-1034; *Armstrong v Peat, Marwick, Mitchell & Co.*, 150 AD2d at 191; *Ballen v Aero Mayflower Tr. Co.*, 144 AD2d 407, 409; *McIvor v Di Benedetto*, 121 AD2d 519, 521-522; *see also Dampskibsselskabet Torm A/S v Thomas Paper Co.*, 26 AD2d 347, 352).

Finally, CPLR 3211(e) lists an additional set of defenses which may be raised in a motion "made at any subsequent time or in a later pleading, if one is permitted." These defenses include lack of subject matter jurisdiction (*see* CPLR 3211[a][2]), failure to state a cause of action (*see* CPLR 3211[a][7]), and "the absence of a person who should be a party" (CPLR 3211[a][10]). The defenses listed in CPLR 3211(a)(2), (7), and (10), implicate fundamental limitations on the power of a court to render an enforceable judgment (*see* Restatement [Second] of Judgments §§ 11, 62). Subject matter jurisdiction, in particular, is "so fundamental to the power of adjudication of a court that [the defense will] survive even a final judgment or order" (*Lacks v Lacks*, 41 NY2d 71, 74-75; *see generally* Restatement [Second] of Judgments §§ 12, 76). Under CPLR 3211(e), the defenses listed in subdivisions CPLR 3211(a)(2), (7), and (10) may be raised by motion "at any time" (*M & E 73-75, LLC v*

57 Fusion LLC,_____ AD3d _____, 2020 NY Slip Op 04372, *2; *see McMahon v Cobblestone Lofts Condominium*, 161 AD3d 536, 536-537; *Chuqui v Church of St. Margaret Mary*, 39 AD3d 397, 397; *Rainbow Hospitality Mgt. v Mesch Eng'g*, 270 AD2d 906, 906; *Pace v Perk*, 81 AD2d at 449), or by amendment to a pleading, "if one is permitted" (CPLR 3211[e]).

The defense of standing is not specifically mentioned in CPLR 3211(a) or (e). In *Wells Fargo Bank Minn., N.A. v Mastropaolo* (42 AD3d 239, 242, quoting CPLR 3211[a][3]), this Court considered "whether a defense based on lack of standing is more akin to the defense that the plaintiff 'has not legal capacity to sue,' as set forth in CPLR 3211(a)(3), or to the nonwaivable defense that the court lacks subject matter jurisdiction, as set forth in CPLR 3211(a)(2)."

This Court determined that "[e]ven though the frequently invoked term 'jurisdictional' has been used occasionally to refer to standing, a plaintiff's lack of standing affects, at most, a court's power to render a judgment on the merits in the plaintiff's favor" (*Wells Fargo Bank Minn., N.A. v Mastropaolo*, 42 AD3d at 243). This Court stated that a plaintiff's "alleged lack of standing at the time [the] action was commenced . . . [is] not a jurisdictional defect that [is] 'so fundamental to the power of adjudication of a court' (*Lacks v Lacks*, [41 NY2d] at 74), that it could not be waived" (*id.* at 244; *cf. MacAffer v Boston & Me. R.R.*, 268 NY 400, 405). Accordingly, this Court held that "where a defendant does not challenge a plaintiff's standing," the issue may be waived and "the plaintiff may be relieved of its obligation to prove that it is the proper party to seek the requested relief" (*Wells Fargo Bank Minn., N.A. v Mastropaolo*, 42 AD3d at 242, 244-245). In reaching its conclusion, this Court cited to authority which described standing as "'an aspect of justiciability which, when challenged, must be considered at the outset of any litigation'" (*id.* at 242 [emphasis omitted], quoting *Society of Plastics Indus. v County of Suffolk*, 77 NY2d 761, 769; *see Community Bd. 7 of Borough of Manhattan v Schaffer*, 84 NY2d 148, 154-155).

In subsequent case law this Court, citing to *Wells Fargo Bank Minn., N.A. v Mastropaolo* (42 AD3d 239), used language that may be read to imply that a waiver of the defense of standing should be applied in a manner consistent with a waiver of the threshold jurisdictional defenses listed in CPLR 3211(a)(8) and (9), which may not be retracted by subsequent amendment to a pleading (*see e.g. HSBC Bank, USA v Dammond*, 59 AD3d 679, 680). Of course, this Court has never held that a waiver of the defense of standing could not be

retracted in an answer amended by leave of court pursuant to CPLR 3025(b) (*see U.S. Bank N.A. v Laino*, 172 AD3d 947, 948; *HSBC Mtge. Servs., Inc. v Alphonso*, 163 AD3d 934, 936; *DLJ Mtge. Capital, Inc. v David*, 147 AD3d 1024, 1025; *HSBC Bank USA, NA v Halls*, 136 AD3d 752, 753-754; *Bank of N.Y. Mellon v Aquino*, 131 AD3d 1186, 1187; *U.S. Bank, N.A. v Sharif*, 89 AD3d 723, 724).

Such a holding would be contrary to the language in *Wells Fargo Bank Minn., N.A. v Mastropaolo* (42 AD3d 239, 243), which indicated that "for purposes of the waiver rule set forth in CPLR 3211(e), standing and capacity to sue are sufficiently related that they should be afforded identical treatment" (*see* Siegel & Connors, NY Prac §§ 136, 261 [6th ed]; *cf. Guiffrida v Storico Dev., LLC*, 60 AD3d 1286, 1287). As already observed, a waiver of the affirmative defenses listed under CPLR 3211(a)(3) and (5), including capacity to sue, may generally be retracted through the amendment of a pleading pursuant to CPLR 3025 (*see Complete Mgt., Inc. v Rubenstein*, 74 AD3d 722, 723-724; *see also Tedesco v A.P. Green Indus., Inc.*, 8 NY3d 243, 246; *Igbara Realty Corp. v New York Prop. Ins. Underwriting Assn.*, 63 NY2d 201, 218-219; *cf. A. A. Sutain, Ltd. v Montgomery Ward & Co.*, 17 NY2d at 778).

In any event, to the extent that "our past decisions have lacked a precise consistency" on this issue (*Miller v Miller*, 22 NY2d 12, 15; *see Stukas v Streiter*, 83 AD3d 18, 30), we now reaffirm that a waiver of the defense of standing pursuant to CPLR 3211(e) should be given the same [*4]force and effect as a waiver of the affirmative defenses specifically enumerated in CPLR 3211(a)(3) and (5) (*see Wells Fargo Bank Minn., N.A. v Mastropaolo*, 42 AD3d at 243). Accordingly, a waiver of the affirmative defense of standing pursuant to CPLR 3211(e) may be retracted through the amendment of a pleading pursuant to CPLR 3025 (*see e.g. U.S. Bank N.A. v Laino*, 172 AD3d at 948; *DLJ Mtge. Capital, Inc. v David*, 147 AD3d at 1025; *U.S. Bank, N.A. v Sharif*, 89 AD3d at 724). Case law from this Court should not be read to hold otherwise (*cf. US Bank N.A. v Dorestant*, 131 AD3d 467, 470; *Wells Fargo Bank, N.A. v Combs*, 128 AD3d 812, 813; *JPMorgan Mtge. Acquisition Corp. v Hayles*, 113 AD3d 821, 822; *Deutsche Bank Natl. Trust Co. v Hussain*, 78 AD3d 989, 990; *New York Community Bank v Vermonty*, 68 AD3d 1074, 1076; *HSBC Bank, USA v Dammond*, 59 AD3d at 680).

RPAPL 1302-a adds an additional layer of complexity to the operation of CPLR 3211(e), and to the defense of standing in certain actions. Enacted on December 23, 2019, and effective that same date (*see* L 2019, ch 739, § 1), the statute, *in toto*, provides:

> "Notwithstanding the provisions of [CPLR 3211(e)], any objection or defense based on the plaintiff's lack of standing in a foreclosure proceeding related to a home loan, as defined in [RPAPL 1304(6)(a)], shall not be waived if a defendant fails to raise the objection or defense in a responsive pleading or pre-answer motion to dismiss. A defendant may not raise an objection or defense of lack of standing following a foreclosure sale, however, unless the judgment of foreclosure and sale was issued upon defendant's default" (RPAPL 1302-a).

The new statute, by its own terms, only applies to residential mortgage foreclosure actions involving a "home loan," as that term is defined in RPAPL 1304(6)(a) (RPAPL 1302-a). Accordingly, with the enactment of RPAPL 1302-a, the procedural rules applicable to the defense of standing may vary depending on the substantive nature of the litigation at issue (*see* RPAPL 1302-a).

Where applicable, RPAPL 1302-a provides that a failure to raise standing as a defense in a responsive pleading or motion to dismiss does not constitute a waiver pursuant to CPLR 3211(e) (*see* RPAPL 1302-a). The purpose of the law is to help assure that issues of standing are resolved on their merits (*see* Sponsor's Mem, Bill Jacket, L 2019 SB 5160, ch 739 [April 12, 2019]).

Although the new statute provides that the defense of standing is not waived pursuant to CPLR 3211(e) by a defendant's failure to raise it in a responsive pleading or motion to dismiss, it does not thereby absolve a defendant from actually raising the issue before it may properly be considered by a court (*see HSBC Bank USA, N.A. v Szoffer*, 149 AD3d 1400, 1401). Indeed, had the Legislature intended to vest a court with the discretionary authority to raise the issue of standing "on its own initiative," as it has done in several provisions of the CPLR (CPLR 1003; *see* CPLR 3215[c]; 3216[a]; 4404[a], [b]), it could have inserted such language into RPAPL 1302-a. It did not do so. Accordingly, we conclude that RPAPL 1302-a does not disturb the well-settled case law holding that "a party's lack of standing does not constitute a jurisdictional defect" (*U.S. Bank, N.A. v Emmanuel*, 83 AD3d 1047, 1048-1049; *see Matter of Fossella v Dinkins*, 66 NY2d 162; *HSBC Bank USA, N.A. v Taher*, 104 AD3d 815, 817), and that the defense of standing should not be raised by a court, sua sponte (*see e.g. Matter of Barbeau v Village of LeRoy*, 181 AD3d 1155, 1157; *Emic Corp. v Barenblatt*, 169 AD3d 621, 621-622; *Citimortgage, Inc. v Gill*, 165 AD3d 623, 623; *HSBC Bank USA, N.A. v Szoffer*, 149 AD3d at 1401).

The Legislature also could have required a plaintiff to plead and prove standing as an essential element of every applicable residential mortgage foreclosure action. It did not do this either. Although RPAPL 1302-a specifies that its provisions are controlling " [n]otwithstanding the provisions of [CPLR 3211(e)]," it makes no reference to any other section of the CPLR. Under basic rules of statutory construction, the express inclusion of CPLR 3211(e) and the omission of any other reference to the CPLR leads to the conclusion that CPLR 3211(e) is the only statute impacted by the enactment of RPAPL 1302-a (*see* McKinneys Cons Laws of NY, Book 1, Statutes, § 240; *Matter of Benjamin v New York City Empls. Retirement Sys.*, 170 AD3d 714, 716).

Accordingly, even where applicable, the new statute does not impact the operation of CPLR 3018(b) or case law holding that "where, as here, standing is not an essential element of the cause of action, under CPLR 3018(b) a defendant must affirmatively plead lack of standing as an affirmative defense in the answer in order to properly raise the issue in its responsive pleading" (*US Bank N.A. v Nelson*, 169 AD3d at 114; *see Citimortgage, Inc. v Etienne*, 172 AD3d 808, 810; *[*5]BAC Home Loans Servicing, LP v Alvarado*, 168 AD3d 1029, 1030). However, it should again be emphasized that the waiver that results from a failure to affirmatively plead a defense in accordance with CPLR 3018(b), including a waiver of the defense of standing, may be retracted through subsequent amendment to the pleadings (*see* CPLR 3025; *U.S. Bank N.A. v Laino*, 172 AD3d at 948; *DLJ Mtge. Capital, Inc. v David*, 147 AD3d at 1025; *U.S. Bank, N.A. v Sharif*, 89 AD3d at 724; *Mendrzycki v Cricchio*, 58 AD3d 171, 175; *cf. Nannini & Callahan Excavating v Park Rd. Constr. Corp.*, 234 AD2d 352, 352).

Where applicable, RPAPL 1302-a places the defense of standing on a footing comparable with the other defenses that are exempt from the waiver provisions of CPLR 3211(e), to wit, those defenses listed in subdivisions CPLR 3211(a)(2), (7), and (10), which may be raised by motion "at any time" (*M & E 73-75, LLC v 57 Fusion LLC*, _____ AD3d _____, 2020 NY Slip Op 04372, *2), or by amendment to a pleading, "if one is permitted" (CPLR 3211[e]; *see* CPLR 3025[b]). Even where the defense of standing is omitted from a defendant's answer in violation of CPLR 3018(b), the defense may be raised for the first time in opposition to a plaintiff's motion for summary judgment (*see First Trust Natl. Assn. v DeLuca*, 284 AD2d 494, 494; *Kelly v City of New York*, 117 AD2d 781, 782; *Village of Port Chester v Hartford Acc. & Indem. Co.*, 90 AD2d 831, 831-832; *Jandous Elec. Constr. Corp. v City of New York*, 88 AD2d 821, 822, *affd* 57 NY2d 848; *Rizzi v Sussman*, 9 AD2d 961; *see*

generally Curry v Mackenzie, 239 NY 267, 272). Under such circumstances a court may, in the provident exercise of its discretion, "deem[ ] [the] defendant's answer amended to include the affirmative defense . . . on [the] motion for summary judgment" (*Barrett v Kasco Constr. Co.*, 56 NY2d at 831; *see Adsit v Quantum Chem. Corp.*, 199 AD2d at 900; *cf. Rooney v Slomowitz*, 11 AD3d at 867; *Counties of Warren & Washington Indus. Dev. Agency v Boychuck*, 109 AD2d at 1026). Where an affirmative defense is raised for the first time in opposition to a motion for summary judgment, new evidence relevant to that defense may generally be submitted in reply papers inasmuch as "the evidence [is] submitted...in response to allegations raised for the first time in the opposition papers" (*Citimortgage, Inc. v Espinal*, 134 AD3d 876, 879; *see e.g. CitiMortgage, Inc. v Goldberg*, 179 AD3d 1006, 1008; *JPMorgan Chase Bank, N.A. v Corrado*, 162 AD3d 994, 995-996).

If an amendment to the answer pursuant to CPLR 3025(a) is not possible, leave to amend an answer may be obtained pursuant to CPLR 3025(b). As that subdivision commands, leave to amend should be "freely given upon such terms as may be just including the granting of costs and continuances" (CPLR 3025[b]; *see Murray v City of New York*, 43 NY2d at 404-406). "[L]eave to amend a pleading should be granted where the amendment is neither palpably insufficient nor patently devoid of merit, and the delay in seeking amendment does not prejudice or surprise the opposing party" (*DLJ Mtge. Capital, Inc. v David*, 147 AD3d at 1025; *see Aurora Loan Servs., LLC v Dimura*, 104 AD3d 796, 796-797; *Lucido v Mancuso*, 49 AD3d 220, 226-227). "Notably, unless coupled with significant prejudice to plaintiff, even inordinate delay is not a barrier to amendment" (*Endicott Johnson Corp. v Konik Indus.*, 249 AD2d 744, 744; *see Edenwald Contr. Co. v City of New York*, 60 NY2d 957, 959).

The burden of proving prejudice is on the party opposing the motion for leave to amend the pleading (*see Kimso Apts., LLC v Ghandi*, 24 NY3d 403, 411; *Caceras v Zorbas*, 74 NY2d 884, 885). Prejudice, in this context, is more than "the mere exposure of the [party] to greater liability" (*Loomis v Civetta Corinno Constr. Corp.*, 54 NY2d 18, 23; *see Kimso Apts., LLC v Ghandi*, 24 NY3d at 411). Furthermore, prejudice that may be remedied "by the award of costs, or a continuance, or some other sanction" will generally not provide grounds for the outright denial of a motion for leave to amend (5 Weinstein-Korn-Miller, NY Civ Prac: CPLR ¶ 3018.18; *see* CPLR 3025[b]; *Kalish v Manhasset Med. Ctr. Hosp.*, 100 AD2d 507, 508; *Campbell v La Forgia Oil Co.*, 81 AD2d 824, 824). Rather, "there must be some indication that the [party] has been hindered in the preparation of [the party's] case or has been

prevented from taking some measure in support of [its] position" (*Loomis v Civetta Corinno Constr. Corp.*, 54 NY2d at 23; *see Kimso Apts., LLC v Ghandi*, 24 NY3d at 411; Federal Ins. Co. v Lakeville Pace Mech. Inc., 159 AD3d 469, 469; *Armstrong v Peat, Marwick, Mitchell & Co.*, 150 AD2d at 190; *A. J. Pegno Constr. Corp. v City of New York*, 95 AD2d at 656; *Surlak v Surlak*, 95 AD2d at 383-384; *cf. Edenwald Contr. Co. v City of New York*, 60 NY2d at 959).

In applying the foregoing principles to the facts of this case, we note that "[t]he general rule holds that an appellate court must apply the law as it exists at the time of its decision" (*Matter of Gardiner v Lo Grande*, 83 AD2d 614, 615; *see Matter of Boardwalk & Seashore Corp. [*6]v Murdock*, 286 NY 494, 498; *see also Thorpe v Hous. Auth. of Durham*, 393 US 268, 281). Accordingly, we consider RPAPL 1302-a in connection with the present appeal, even though that statute had not been enacted at the time the order appealed from was decided by the Supreme Court (*see* L 2019, ch 739, § 1).

Under the circumstances of this case, it is clear that the Supreme Court should have permitted the defendant to raise the affirmative defense of lack of standing and to amend his answer to include it, even though he failed to plead it as an affirmative defense in his answer (*see* CPLR 3025[b]; *see also* RPAPL 1302-a; *cf. HSBC Bank USA, N.A. v Szoffer*, 149 AD3d at 1401). In addressing this issue, the plaintiff failed to allege, much less demonstrate, that it suffered any prejudice as a result of the defendant's delay in interposing the defense (*see DLJ Mtge. Capital, Inc. v David*, 147 AD3d at 1025; *U.S. Bank, N.A. v Sharif*, 89 AD3d at 724). Under the circumstances, the Supreme Court should have deemed the defendant's answer amended to include the affirmative defense of lack of standing (*see Barrett v Kasco Constr. Co.*, 56 NY2d at 831; *Adsit v Quantum Chem. Corp.*, 199 AD2d at 900).

"CPLR 3212(b) requires the proponent of a motion for summary judgment to demonstrate the absence of genuine issues of material fact on every relevant issue raised by the pleadings, including any affirmative defenses" (*Stone v Continental Ins. Co.*, 234 AD2d 282, 284; *see Morley Maples, Inc. v Dryden Mut. Ins. Co.*, 130 AD3d 1413, 1413; *Aimatop Rest. v Liberty Mut. Fire Ins. Co*, 74 AD2d 516, 517; *see also Sokolow, Dunaud, Mercadier, & Carreras v Lacher*, 299 AD2d 64, 70). Accordingly, where, as here, a court deems the defendant's answer amended to include the affirmative defense of lack of standing in opposition to a plaintiff's motion for summary judgment, a plaintiff must establish its standing in order to be entitled to summary judgment on the complaint (*see* CPLR 3212[b]; *see*

generally M & T Bank v Barter, 186 AD3d 698, 700; *Nationstar Mtge., LLC v Medley*, 168 AD3d 959, 960; *Security Lending, Ltd. v New Realty Corp.*, 142 AD3d 986, 987).

To establish prima facie entitlement to judgment as a matter of law in an action to foreclose a mortgage, a plaintiff must produce the mortgage, the unpaid note, and evidence of default (*see Deutsche Bank Trust Co. Ams. v Garrison*, 147 AD3d 725, 726; *Deutsche Bank Natl. Trust Co. v Abdan*, 131 AD3d 1001, 1002; *Plaza Equities, LLC v Lamberti*, 118 AD3d 688, 689). A plaintiff establishes its standing in a mortgage foreclosure action by demonstrating that, when the action was commenced, it was either the holder of, or the assignee of, the underlying note (*see Aurora Loan Servs., LLC v Taylor*, 25 NY3d 355, 361-362; *Nationstar Mtge., LLC v Medley*, 168 AD3d at 960). "Either a written assignment of the underlying note or the physical delivery of the note prior to the commencement of the foreclosure action is sufficient to transfer the obligation, and the mortgage passes with the debt as an inseparable incident" (*U.S. Bank, N.A. v Collymore*, 68 AD3d 752, 754; *see Deutsche Bank Natl. Trust Co. v Adlerstein*, 171 AD3d 868, 870; *Nationstar Mtge., LLC v Rodriguez*, 166 AD3d 990, 992).

Here, in support of its motion, inter alia, for summary judgment on the complaint insofar as asserted against the defendant, the plaintiff produced the mortgage, the unpaid note, and evidence of default. Since the issue of standing was raised for the first time in opposition to the plaintiff's motion for summary judgment, the plaintiff was entitled to submit evidence on that issue for the first time in its reply papers. The plaintiff's submissions demonstrated, prima facie, that it had physical possession of the note and mortgage prior to the commencement of this action. In opposition, the defendant failed to raise a triable issue of fact. The defendant did not dispute the evidence submitted by the plaintiff to establish that it had physical possession of the note and mortgage prior to the commencement of this action. Rather, the standing defense raised by the defendant related solely to the validity of certain assignments of the note and mortgage. "Since the plaintiff does not base its claim of standing on an assignment of the note, but on its purported physical possession thereof, the [defendant's] arguments as to the validity of the assignment of mortgage and the correction assignment of mortgage are irrelevant" and insufficient to raise a triable issue of fact in opposition to the plaintiff's prima facie showing (*Deutsche Bank Natl. Trust Co. v Dennis*, 181 AD3d 864, 869; *see Aurora Loan Servs., LLC v Taylor*, 25 NY3d at 361-362; *Wells Fargo Bank, N.A. v Davis*, 181 AD3d 890, 892).

The defendant's remaining contentions are without merit.

In view of the foregoing, we agree with the Supreme Court's determination to grant leave to reargue and, upon reargument, grant the plaintiff's motion, inter alia, for summary judgment on the complaint insofar as asserted against the defendant. Accordingly, the order appealed from is [*7]affirmed.

ROMAN, J.P., MALTESE and IANNACCI, JJ., concur.

ORDERED that the order dated June 19, 2017, is affirmed, with costs.

ENTER:

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Clerk of the Court

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COVID hardship forbearance

Forbearance (https://www.consumerfinance.gov/ask-cfpb/what-is-forbearance-en-289/) is when your mortgage servicer or lender allows you to pause (suspend) or reduce your mortgage payments for a limited time while you build back your finances.

If you experience financial hardship due to the coronavirus pandemic, you may have a right to an initial COVID hardship forbearance of up to 180 days. You also may have the right to one or more extensions of that forbearance. You must request these options – they're not automatic!

If your loan is backed by HUD/FHA, USDA, or VA, the deadline for requesting an *initial* forbearance is June 30, 2021. If your loan is backed by Fannie Mae or Freddie Mac, there is not currently a deadline for requesting an *initial* forbearance.

You must contact your loan servicer to request this forbearance. There will be no additional fees, penalties, or additional interest (beyond scheduled amounts) added to your account. You do not need to submit additional documentation to qualify other than your claim to have a pandemic-related financial hardship. If you are facing financial hardships, you should ask for forbearance immediately.

If you already have a forbearance plan and need more time, you can request an extension. If your mortgage is backed by Fannie Mae, Freddie Mac, or the federal government, you are entitled to a 180-day extension of your COVID hardship forbearance if you request it.

In addition:

- **If your mortgage is backed by Fannie Mae or Freddie Mac** (https://www.fhfa.gov/Media/PublicAffairs/Pages/FHFA-Extends-COVID-19-Forbearance-Period-and-Foreclosure-and-REO-Eviction-Moratoriums.aspx): You may request up to two additional three-month extensions, up to a maximum of 18 months of total forbearance. But to qualify, you **must** be in a COVID forbearance plan as of February 28, 2021, so don't delay contacting your servicer if you're having trouble paying your mortgage and are not in a forbearance plan.
- **If your mortgage is backed by HUD/FHA** (https://www.hud.gov/press/press_releases_media_advisories/hud_no_21_023)**, USDA** (https://www.usda.gov/media/press-releases/2021/02/16/biden-administration-announces-another-foreclosure-moratorium-and#:~:text=Forbearance%20Options&text=In%20addition%2C%20the%20initial%20forbearance,later%20than%20June%2030%2C%202021)**, or VA** (https://blogs.va.gov/VAntage/84744/va-extends-existing-moratoriums-evictions-foreclosures-extends-loan-forbearance-opportunities/): You may request up to two additional three-month extensions, up to a maximum of 18 months of total forbearance. But to qualify, you must have started a forbearance plan on or before June 30, 2020. Not all borrowers will qualify for the maximum. Check with your servicer about the options available.

Seven things you should know about mortgage forbearance during the COVID-19 national emergency (https://www.consumerfinance.gov/coronavirus/mortgage-and-housing-assistance/mortgage-forbearance-during-covid-19-what-know-what-do/)

Forbearance doesn't mean your payments are forgiven or erased. You are still required to repay any missed or reduced payments in the future, which in most cases may be repaid over time. At the end of the forbearance, your servicer will contact you about how the missed payments can be repaid. There may be different programs available.

Make sure you understand how the forbearance will be repaid (https://www.consumerfinance.gov/coronavirus/mortgage-and-housing-assistance/after-you-receive-relief/). There can be different forbearance programs or options, depending on the type of your loan.

For example, you won't have to pay back the amount that was suspended all at once if you have a Fannie Mae, Freddie Mac, HUD/FHA, VA, or USDA loan—unless you are able to do so.

If your income is restored before the end of your forbearance, reach out to your servicer and resume making payments as soon as you can to reduce the amount you owe later.

If you want to learn more

If forbearance is available to you, read our guide to help you make the best decision based on your situation (https://www.consumerfinance.gov/ask-cfpb/what-is-forbearance-en-289/).

Foreclosure moratoriums

Foreclosure (https://www.consumerfinance.gov/ask-cfpb/how-does-foreclosure-work-en-287/) is when the lender takes back the property after the homeowner fails to make required payments on a mortgage.

Foreclosure processes differ by state. Under federal law, a servicer generally cannot start the state foreclosure process until your loan is more than 120 days past due (https://www.consumerfinance.gov/ask-cfpb/i-cant-make-my-mortgage-payments-how-long-will-it-take-before-i ll-face-foreclosure-en-1849/). There can be exceptions depending on your forbearance or other relief (often called "loss mitigation programs").

Foreclosure moratoriums suspend or stop foreclosure.

If your loan is backed by Fannie Mae, Freddie Mac, HUD/FHA, USDA, or VA, your lender or loan servicer cannot foreclose on you until after June 30, 2021.

Specifically, the guidance from Fannie Mae and Freddie Mac, HUD/FHA, VA, and USDA, prohibit lenders and servicers from beginning a judicial or non-judicial foreclosure against you, or from finalizing a foreclosure judgment or sale. This protection began on March 18, 2020.

Some states and local governments have temporarily stopped foreclosures. Check your state's government website for details (https://www.usa.gov/states-and-territories).

If you want to learn more

Your servicer can work with you to avoid foreclosure (https://www.consumerfinance.gov/ask-cfpb/does-my-mortgage-servicer-have-to-help-me-avoid-foreclosure-en-1803/).

The Homeowner's Guide to Success (https://www.consumerfinance.gov/documents/5940/cfpb_mortgages_homeowners-guide-to-success.pdf) explains the federal law and what to do if you can't pay your mortgage.

What to do next

You must determine who owns or backs your mortgage to see if one of these mortgage relief options may be available.

Find out which mortgage relief options and protections you may qualify for (https://www.consumerfinance.gov/coronavirus/mortgage-and-housing-assistance/mortgage-relief-do-i-qualify/)

FEDERAL CORONAVIRUS RESOURCES

White House Coronavirus Task Force

Information about COVID-19 from the White House Coronavirus Task Force in conjunction with CDC, HHS, and other agency stakeholders.
Visit coronavirus.gov (https://www.coronavirus.gov/)

USAGov

Information on what the U.S. Government is doing in response to COVID-19.
Visit usa.gov (English) (https://www.usa.gov/coronavirus)
Visit usa.gov (Spanish) (https://www.usa.gov/espanol/coronavirus)

Page last modified: February 16, 2021

Loan modifications and forbearance during the COVID-19 crisis

Real Estate Alert

COVID-19 Alert

28 April 2020
By: Jarrid King

The coronavirus disease 2019 (COVID-19) has created a devastating and unprecedented health and economic crisis that will forever change the way we live. The pandemic has pushed the world into a recession that is worse than the global financial crisis and on a scale not seen since World War II.

Disruptions caused by the virus are upending the real estate industry. For example, the pandemic has accelerated online shopping demand, with the concomitant demise of brick and mortar retail, while causing us to rethink how we view ongoing trends for the densification of work and living space.

From tenants to landlords to lenders, COVID-19's impact has been devastating, and both states and the federal government have implemented changes to real estate policy in an attempt to lessen the burden. In the context of commercial real estate lending, these changes clearly favor loan modifications and forbearance over foreclosure, and with the next round of missed loan payments coming in May, borrowers and lenders need to be aware of the breadth of such changes.

State-level guidance

Many states and the District of Columbia have enacted legislation or issued emergency orders to promote loan modifications and forbearance.

For example, New York Governor Andrew M. Cuomo signed Executive Order 202.8 (EO 202.8) and Executive Order 202.9 (EO 202.9) on March 20 and 21, 2020, respectively, as part of a series of executive orders aimed at providing relief to businesses affected by the crisis. Given New York's standing as the financial industry epicenter and the fact that many financial institutions are subject to New York law and regulators, the New York governor's executive orders have broad implications and are an appropriate focus for our state-level analysis.

While the New York Department of Financial Services regulations issued pursuant to EO 202.9 on March 24, 2020 (*Emergency Relief for New Yorkers Who Can Demonstrate Financial Hardship as a Result of COVID-19*, 119 NYCRR 3) clarify that the regulations do not apply to foreclosures on commercial mortgages, the bar on such foreclosures remains subject to EO 202.8. EO 202.8 provides that lenders cannot proceed with commercial mortgage foreclosures on New York properties for a period of 90 days, and recommends, but does not require, that lenders refrain from exercising other remedies (*eg*, charging late fees) during such 90-day period.

Federal guidance for banks and credit unions

In addition to the efforts of various states, federal regulators, including The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, the Consumer Financial Protection Bureau and the State Banking Regulators issued a statement on April 7, 2020 to provide guidance to financial institutions who are working with borrowers affected by COVID-19.

The guidance encourages financial institutions (including national banks and credit unions) to work constructively with borrowers that are unable to meet their contractual payment obligations due to the crisis and provides that the agencies view loan modifications as a positive step in order to mitigate the negative effects of the pandemic on borrowers. The guidance confirms that the agencies will not criticize such actions. Under the guidance, the agencies will not direct financial institutions to automatically classify COVID-19-related loan modifications as troubled debt restructurings (TDRs) − this includes short-term loan modifications such as payment deferrals, fees waivers or extensions of repayment terms.

By way of background, the TDR designation is an accounting categorization, as promulgated by the Financial Accounting Standards Board (FASB) and codified within Accounting Standards Codification (ASC) Subtopic 310-40, Receivables – Troubled Debt Restructurings by Creditors (ASC 310-40). Since classifying loan modifications as TDRs could have a significant negative impact on a bank's financial statements, and since not all loan restructurings will result in TDRs, the agencies have attempted to provide guidance on the type of restructurings that do not result in TDRs in order to encourage financial institutions to provide borrowers that are negatively impacted by the COVID-19 outbreak with certain payment accommodations.

A restructuring of a debt constitutes a TDR if the creditor, for economic or legal reasons related to the debtor's financial difficulties, grants a concession that it would not otherwise consider. FASB has confirmed that short-term (*eg,* six months) modifications (such as payment deferrals, fee waivers, extensions of repayment terms or other delays in payment that are insignificant) made on a good faith basis in response to the pandemic to borrowers that were current prior to such relief do not constitute TDRs. According to the agencies, financial institutions may presume that borrowers that are current on payments are not experiencing financial difficulties at the time of the modification for purposes of determining TDR status, and accordingly no further TDR analysis is required. Consistent with the state-level guidance, the federal guidance is designed to promote loan modifications and forbearance.

Insurance company guidance

On March 27, 2020, the Financial Condition (E) Committee (Committee) of the National Association of Insurance Commissioners (NAIC) issued guidance encouraging insurers to work with borrowers who are or who may become unable to meet their contractual payment obligations because of the effects of COVID-19. The March 27, 2020 pronouncement supports the use of loan modifications that can mitigate the consequences of the pandemic.

A life insurance company's ability to make appropriate business decisions in order to address borrower requests for temporary relief due to the impact of the virus is impaired by uncertainty surrounding accounting and risk-based capital (RBC) consequences of those actions. The Committee's guidance addresses this uncertainty. The guidance applies to a TDR issued as a result of COVID-19 and is applicable to the term of the loan modification, but solely with respect to a modification, including a forbearance agreement, an interest rate modification, etc., that occurs during the applicable reporting period for a loan that was not more than 30 days past due as of December 31, 2019.

For any RBC calculations for March 31, 2020 and June 30, 2020, all direct mortgages and Schedule BA mortgages for which the insurer chooses, or are mandated by the government, to allow delays in any required principal and interest payments are not required to be reclassified to a different RBC category (*eg*, will not affect the origination date, valued date and net operating income or be treated as delinquent) than was utilized for the December 31, 2019 RBC filing and which may have otherwise required a higher capital charge for such a mortgage.

For reporting of any NAIC designations in March 31, 2020 and June 30, 2020 financial statements, or any RBC calculations by insurers for March 31, 2020 and June 30, 2020, all commercial mortgage-backed securities (CMBS) and residential mortgage-backed securities (RMBS) modeled by the NAIC for year-end 2019 and for which any required debt service payments have been deferred in accordance with the Committee's guidance may be reported with the same NAIC designation as year-end 2019.

IRS guidance for CMBS

In response to these developments, the Internal Revenue Service (IRS) on April 13, 2020, issued rules (IRS Rules) to help promote loan modifications when a loan is held in a mortgage-backed security. This guidance is designed to protect against adverse tax consequences for the bondholders that may arise as a result of any loan modifications or forbearance, and is consistent with the steps taken by states, the federal government and the insurance industry.

Among other things, these IRS Rules provide new safe harbors that extend to real estate mortgage investment conduits (REMICs) and investment trusts affected by mortgage loan payment forbearances of three to six months and related modifications occurring between March 27, 2020 and December 31, 2020, and apply to mortgage loan forbearance that is provided voluntarily by the mortgage holder or servicer, any state-mandated forbearance, and forbearance that is mandated in the Coronavirus Aid, Relief, and Economic Security Act. The IRS Rules provide that REMICs and investment trusts can grant forbearance relief to affected borrowers, and can acquire mortgage loans for which such forbearance is already in place without adverse tax consequences or threatening their REMIC tax status.

During these unprecedented times, state and federal regulators, and the insurance industry, are encouraging lenders to negotiate loan modifications and forbearance with affected borrowers in lieu of immediately enforcing remedies.

If you have any questions, please contact any member of DLA Piper's Real Estate group or your DLA Piper relationship attorney.

Please visit our Coronavirus Resource Center and subscribe to our mailing list to receive alerts, webinar invitations and other publications to help you navigate this challenging time.

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Mortgages Forbearance Vs. Deferment - What's The Difference (And Which Is Right For You)?

Written by
Rosemary Carlson
Modified date: December 3, 2020

If you are struggling with paying your mortgage due to COVID19 or other reasons, mortgage forbearance or mortgage deferment may be your solution.

Do you own your home? Are you having trouble paying your mortgage payment? You may be a good candidate for mortgage forbearance or mortgage deferment.

In late February to early March 2020, the COVID19 virus started to sweep the world. One

What is mortgage forbearance?

You suspend your payments for a period of time

In a general sense, mortgage forbearance is for homeowners who are either delinquent on their mortgage payments or know they are going to be delinquent in the future due to a temporary hardship. That hardship could be for financial or medical reasons. Usually,

Each lender has their own terms for mortgage forbearance. You will sign an agreement that will state your obligations under the forbearance agreement. Read the agreement carefully and be sure you can repay the payments you miss on the schedule the lender specifies. Most lenders are willing to negotiate with you.

Forbearance is only for certain situations

Mortgage forbearance is a temporary solution that you can use if you can't pay your mortgage payments due to a medical emergency, financial hardship, or natural disaster. If there is some other reason that you are finding it difficult to pay your mortgage payments, such as an interest rate that is too high or payments that are too big, then you need to negotiate some other type of mortgage loan with your lender.

Mortgage forbearance will help protect your credit since your mortgage lender has agreed that you will miss a certain number of mortgage payments. If you have a forbearance agreement, the lender is not obligated to report it to the credit bureaus. If they do report it, it will not be viewed as negatively as a foreclosure or skipping mortgage payments.

What is mortgage deferment?

You pay back the money at the end of your mortgage loan

of the loan time period. Due to the COVID19 crisis, mortgage forbearance plans are often offering the same type of payment plans.

The term “mortgage deferment” is actually seldom used. You hear “deferment” used more often with regard to student loans. With mortgages, the only difference in forbearance and deferment is at the end of the period when your mortgage payments are delayed.

Qualifying for forbearance and deferment

The terms mortgage forbearance and mortgage deferment are often used interchangeably, as they do have the same qualifiers. In order to qualify for these programs:

- the home must be your principal residence.
- You can’t vacate the home permanently.
- You must have a certain expense-to-income ratio stated by the bank.
- Your monthly expenses must be a certain percentage of your monthly income.

The eligibility period for a forbearance or deferment is usually not more than one year, although it may be longer due to COVID19. It is determined by the lender.

Index Number (if known/applicable): County and Court (if known/applicable):

NOTICE TO MORTGAGOR:

If you have lost income or had increased costs during the COVID-19 pandemic, and you sign and deliver this hardship declaration form to your mortgage lender or other foreclosing party, you cannot be foreclosed on until at least May 1, 2021. If your mortgage lender or other foreclosing party provided you with this form, the mortgage lender or other foreclosing party must also provide you with a mailing address and e-mail address to which you can return this form. If you are already in foreclosure proceedings, you may return this form to the court. You should keep a copy or picture of the signed form for your records. You will still owe any unpaid mortgage payments and lawful fees to your lender. You should also keep careful track of what you have paid and any amount you still owe.

MORTGAGOR'S DECLARATION OF COVID-19-RELATED HARDSHIP

I am the mortgagor of the property at (address of dwelling unit):

Including my primary residence, I own, whether directly or indirectly, ten or fewer residential dwelling units. I am experiencing financial hardship, and I am unable to pay my mortgage in full because of one or more of the following:

1. Significant loss of household income during the COVID-19 pandemic.
2. Increase in necessary out-of-pocket expenses related to performing essential work or related to health impacts during the COVID-19 pandemic.

3. Childcare responsibilities or responsibilities to care for an elderly, disabled, or sick family member during the COVID-19 pandemic have negatively affected my ability or the ability of someone in my household to obtain meaningful employment or earn income or increased my necessary out-of-pocket expenses.

4. Moving expenses and difficulty I have securing alternative housing make it a hardship for me to relocate to another residence during the COVID-19 pandemic.

5. Other circumstances related to the COVID-19 pandemic have negatively affected my ability to obtain meaningful employment or earn income or have significantly reduced my household income or significantly increased my expenses.

6. One or more of my tenants has defaulted on a significant amount of their rent payments since March 1, 2020.

To the extent I have lost household income or had increased expenses, any public assistance, including unemployment insurance, pandemic unemployment assistance, disability insurance, or paid family leave, that I have received since the start of the COVID-19 pandemic does not fully make up for my loss of household income or increased expenses.

I understand that I must comply with all other lawful terms under my mortgage agreement. I further understand that lawful fees, penalties or interest for not having paid my mortgage in full as required by my mortgage agreement may still be charged or collected and may result in a monetary judgment against me. I also understand that my mortgage lender or other foreclosing party may pursue a foreclosure action against me on or after May 1, 2021, if I do not fully repay any missed or partial payments and lawful fees.

Signed: _____

Printed name: _____

Date signed: _____

NOTICE: You are signing and submitting this form under penalty of law. That means it is against the law to make a statement on this form that you know is false.

NOTICE TO TENANT:

If you have lost income or had increased costs during the COVID-19 pandemic, or moving would pose a significant health risk for you or a member of your household due to an increased risk for severe illness or death from COVID-19 due to an underlying medical condition, and you sign and deliver this hardship declaration form to your landlord, you cannot be evicted until at least May 1, 2021 for nonpayment of rent or for holding over after the expiration of your lease. You may still be evicted for violating your lease by persistently and unreasonably engaging in behavior that substantially infringes on the use and enjoyment of other tenants or occupants or causes a substantial safety hazard to others.

If your landlord has provided you with this form, your landlord must also provide you with a mailing address and e-mail address to which you can return this form. If your landlord has already started an eviction proceeding against you, you can return this form to either your landlord, the court, or both at any time. You should keep a copy or picture of the signed form for your records. You will still owe any unpaid rent to your landlord. You should also keep careful track of what you have paid and any amount you still owe.

For more information about legal resources that may be available to you, go to www.nycourts.gov/evictions/nyc/ or call 718-557-1379 if you live in New York City or go to www.nycourts.gov/evictions/outside-nyc/ or call a local bar association or legal services provider if you live outside of New York City. Rent relief may be available to you, and you should contact your local housing assistance office.

Index Number (if known/applicable): _____

County and Court (if known/applicable): _____

TENANT'S DECLARATION OF HARDSHIP DURING THE COVID-19 PANDEMIC

I am a tenant, lawful occupant, or other person responsible for paying rent, use and occupancy, or any other financial obligation under a lease or tenancy agreement at (address of dwelling unit):

_____

YOU MUST INDICATE BELOW YOUR QUALIFICATION FOR EVICTION PROTECTION BY SELECTING OPTION "A" OR "B", OR BOTH.

☐ A. I am experiencing financial hardship, and I am unable to pay my rent or other financial obligations under the lease in full or obtain alternative suitable permanent housing because of one or more of the following:

1. Significant loss of household income during the COVID-19 pandemic.

2. Increase in necessary out-of-pocket expenses related to performing essential work or related to health impacts during the COVID-19 pandemic.

3. Childcare responsibilities or responsibilities to care for an elderly, disabled, or sick family member during the COVID-19 pandemic have negatively affected my ability or the ability of someone in my household to obtain meaningful employment or earn income or increased my necessary out-of-pocket expenses.

4. Moving expenses and difficulty I have securing alternative housing make it a hardship for me to relocate to another residence during the COVID-19 pandemic.

must submit an annual summary of such evaluations to the Office of Court Administration. Thank you for helping us to comply with these rules.

5. Other circumstances related to the COVID-19 pandemic have negatively affected my ability to obtain meaningful employment or earn income or have significantly reduced my household income or significantly increased my expenses.

To the extent that I have lost household income or had increased expenses, any public assistance, including unemployment insurance, pandemic unemployment assistance, disability insurance, or paid family leave, that I have received since the start of the COVID-19 pandemic does not fully make up for my loss of household income or increased expenses.

☐ B. Vacating the premises and moving into new permanent housing would pose a significant health risk because I or one or more members of my household have an increased risk for severe illness or death from COVID-19 due to being over the age of sixty-five, having a disability or having an underlying medical condition, which may include but is not limited to being immunocompromised.

I understand that I must comply with all other lawful terms under my tenancy, lease agreement or similar contract. I further understand that lawful fees, penalties or interest for not having paid rent in full or met other financial obligations as required by my tenancy, lease agreement or similar contract may still be charged or collected and may result in a monetary judgment against me. I further understand that my landlord may be able to seek eviction after May 1, 2021, and that the law may provide certain protections at that time that are separate from those available through this declaration.

Signed: _____

Printed name: _____

Date signed: _____

NOTICE: You are signing and submitting this form under penalty of law. That means it is against the law to make a statement on this form that you know is false.

Inns of Court Document list (John P. Reali)

1. John Reali Bio
2. Chief Judge Administrative order re: Moratorium 12/31/20
3. Notice to Mortgagor form
4. Notice to Tenant form
5. Foreclosure case:(Deutsche Bank Natl. V- Burke) (defense re: proof of allonge attached to note)
6. Foreclosure case: (Deutsche Bank Natl. V Feeney) (defense re: proof of mailing notice by person with actual knowledge of procedure is required)
7. Foreclosure case: GMAC Mtge LLC v. Coombs (failure to raise lack of standing in answer, not waived and can be raised at any time or amendment to pleading)
8. Copy of RPAPL Sec: 1302 -a
9. Judge Bluth Decision 204 E. 38th LLC v. Sons of Thunder LLC upholding constitutionality of NY City Admin. Code 22-1005 baring suit on personal guaranty on lease
10. Judge Bluth Decision (27 Morton L.P v. MDS Fashions, Ltd.) indicating non enforceability of personal guaranty of lease is retroactive
11. Judge Bluth Decision (CP Associates v Concourse Family Dental) ,permitting action to recover rent (not seeking eviction) is permissible
12. Judge Kelley Decision (188 Ave A. Takeout v. Lucky Jab Realty) stating, in action for Yellowstone Injunction, pandemic constitutes a "casualty" under the lease, and since Landlord is responsible to "restore the premises" Landlord can not proceed to terminate lease or evict tenant:.
13. Town of Oyster Bay Code: 96-21 to 24 re: Registration and maintenance of real property with mortgage in default

As of 01/04/2021 11:46AM, the Laws database is current through 2020 Chapters 1-387

Real Property Actions and Proceedings

§ 1302-a. Defense of lack of standing; not waived. Notwithstanding the provisions of subdivision (e) of rule thirty-two hundred eleven of the civil practice law and rules, any objection or defense based on the plaintiff's lack of standing in a foreclosure proceeding related to a home loan, as defined in paragraph (a) of subdivision six of section thirteen hundred four of this article, shall not be waived if a defendant fails to raise the objection or defense in a responsive pleading or pre-answer motion to dismiss. A defendant may not raise an objection or defense of lack of standing following a foreclosure sale, however, unless the judgment of foreclosure and sale was issued upon defendant's default.

~~manner as provided in § 96-19 hereof.~~

§ 96-21 Registration of real property with mortgage-in-default.

[Added 1-29-2019 by L.L. No. 2-2019[1]; 4-21-2020 by L.L. No. 1-2020]

A. This section shall be considered cumulative and not superseding or subject to any other law or provision for same, but shall rather be an additional remedy available to the Town, above and beyond any other state, county and/or local provisions for same. This section relates to property subject to a mortgage which has been determined by the mortgagee to be in default.

B. Within 10 days of the date that the mortgagee declares its mortgage on a particular parcel of real property to be in default, the mortgagee shall inspect the premises and register the real property with the Town's mortgage-in-default registry, which said registry shall be maintained by the Department of Planning and Development. The mortgagee shall include in the registration if the property is vacant or occupied.

C. If the property is occupied but remains in default, it shall be inspected by the mortgagee, or said mortgagee's designee, monthly until the mortgagor or other party remedies the default.

D. Registration pursuant to this section shall contain the name of the mortgagee and mortgage servicer; the direct mailing address, email address and telephone number of the mortgagee and servicer; the name and address, email address and telephone number of a local property manager who shall be responsible for the inspection, security and maintenance of the property. The local property manager named in the registration shall be located and available within Nassau and Suffolk Counties to be contacted by the Town, Monday through Friday, between 9:00 a.m. and 5:00 p.m., holidays and lunch hours excepted.

E. A semiannual, nonrefundable fee in the amount of $500 per property shall accompany the mortgage-in-default registration form(s). An additional fee of $500 shall be due and payable within 10 days of the expiration of the previous registration.

F. Each owner of an individual property on the registry that has been registered as required prior to the effective date shall renew the registration and pay the nonrefundable $500 semiannual registration fee within 10 days of the current registration's expiration. Properties registered after the effective date shall renew the registration every six months from the expiration of the original registration renewal date and shall pay the nonrefundable $500 semiannual registration fee.

G. If the foreclosing or foreclosed property is not registered, or the registration fee is not paid within 30 days of when the registration or renewal is required pursuant to this section, a late fee equivalent to 10% of the semiannual registration fee shall be charged for every thirty-day period or portion thereof that the property is not registered and shall be due and payable with the registration.

H. This section shall also apply to properties that have been the subject of foreclosure sale where the title was transferred to the beneficiary of a mortgage involved in the foreclosure and any properties transferred under a deed in lieu of foreclosure/sale.

I. Properties subject to this section shall remain under the semiannual mortgage-in-default registration requirement, inspection, security, and maintenance standards of this section as long as they remain in default.

J. Any person or other legal entity that has registered a property under this section must report any change of information contained in the registration within 10 days of the change.

K. Failure of the mortgagee and/or property owner of record to properly register or revise the registration from time to time to reflect a change of circumstances as required by the Town's Department of Planning and Development shall be a violation of this section.

[1] *Editor's Note: This local law also renumbered former §§ 96-21 through 96-24 as §§* **96-24**, **96-25**, **96-26**, **96-22**, *and* **96-23**, *respectively.*

§ 96-21.1 Maintenance requirements.

[Added 1-29-2019 by L.L. No. 2-2019]

A. Properties subject to this section shall be kept free of weeds, overgrown brush, dead vegetation, trash, junk, debris, wildlife, vermin, building materials, any accumulation of newspapers, circulars, flyers, notices (except those required by federal, state, or local law), discarded personal items, including, but not limited to, furniture, clothing, large and small appliances, printed material or any other items that give the appearance that the property is abandoned or not being properly maintained.

B. The property shall be maintained free of graffiti or similar markings by removal or painting over with an exterior grade paint that matches the color of the exterior structure.

C. Yards shall be landscaped and maintained pursuant to the standards previously established in this Code.

D. Pools and spas shall be kept in working order so that pool and spa water remains free and clear of pollutants and debris and insects. Pools and spas shall comply with the enclosure requirements and any other requirements of this Code and the New York State Building Code and New York State Property Maintenance Code, as amended from time to time.

E. Failure of the mortgagee and/or property owner of record to properly maintain the property is a violation of the Town Code and may result in citation by the Town's Department of Planning and Development.

§ 96-21.2 Security requirements.

[Added 1-29-2019 by L.L. No. 2-2019]

A. Properties subject to this section shall be maintained in a secure manner so as not to be accessible to unauthorized persons.

B. A "secure manner" shall include, but not be limited to, the closure and locking of windows, doors, gates and other openings of such size that may allow a child to access the interior of the property and/or structure. Broken windows shall be secured by reglazing or boarding of the window with polycarbonate sheeting of a thickness in excess of 3/16 inch.

C. If a mortgage on property is in default and has become vacant, the local property manager or mortgagee must perform weekly inspections to verify compliance with the requirements of this section and any other applicable laws or Town ordinances.

D. Failure of the mortgagee and/or property owner of record to properly inspect and secure the property, and post and maintain the signage noted in this section, is a violation of this Code and may result in a citation by the Town's Department of Planning and Development.

§ 96-21.3 Immunity.

[Added 1-29-2019 by L.L. No. 2-2019]

Any Code Enforcement Inspector, or any person authorized by the Department of Planning and Development to enforce Town Code, shall be immune from prosecution, civil or criminal, for reasonable, good faith entrance upon real property while in the discharge of duties imposed by this section.

§ 96-21.4 Additional authority.

[Added 1-29-2019 by L.L. No. 2-2019]

The Code Enforcement Inspector or any person authorized by the Department of Planning and Development to enforce Town Code, shall have authority to require the mortgagee and/or owner of record of any property affected by this section to implement additional maintenance and/or security measures including, but not limited to, securing any and all doors, windows or other openings, employment of an on-site security guard, or other measures as may be reasonably required to prevent a decline of the property. If the owner of the real property fails to take the maintenance and/or security measures required, the Commissioner of the Department of Planning and Development, or his/her designee, may direct Department of Planning and Development, the Highway Department, and/or Department of Parks to take such necessary measures, and the Town shall be reimbursed for said work in accordance with § 135-54 of the Town Code.

§ 96-22 Foreclosures; undertaking.

[Added 1-9-2018 by L.L. No. 2-2018]

Legislative intent: When residential properties in the Town of Oyster Bay fall vacant and become the subject of foreclosure actions, they frequently become neglected and overgrown with grass, weeds and rubbish, creating an unsightly appearance in the surrounding residential area and detracting from the use, enjoyment and value of surrounding properties. The Town of Oyster Bay is committed to using all legal avenues to proactively address these adverse conditions, to alleviate the burden these vacant properties impose on neighboring residents. This § 96-22 places the financial burden on any person, business, organization, bank or lender who commences a foreclosure action against any vacant residential property in the Town of Oyster Bay to deposit funds with the Town after the foreclosure action is commenced, for use in achieving prompt remediation, if or when it shall occur. This new section is clearly in the public interest. It will help deter violations by creating a financial disincentive against allowing the property to lie fallow and unmaintained. It will help to expedite remediation of overgrown grass, weeds and rubbish when they occur. It will also help avoid substantial outlays of public funds in accomplishing same.

A. Except as otherwise provided by law, any person, business, organization, bank or lender who commences a foreclosure action against a residential property (improved with a single-family, two-family or multiple-family residence) that has become vacant shall provide to the Town of Oyster Bay an undertaking in the form of cash, a cash bond, or a letter of credit acceptable to the Town Attorney, in the sum of $25,000, to secure the continued maintenance of the property free of any violations as provided for by Oyster Bay Town Code, during the entire time that vacancy shall exist, as determined by the Commissioner. When the foreclosure action is finally discontinued, any unused funds shall be returned upon written request of the party which commenced foreclosure, which request shall be made in writing to the Town Attorney within 90 days of the action's discontinuance.

B. It shall be unlawful for any such person, business, organization, bank or lender to fail to properly deposit such cash, a cash bond, or a letter of credit within 45 calendar days after the foreclosure action is commenced.

C. In the event that the Commissioner determines that any property referenced in Subsection A above is being maintained in violation of § 96-22 of this chapter, then, in addition to or in lieu of any other enforcement remedy at his/her disposal, the Commissioner may utilize the deposited funds to pay the full and actual cost of actions necessary to eliminate the violation.

D. In the event that any such funds are utilized as set forth above, such person, business, organization, bank or lender shall restore such funds to the full amount referenced in Subsection A above, within 15 calendar days after written demand by the Town of Oyster Bay, sent by regular mail and certified mail, return receipt requested, to such person, business, organization, bank or lender at an address designated by them for service of notices, or else to their last known address. It shall be unlawful for such person, business, organization, bank or lender to fail to timely restore funds as required herein.

E. In the event that the Commissioner determines that any property referenced in Subsection A above is being maintained in violation of § 96-22 of this chapter, and no cash, cash bond, or letter of credit acceptable to the Town Attorney has been provided or replenished as required by Subsection A or D above, then, in addition to or in lieu of any other enforcement remedy at his/her disposal, the Commissioner may serve a written demand upon such person, business, organization, bank

or lender to provide the required cash, cash bond, or letter of credit acceptable to the Town Attorney, within 10 days after the date of such written demand, subject to the following:

(1) The forty-five-day time allotment of Subsection B hereof is superseded;

(2) The written demand shall be served in any manner authorized to obtain personal service under Article 3 of the Civil Practice Law and Rules of the State of New York, or otherwise at applicable law; and

(3) In the event that no cash, cash bond, or letter of credit acceptable to the Town Attorney has been provided or replenished as required by Subsection A or D above, within 10 days after the date of such written demand, then such person, business, organization, bank or lender shall be subject to fines of up to triple the maximum amount set forth under § 96-24C of this chapter, with each calendar day of failure to timely provide same constituting a separate additional offense, as set forth under § 96-24B of this chapter.

F. If any provision of this § 96-22 is declared unenforceable for any reason by a court of competent jurisdiction, such declaration shall affect only that provision, and shall not affect the remainder of this section, which shall remain in full force and effect.

G. This § 96-22 shall apply to all foreclosures commencing after the effective date of this section. It is to be considered remedial legislation and shall be liberally construed so that substantial justice is done.

§ 96-23 Nonresidential foreclosures; undertaking.

[Added 1-9-2018 by L.L. No. 2-2018]

Legislative intent: When nonresidential properties in the Town of Oyster Bay fall vacant and become the subject of foreclosure actions, they frequently become neglected and overgrown with grass, weeds and rubbish, creating an unsightly appearance in the surrounding area and detract from the use, enjoyment and value of surrounding properties and impair the ability for people to, among other things, shop, conduct commerce, attend meetings or go to school in a safe, clear, and aesthetic environment. The Town of Oyster Bay is committed to using all legal avenues to proactively address these adverse conditions to alleviate the burden these vacant properties impose on a neighborhood. This § 96-23 places the financial burden on any person, business, organization, bank or lender who commences a foreclosure action against any vacant property in the Town of Oyster Bay not subject to the provisions of § 96-22 of this chapter to deposit funds with the Town after the foreclosure action is commenced, for use in achieving prompt remediation, if or when it shall occur. This section is clearly in the public interest. It will help deter violations by creating a financial disincentive against allowing the property to lie fallow and unmaintained. It will help to expedite remediation of overgrown grass, weeds and rubbish, when they occur. It will also help avoid substantial outlays of public funds in accomplishing same.

A. Except as otherwise provided by law, any person, business, organization, bank or lender who commences a foreclosure action against a property not subject to the requirements of § 96-22 of this chapter (including, among other property, commercial properties) that has become vacant, or subsequent parties of such an action, shall provide to the Town of Oyster Bay an undertaking in the form of cash, a cash bond, or a letter of credit acceptable to the Town Attorney, in the sum of $35,000, to secure the continued maintenance of the property free of any violations as provided for by the Oyster Bay Town Code, during the entire time that vacancy shall exist, as determined by the Commissioner. When the foreclosure action is finally discontinued, any unused funds shall be returned upon written request of the party which commenced foreclosure, which request shall be made in writing to the Town Attorney within 90 days of the action's discontinuance.

B. It shall be unlawful for any such person, business, organization, bank or lender to fail to properly deposit such cash, a cash bond, or a letter of credit within 45 calendar days after the foreclosure action is commenced.

C. In the event that the Commissioner determines that any property referenced in Subsection A above is being maintained in violation of § 96-23 of this chapter, then, in addition to or in lieu of any other enforcement remedy at his/her disposal, the Commissioner may utilize the deposited funds to pay the full and actual cost of actions necessary to eliminate the violation.

D. In the event that any such funds are utilized as set forth above, such person, business, organization, bank or lender shall restore it to the full amount referenced in Subsection A above, within 15 calendar days after written demand by the Town of Oyster Bay, sent by regular mail and certified mail, return receipt requested, to such person, business, organization,

bank or lender at an address designated by them for service of notices, or else to their last known address. It shall be unlawful for such person, business, organization, bank or lender to fail to timely restore funds as required herein.

E. In the event that the Commissioner determines that any property referenced in Subsection A above is being maintained in violation of § 96-23 of this chapter and no cash, cash bond, or letter of credit acceptable to the Town Attorney has been provided or replenished as required by Subsection A or D above, then in addition to or in lieu of any other enforcement remedy at his/her disposal, the Commissioner may serve a written demand upon such person, business, organization, bank or lender to provide the required cash, cash bond, or letter of credit acceptable to the Town Attorney, within 10 days after the date of such written demand, subject to the following:

(1) The forty-five-day time allotment of Subsection B hereof is superseded;

(2) The written demand shall be served in any manner authorized to obtain personal service under Article 3 of the Civil Practice Law and Rules of the State of New York, or otherwise at applicable law; and

(3) In the event that no cash, cash bond, or letter of credit acceptable to the Town Attorney has been provided or replenished as required by Subsection A or D above, within 10 days after the date of such written demand, then such person, business, organization, bank or lender shall be subject to fines of up to triple the maximum amount set forth under § 96-24C of this chapter and a minimum fine of $500 for each day of the noncompliance until such time as that person or entity complies with the provisions of this section, or by imprisonment for not more than 15 days, or by both such fine and imprisonment, with each calendar day of failure to timely provide same constituting a separate additional offense, as set forth under § 96-24B of this chapter.

F. If any provision of this section is declared unenforceable for any reason by a court of competent jurisdiction, such declaration shall affect only that provision, and shall not affect the remainder of this section, which shall remain in full force and effect.

G. This section shall apply to all nonresidential foreclosures commencing after the effective date of this section. It is to be considered remedial legislation and shall be liberally construed so that substantial justice is done.

§ 96-24 Penalties for offenses.

[Amended 1-9-2018 by L.L. No. 2-2018; 1-29-2019 by L.L. No. 2-2019]

A. Any person or persons other than those duly authorized by the Commissioner of Department of Planning and Development who shall remove from a building or structure any notice prescribed by this chapter prior to compliance with the orders contained in the notice or committing any offense against the provisions of § 96-18 of this chapter is guilty of a violation punishable by a fine not exceeding $500.

B. Any owner, occupant or lessee of any dangerous building or structure who shall fail to comply with any notice or administrative order to vacate shall be guilty of a violation punishable by a fine not exceeding $500.

C. Any person or persons who shall create a dangerous building or allow a building to become a dangerous building or allow a dangerous building to continue to remain in a dangerous condition, in violation of this chapter, shall be guilty of an offense punishable by a fine not exceeding $500, for conviction of a first offense; for conviction of a second offense, both of which were committed within a period of five years, punishable by a fine of not less than $1,000 nor more than $1,500; and upon conviction for a third or subsequent offense, all of which were committed within a period of five years, punishable by a fine of not less than $1,500 nor more than $2,500. However, for the purpose of conferring jurisdiction upon courts and judicial officers generally, violations of this chapter or of such ordinance or regulation shall be deemed misdemeanors and for such purpose only all provisions of law relating to misdemeanors shall apply to such violations. Each week's continued violation shall constitute a separate additional violation.

D. Any person, corporation, or entity who shall violate any of the provisions of this chapter or who shall fail to comply therewith or with any of the requirements thereof shall be guilty of a violation and, upon conviction thereof, a fine of not less than $500 nor more than $1,000 must be imposed. Each week's continued violation shall constitute a separate additional violation.

Rule 3002.1 Notice Relating to Claims Secured by Security Interest in the Debtor

(a) **In General**. This rule applies in a chapter 13 case to claims (1) that are secured by a security interest in the debtor's principal residence, and (2) for which the plan provides that either the trustee or the debtor will make contractual installment payments. Unless the court orders otherwise, the notice requirements of this rule cease to apply when an order terminating or annulling the automatic stay becomes effective with respect to the residence that secures the claim.

(b) **Notice of Payment Changes; Objection**. The holder of the claim shall file and serve on the debtor, debtor's counsel, and the trustee a notice of any change in the payment amount, including any change that results from an interest rate or escrow account adjustment, no later than 21 days before a payment in the new amount is due.

(1) *Notice*. The hold of the claim shall file and serve on the debtor, debtor's counsel, and the trustee a notice of any change that results in the payment amount, including any change that results from an interest-rate or escrow-account adjustment, not later than 21 days before a payment in the new amount is due. If the claim arises from a home-equity line of credit, this requirement may be modified by court order.

(2) *Objection*. A party in interest who objects to the payment change may file a motion to determine whether the change is required to maintain payments in accordance with § 1322(b)(5) of the Code. If no motion is filed by the day before the new amount is due, the change goes into effect, unless the court orders otherwise.

(c) **Notice of Fees, Expenses, and Charges**. The holder of the claim shall file and serve on the debtor, debtor's counsel, and the trustee a notice itemizing all fees, expenses, or charges (1) that were incurred in connection with the claim after the bankruptcy case was filed, and (2) that the holder asserts are recoverable against the debtor or against the debtor's principal residence. The notice shall be served within 180 days after the date on which the fees, expenses, or charges are incurred.

(d) **Form and Content**. A notice filed and served under subdivision (b) or (c) of this rule shall be prepared as prescribed by the appropriate Official Form, and filed as a supplement to the holder's proof of claim. The notice is not subject to Rule 3001(f).

(e) **Determination of Fees, Expenses, or Charges**. On motion of a party in interest filed within one year after service of a notice under subdivision (c) of this rule, the court shall, after notice and hearing, determine whether payment of any claimed fee, expense, or charge is required by the underlying agreement and applicable nonbankruptcy law to cure a default or maintain payments in accordance with § 1322(b)(5) of the Code.

(f) **Notice of Final Cure Payment**. Within 30 days after the debtor completes all payments under the plan, the trustee shall file and serve on the holder of the claim, the debtor, and debtor's counsel a notice stating that the debtor has paid in full the amount required to cure any default on the claim. The notice shall also inform the holder of its obligation to file and serve a response under subdivision (g). If the debtor contends that final cure payment has been made and all plan payments have been completed, and the trustee does not timely file and serve the notice required by this subdivision, the debtor may file and serve the notice.

(g) **Response to Notice of Final Cure Payment**. Within 21 days after service of the notice under subdivision (f) of this rule, the holder shall file and serve on the debtor, debtor's counsel, and the trustee a statement indicating (1) whether it agrees that the debtor has paid in full the amount required to cure the default on the claim, and (2) whether the debtor is otherwise current on all payments consistent with § 1322(b)(5) of the Code. The statement shall itemize the required cure or postpetition amounts, if any, that the holder contends remain unpaid as of the date of the statement. The statement shall be filed as a supplement to the holder's proof of claim and is not subject to Rule 3001(f).

(h) **Determination of Final Cure and Payment**. On motion of the debtor or trustee filed within 21 days after service of the statement under subdivision (g) of this rule, the court shall, after notice and hearing, determine whether the debtor has cured the default and paid all required postpetition amounts.

(i) **Failure to Notify**. If the holder of a claim fails to provide any information as required by subdivision (b), (c), or (g) of this rule, the court may, after notice and hearing, take either or both of the following actions:

(1) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or

(2) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure.

McKinney's Consolidated Laws of New York Annotated
Civil Practice Law and Rules (Refs & Annos)
Chapter Eight. Of the Consolidated Laws
Article 45. Evidence (Refs & Annos)

McKinney's CPLR § 4503

§ 4503. Attorney

Effective: November 20, 2019
Currentness

(a) 1. Confidential communication privileged. Unless the client waives the privilege, an attorney or his or her employee, or any person who obtains without the knowledge of the client evidence of a confidential communication made between the attorney or his or her employee and the client in the course of professional employment, shall not disclose, or be allowed to disclose such communication, nor shall the client be compelled to disclose such communication, in any action, disciplinary trial or hearing, or administrative action, proceeding or hearing conducted by or on behalf of any state, municipal or local governmental agency or by the legislature or any committee or body thereof. Evidence of any such communication obtained by any such person, and evidence resulting therefrom, shall not be disclosed by any state, municipal or local governmental agency or by the legislature or any committee or body thereof. The relationship of an attorney and client shall exist between a professional service corporation organized under article fifteen of the business corporation law to practice as an attorney and counselor-at-law and the clients to whom it renders legal services.

2. Personal representatives. (A) For purposes of the attorney-client privilege, if the client is a personal representative and the attorney represents the personal representative in that capacity, in the absence of an agreement between the attorney and the personal representative to the contrary:

(i) No beneficiary of the estate is, or shall be treated as, the client of the attorney solely by reason of his or her status as beneficiary;

(ii) The existence of a fiduciary relationship between the personal representative and a beneficiary of the estate does not by itself constitute or give rise to any waiver of the privilege for confidential communications made in the course of professional employment between the attorney or his or her employee and the personal representative who is the client; and

(iii) The fiduciary's testimony that he or she has relied on the attorney's advice shall not by itself constitute such a waiver.

(B) For purposes of this paragraph, "personal representative" shall mean (i) the administrator, administrator c.t.a., ancillary administrator, executor, preliminary executor, temporary administrator, lifetime trustee or trustee to whom letters have been issued within the meaning of subdivision thirty-four of section one hundred three of the surrogate's court procedure act, and (ii) the guardian of an incapacitated communicant if and to the extent that the order appointing such guardian under subdivision (c) of section 81.16 of the mental hygiene law or any subsequent order of any court expressly provides that the guardian is to be the personal representative of the incapacitated communicant for purposes of this section; "beneficiary" shall have the meaning set

forth in subdivision eight of section one hundred three of the surrogate's court procedure act and "estate" shall have the meaning set forth in subdivision nineteen of section one hundred three of the surrogate's court procedure act.

(b) Wills and revocable trusts. In any action involving the probate, validity or construction of a will or, after the grantor's death, a revocable trust, an attorney or his employee shall be required to disclose information as to the preparation, execution or revocation of any will, revocable trust, or other relevant instrument, but he shall not be allowed to disclose any communication privileged under subdivision (a) which would tend to disgrace the memory of the decedent.

Credits

(L.1962, c. 308. Amended L.1977, c. 418, § 1; L.2002, c. 430, § 1, eff. Aug. 20, 2002; L.2016, c. 262, § 1, eff. Aug. 19, 2016; L.2019, c. 529, § 1, eff. Nov. 20, 2019.)

McKinney's CPLR § 4503, NY CPLR § 4503

Current through L.2021, chapters 1 to 49, 61 to 68. Some statute sections may be more current, see credits for details.

End of Document

McKinney's Consolidated Laws of New York Annotated
Judiciary Law (Refs & Annos)
Appendix
Rules of Professional Conduct [eff. April 1, 2009. As Amended to June 24, 2020.] (Refs & Annos)
Client-Lawyer Relationship

Rules of Prof. Con., Rule 1.6 McK.Consol.Laws, Book 29 App.

Rule 1.6. Confidentiality of Information

Currentness

(a) A lawyer shall not knowingly reveal confidential information, as defined in this Rule, or use such information to the disadvantage of a client or for the advantage of the lawyer or a third person, unless:

(1) the client gives informed consent, as defined in Rule 1.0(j);

(2) the disclosure is impliedly authorized to advance the best interests of the client and is either reasonable under the circumstances or customary in the professional community; or

(3) the disclosure is permitted by paragraph (b).

"Confidential information" consists of information gained during or relating to the representation of a client, whatever its source, that is (a) protected by the attorney-client privilege, (b) likely to be embarrassing or detrimental to the client if disclosed, or (c) information that the client has requested be kept confidential. "Confidential information" does not ordinarily include (i) a lawyer's legal knowledge or legal research or (ii) information that is generally known in the local community or in the trade, field or profession to which the information relates.

(b) A lawyer may reveal or use confidential information to the extent that the lawyer reasonably believes necessary:

(1) to prevent reasonably certain death or substantial bodily harm;

(2) to prevent the client from committing a crime;

(3) to withdraw a written or oral opinion or representation previously given by the lawyer and reasonably believed by the lawyer still to be relied upon by a third person, where the lawyer has discovered that the opinion or representation was based on materially inaccurate information or is being used to further a crime or fraud;

(4) to secure legal advice about compliance with these Rules or other law by the lawyer, another lawyer associated with the lawyer's firm or the law firm;

(5)(i) to defend the lawyer or the lawyer's employees and associates against an accusation of wrongful conduct; or

(ii) to establish or collect a fee; or

(6) when permitted or required under these Rules or to comply with other law or court order.

(c) A lawyer shall make reasonable efforts to prevent the inadvertent or unauthorized disclosure or use of, or unauthorized access to, information protected by Rules 1.6, 1.9(c), or 1.18(b).

Comment

Scope of the Professional Duty of Confidentiality

[1] This Rule governs the disclosure of information protected by the professional duty of confidentiality. Such information is described in these Rules as "confidential information" as defined in this Rule. Other rules also deal with confidential information. *See* Rules 1.8(b) and 1.9(c)(1) for the lawyer's duties with respect to the use of such information to the disadvantage of clients and former clients; Rule 1.9(c)(2) for the lawyer's duty not to reveal information relating to the lawyer's prior representation of a former client; Rule 1.14(c) for information relating to representation of a client with diminished capacity; Rule 1.18(b) for the lawyer's duties with respect to information provided to the lawyer by a prospective client; Rule 3.3 for the lawyer's duty of candor to a tribunal; and Rule 8.3(c) for information gained by a lawyer or judge while participating in an approved lawyer assistance program.

[2] A fundamental principle in the client-lawyer relationship is that, in the absence of the client's informed consent, or except as permitted or required by these Rules, the lawyer must not knowingly reveal information gained during and related to the representation, whatever its source. *See* Rule 1.0(j) for the definition of informed consent. The lawyer's duty of confidentiality contributes to the trust that is the hallmark of the client-lawyer relationship. The client is thereby encouraged to seek legal assistance and to communicate fully and frankly with the lawyer, even as to embarrassing or legally damaging subject matter. The lawyer needs this information to represent the client effectively and, if necessary, to advise the client to refrain from wrongful conduct. Typically, clients come to lawyers to determine their rights and what is, in the complex of laws and regulations, deemed to be legal and correct. Based upon experience, lawyers know that almost all clients follow the advice given, and the law is thereby upheld.

[3] The principle of client-lawyer confidentiality is given effect in three related bodies of law: the attorney-client privilege of evidence law, the work-product doctrine of civil procedure and the professional duty of confidentiality established in legal ethics codes. The attorney-client privilege and the work-product doctrine apply when compulsory process by a judicial or other governmental body seeks to compel a lawyer to testify or produce information or evidence concerning a client. The professional duty of client-lawyer confidentiality, in contrast, applies to a lawyer in all settings and at all times, prohibiting the lawyer from disclosing confidential information unless permitted or required by these Rules or to comply with other law or court order. The confidentiality duty applies not only to matters communicated in confidence by the client, which are protected by the attorney-client privilege, but also to all information gained during and relating to the representation, whatever its source. The confidentiality duty, for example, prohibits a lawyer from volunteering confidential information to a friend or to any other person except in compliance with the provisions of this Rule, including the Rule's reference to other law that may compel disclosure. *See* Comments [12]-[13]; *see also* Scope.

[4] Paragraph (a) prohibits a lawyer from knowingly revealing confidential information as defined by this Rule. This prohibition also applies to disclosures by a lawyer that do not in themselves reveal confidential information but could reasonably lead to the

discovery of such information by a third person. A lawyer's use of a hypothetical to discuss issues relating to the representation with persons not connected to the representation is permissible so long as there is no reasonable likelihood that the listener will be able to ascertain the identity of the client.

[4A] Paragraph (a) protects all factual information "gained during or relating to the representation of a client." Information relates to the representation if it has any possible relevance to the representation or is received because of the representation. The accumulation of legal knowledge or legal research that a lawyer acquires through practice ordinarily is not client information protected by this Rule. However, in some circumstances, including where the client and the lawyer have so agreed, a client may have a proprietary interest in a particular product of the lawyer's research. Information that is generally known in the local community or in the trade, field or profession to which the information relates is also not protected, unless the client and the lawyer have otherwise agreed. Information is not "generally known" simply because it is in the public domain or available in a public file.

Use of Information Related to Representation

[4B] The duty of confidentiality also prohibits a lawyer from using confidential information to the advantage of the lawyer or a third person or to the disadvantage of a client or former client unless the client or former client has given informed consent. *See* Rule 1.0(j) for the definition of "informed consent." This part of paragraph (a) applies when information is used to benefit either the lawyer or a third person, such as another client, a former client or a business associate of the lawyer. For example, if a lawyer learns that a client intends to purchase and develop several parcels of land, the lawyer may not (absent the client's informed consent) use that information to buy a nearby parcel that is expected to appreciate in value due to the client's purchase, or to recommend that another client buy the nearby land, even if the lawyer does not reveal any confidential information. The duty also prohibits disadvantageous use of confidential information unless the client gives informed consent, except as permitted or required by these Rules. For example, a lawyer assisting a client in purchasing a parcel of land may not make a competing bid on the same land. However, the fact that a lawyer has once served a client does not preclude the lawyer from using generally known information about that client, even to the disadvantage of the former client, after the client-lawyer relationship has terminated. *See* Rule 1.9(c)(1).

Authorized Disclosure

[5] Except to the extent that the client's instructions or special circumstances limit that authority, a lawyer may make disclosures of confidential information that are impliedly authorized by a client if the disclosures (i) advance the best interests of the client and (ii) are either reasonable under the circumstances or customary in the professional community. In some situations, for example, a lawyer may be impliedly authorized to admit a fact that cannot properly be disputed or to make a disclosure that facilitates a satisfactory conclusion to a matter. In addition, lawyers in a firm may, in the course of the firm's practice, disclose to each other information relating to a client of the firm, unless the client has instructed that particular information be confined to specified lawyers. Lawyers are also impliedly authorized to reveal information about a client with diminished capacity when necessary to take protective action to safeguard the client's interests. See Rules 1.14(b) and (c).

Disclosure Adverse to Client

[6] Although the public interest is usually best served by a strict rule requiring lawyers to preserve the confidentiality of information relating to the representation of their clients, the confidentiality rule is subject to limited exceptions that prevent substantial harm to important interests, deter wrongdoing by clients, prevent violations of the law, and maintain the impartiality and integrity of judicial proceedings. Paragraph (b) permits, but does not require, a lawyer to disclose information relating to the representation to accomplish these specified purposes.

[6A] The lawyer's exercise of discretion conferred by paragraphs (b)(1) through (b)(3) requires consideration of a wide range of factors and should therefore be given great weight. In exercising such discretion under these paragraphs, the lawyer should

consider such factors as: (i) the seriousness of the potential injury to others if the prospective harm or crime occurs, (ii) the likelihood that it will occur and its imminence, (iii) the apparent absence of any other feasible way to prevent the potential injury, (iv) the extent to which the client may be using the lawyer's services in bringing about the harm or crime, (v) the circumstances under which the lawyer acquired the information of the client's intent or prospective course of action, and (vi) any other aggravating or extenuating circumstances. In any case, disclosure adverse to the client's interest should be no greater than the lawyer reasonably believes necessary to prevent the threatened harm or crime. When a lawyer learns that a client intends to pursue or is pursuing a course of conduct that would permit disclosure under paragraphs (b)(1), (b)(2) or (b)(3), the lawyer's initial duty, where practicable, is to remonstrate with the client. In the rare situation in which the client is reluctant to accept the lawyer's advice, the lawyer's threat of disclosure is a measure of last resort that may persuade the client. When the lawyer reasonably believes that the client will carry out the threatened harm or crime, the lawyer may disclose confidential information when permitted by paragraphs (b)(1), (b)(2) or (b)(3). A lawyer's permissible disclosure under paragraph (b) does not waive the client's attorney-client privilege; neither the lawyer nor the client may be forced to testify about communications protected by the privilege, unless a tribunal or body with authority to compel testimony makes a determination that the crime-fraud exception to the privilege, or some other exception, has been satisfied by a party to the proceeding. For a lawyer's duties when representing an organizational client engaged in wrongdoing, *see* Rule 1.13(b).

[6B] Paragraph (b)(1) recognizes the overriding value of life and physical integrity and permits disclosure reasonably necessary to prevent reasonably certain death or substantial bodily harm. Such harm is reasonably certain to occur if it will be suffered imminently or if there is a present and substantial risk that a person will suffer such harm at a later date if the lawyer fails to take action necessary to eliminate the threat. Thus, a lawyer who knows that a client has accidentally discharged toxic waste into a town's water supply may reveal this information to the authorities if there is a present and substantial risk that a person who drinks the water will contract a life-threatening or debilitating disease and the lawyer's disclosure is necessary to eliminate the threat or reduce the number of victims. Wrongful execution of a person is a life-threatening and imminent harm under paragraph (b)(1) once the person has been convicted and sentenced to death. On the other hand, an event that will cause property damage but is unlikely to cause substantial bodily harm is not a present and substantial risk under paragraph (b)(1); similarly, a remote possibility or small statistical likelihood that any particular unit of a mass-distributed product will cause death or substantial bodily harm to unspecified persons over a period of years does not satisfy the element of reasonably certain death or substantial bodily harm under the exception to the duty of confidentiality in paragraph (b)(1).

[6C] Paragraph (b)(2) recognizes that society has important interests in preventing a client's crime. Disclosure of the client's intention is permitted to the extent reasonably necessary to prevent the crime. In exercising discretion under this paragraph, the lawyer should consider such factors as those stated in Comment [6A].

[6D] Some crimes, such as criminal fraud, may be ongoing in the sense that the client's past material false representations are still deceiving new victims. The law treats such crimes as continuing crimes in which new violations are constantly occurring. The lawyer whose services were involved in the criminal acts that constitute a continuing crime may reveal the client's refusal to bring an end to a continuing crime, even though that disclosure may also reveal the client's past wrongful acts, because refusal to end a continuing crime is equivalent to an intention to commit a new crime. Disclosure is not permitted under paragraph (b)(2), however, when a person who may have committed a crime employs a new lawyer for investigation or defense. Such a lawyer does not have discretion under paragraph (b)(2) to use or disclose the client's past acts that may have continuing criminal consequences. Disclosure is permitted, however, if the client uses the new lawyer's services to commit a further crime, such as obstruction of justice or perjury.

[6E] Paragraph (b)(3) permits a lawyer to withdraw a legal opinion or to disaffirm a prior representation made to third parties when the lawyer reasonably believes that third persons are still relying on the lawyer's work and the work was based on "materially inaccurate information or is being used to further a crime or fraud." *See* Rule 1.16(b)(1), requiring the lawyer to withdraw when the lawyer knows or reasonably should know that the representation will result in a violation of law. Paragraph (b)(3) permits the lawyer to give only the limited notice that is implicit in withdrawing an opinion or representation, which may have the collateral effect of inferentially revealing confidential information. The lawyer's withdrawal of the tainted opinion or

representation allows the lawyer to prevent further harm to third persons and to protect the lawyer's own interest when the client has abused the professional relationship, but paragraph (b)(3) does not permit explicit disclosure of the client's past acts unless such disclosure is permitted under paragraph (b)(2).

[7] [Reserved.]

[8] [Reserved.]

[9] A lawyer's confidentiality obligations do not preclude a lawyer from securing confidential legal advice about compliance with these Rules and other law by the lawyer, another lawyer in the lawyer's firm, or the law firm. In many situations, disclosing information to secure such advice will be impliedly authorized for the lawyer to carry out the representation. Even when the disclosure is not impliedly authorized, paragraph (b)(4) permits such disclosure because of the importance of a lawyer's compliance with these Rules, court orders and other law.

[10] Where a claim or charge alleges misconduct of the lawyer related to the representation of a current or former client, the lawyer may respond to the extent the lawyer reasonably believes necessary to establish a defense. Such a claim can arise in a civil, criminal, disciplinary or other proceeding and can be based on a wrong allegedly committed by the lawyer against the client or on a wrong alleged by a third person, such as a person claiming to have been defrauded by the lawyer and client acting together or by the lawyer acting alone. The lawyer may respond directly to the person who has made an accusation that permits disclosure, provided that the lawyer's response complies with Rule 4.2 and Rule 4.3, and other Rules or applicable law. A lawyer may make the disclosures authorized by paragraph (b)(5) through counsel. The right to respond also applies to accusations of wrongful conduct concerning the lawyer's law firm, employees or associates.

[11] A lawyer entitled to a fee is permitted by paragraph (b)(5) to prove the services rendered in an action to collect it. This aspect of the rule expresses the principle that the beneficiary of a fiduciary relationship may not exploit it to the detriment of the fiduciary.

[12] Paragraph (b) does not mandate any disclosures. However, other law may require that a lawyer disclose confidential information. Whether such a law supersedes Rule 1.6 is a question of law beyond the scope of these Rules. When disclosure of confidential information appears to be required by other law, the lawyer must consult with the client to the extent required by Rule 1.4 before making the disclosure, unless such consultation would be prohibited by other law. If the lawyer concludes that other law supersedes this Rule and requires disclosure, paragraph (b)(6) permits the lawyer to make such disclosures as are necessary to comply with the law.

[13] A tribunal or governmental entity claiming authority pursuant to other law to compel disclosure may order a lawyer to reveal confidential information. Absent informed consent of the client to comply with the order, the lawyer should assert on behalf of the client nonfrivolous arguments that the order is not authorized by law, the information sought is protected against disclosure by an applicable privilege or other law, or the order is invalid or defective for some other reason. In the event of an adverse ruling, the lawyer must consult with the client to the extent required by Rule 1.4 about the possibility of an appeal or further challenge, unless such consultation would be prohibited by other law. If such review is not sought or is unsuccessful, paragraph (b)(6) permits the lawyer to comply with the order.

[14] Paragraph (b) permits disclosure only to the extent the lawyer reasonably believes the disclosure is necessary to accomplish one of the purposes specified in paragraphs (b)(1) through (b)(6). Before making a disclosure, the lawyer should, where practicable, first seek to persuade the client to take suitable action to obviate the need for disclosure. In any case, a disclosure adverse to the client's interest should be no greater than the lawyer reasonably believes necessary to accomplish the purpose, particularly when accusations of wrongdoing in the representation of a client have been made by a third party rather than by the client. If the disclosure will be made in connection with an adjudicative proceeding, the disclosure should be made in a manner

that limits access to the information to the tribunal or other persons having a need to know the information, and appropriate protective orders or other arrangements should be sought by the lawyer to the fullest extent practicable.

[15] Paragraph (b) permits but does not require the disclosure of information relating to a client's representation to accomplish the purposes specified in paragraphs (b)(1) through (b)(6). A lawyer's decision not to disclose as permitted by paragraph (b) does not violate this Rule. Disclosure may, however, be required by other Rules or by other law. *See* Comments [12]-[13]. Some Rules require disclosure only if such disclosure would be permitted by paragraph (b). *E.g.*, Rule 8.3(c)(1). Rule 3.3(c), on the other hand, requires disclosure in some circumstances whether or not disclosure is permitted or prohibited by this Rule.

Withdrawal

[15A] If the lawyer's services will be used by the client in materially furthering a course of criminal or fraudulent conduct, the lawyer must withdraw pursuant to Rule 1.16(b)(1). Withdrawal may also be required or permitted for other reasons under Rule 1.16. After withdrawal, the lawyer is required to refrain from disclosing or using information protected by Rule 1.6, except as this Rule permits such disclosure. Neither this Rule, nor Rule 1.9(c), nor Rule 1.16(e) prevents the lawyer from giving notice of the fact of withdrawal. For withdrawal or disaffirmance of an opinion or representation, see paragraph (b)(3) and Comment [6E]. Where the client is an organization, the lawyer may be in doubt whether the organization will actually carry out the contemplated conduct. Where necessary to guide conduct in connection with this Rule, the lawyer may, and sometimes must, make inquiry within the organization. *See* Rules 1.13(b) and (c).

Duty to Preserve Confidentiality

[16] Paragraph (c) imposes three related obligations. It requires a lawyer to make reasonable efforts to safeguard confidential information against unauthorized access by third parties and against inadvertent or unauthorized disclosure by the lawyer or other persons who are participating in the representation of the client or who are otherwise subject to the lawyer's supervision. *See* Rules 1.1, 5.1 and 5.3. Confidential information includes not only information protected by Rule 1.6(a) with respect to current clients but also information protected by Rule 1.9(c) with respect to former clients and information protected by Rule 1.18(b) with respect to prospective clients. Unauthorized access to, or the inadvertent or unauthorized disclosure of, information protected by Rules 1.6, 1.9, or 1.18, does not constitute a violation of paragraph (c) if the lawyer has made reasonable efforts to prevent the unauthorized access or disclosure. Factors to be considered in determining the reasonableness of the lawyer's efforts include, but are not limited to: (i) the sensitivity of the information; (ii) the likelihood of disclosure if additional safeguards are not employed; (iii) the cost of employing additional safeguards; (iv) the difficulty of implementing the safeguards; and (v) the extent to which the safeguards adversely affect the lawyer's ability to represent clients (e.g., by making a device or software excessively difficult to use). A client may require the lawyer to implement special security measures not required by this Rule, or may give informed consent to forgo security measures that would otherwise be required by this Rule. For a lawyer's duties when sharing information with nonlawyers inside or outside the lawyer's own firm, *see* Rule 5.3, Comment [2].

[17] When transmitting a communication that includes information relating to the representation of a client, the lawyer must take reasonable precautions to prevent the information from coming into the hands of unintended recipients. Paragraph (c) does not ordinarily require that the lawyer use special security measures if the method of communication affords a reasonable expectation of confidentiality. However, a lawyer may be required to take specific steps to safeguard a client's information to comply with a court order (such as a protective order) or to comply with other law (such as state and federal laws or court rules that govern data privacy or that impose notification requirements upon the loss of, or unauthorized access to, electronic information). For example, a protective order may extend a high level of protection to documents marked "Confidential" or "Confidential--Attorneys' Eyes Only"; the Health Insurance Portability and Accountability Act of 1996 ("HIPAA") may require a lawyer to take specific precautions with respect to a client's or adversary's medical records; and court rules may require a lawyer to block out a client's Social Security number or a minor's name when electronically filing papers with the court. The specific requirements of court orders, court rules, and other laws are beyond the scope of these Rules.

Lateral Moves, Law Firm Mergers, and Confidentiality

[18A] When lawyers or law firms (including in-house legal departments) contemplate a new association with other lawyers or law firms though lateral hiring or merger, disclosure of limited information may be necessary to resolve conflicts of interest pursuant to Rule 1.10 and to address financial, staffing, operational, and other practical issues. However, Rule 1.6(a) requires lawyers and law firms to protect their clients' confidential information, so lawyers and law firms may not disclose such information for their own advantage or for the advantage of third parties absent a client's informed consent or some other exception to Rule 1.6.

[18B] Disclosure without client consent in the context of a possible lateral move or law firm merger is ordinarily permitted regarding basic information such as: (i) the identities of clients or other parties involved in a matter; (ii) a brief summary of the status and nature of a particular matter, including the general issues involved; (iii) information that is publicly available; (iv) the lawyer's total book of business; (v) the financial terms of each lawyer-client relationship; and (vi) information about aggregate current and historical payment of fees (such as realization rates, average receivables, and aggregate timeliness of payments). Such information is generally not "confidential information" within the meaning of Rule 1.6.

[18C] Disclosure without client consent in the context of a possible lateral move or law firm merger is ordinarily *not* permitted, however, if information is protected by Rule 1.6(a), 1.9(c), or Rule 1.18(b). This includes information that a lawyer knows or reasonably believes is protected by the attorney-client privilege, or is likely to be detrimental or embarrassing to the client, or is information that the client has requested be kept confidential. For example, many clients would not want their lawyers to disclose their tardiness in paying bills; the amounts they spend on legal fees in particular matters; forecasts about their financial prospects; or information relating to sensitive client matters (e.g., an unannounced corporate takeover, an undisclosed possible divorce, or a criminal investigation into the client's conduct).

[18D] When lawyers are exploring a new association, whether by lateral move or by merger, all lawyers involved must individually consider fiduciary obligations to their existing firms that may bear on the timing and scope of disclosures to clients relating to conflicts and financial concerns, and should consider whether to ask clients for a waiver of confidentiality if consistent with these fiduciary duties--*see* Rule 1.10(e) (requiring law firms to check for conflicts of interest). Questions of fiduciary duty are legal issues beyond the scope of the Rules.

[18E] For the unique confidentiality and notice provisions that apply to a lawyer or law firm seeking to sell all or part of its practice, see Rule 1.17 and Comment [7] to that Rule.

[18F] Before disclosing information regarding a possible lateral move or law firm merger, law firms and lawyers moving between firms--both those providing information and those receiving information--should use reasonable measures to minimize the risk of any improper, unauthorized or inadvertent disclosures, whether or not the information is protected by Rule 1.6(a), 1.9(c), or 1.18(b). These steps might include such measures as: (1) disclosing client information in stages; initially identifying only certain clients and providing only limited information, and providing a complete list of clients and more detailed financial information only at subsequent stages; (2) limiting disclosure to those at the firm, or even a single person at the firm, directly involved in clearing conflicts and making the business decision whether to move forward to the next stage regarding the lateral hire or law firm merger; and/or (3) agreeing not to 37 disclose financial or conflict information outside the firm(s) during and after the lateral hiring negotiations or merger process.

Rules of Prof. Con., Rule 1.6 McK. Consol. Laws, Book 29 App., NY ST RPC Rule 1.6
Current with amendments through Oct. 1, 2020.

End of Document

McKinney's Consolidated Laws of New York Annotated
Judiciary Law (Refs & Annos)
Appendix
Rules of Professional Conduct [eff. April 1, 2009. As Amended to June 24, 2020.] (Refs & Annos)
Client-Lawyer Relationship

Rules of Prof. Con., Rule 1.7 McK.Consol.Laws, Book 29 App.

Rule 1.7. Conflict of Interest: Current Clients

Currentness

(a) Except as provided in paragraph (b), a lawyer shall not represent a client if a reasonable lawyer would conclude that either:

(1) the representation will involve the lawyer in representing differing interests; or

(2) there is a significant risk that the lawyer's professional judgment on behalf of a client will be adversely affected by the lawyer's own financial, business, property or other personal interests.

(b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:

(1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;

(2) the representation is not prohibited by law;

(3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and

(4) each affected client gives informed consent, confirmed in writing.

Comment

General Principles

[1] Loyalty and independent judgment are essential aspects of a lawyer's relationship with a client. The professional judgment of a lawyer should be exercised, within the bounds of the law, solely for the benefit of the client and free of compromising influences and loyalties. Concurrent conflicts of interest, which can impair a lawyer's professional judgment, can arise from the lawyer's responsibilities to another client, a former client or a third person, or from the lawyer's own interests. A lawyer should not permit these competing responsibilities or interests to impair the lawyer's ability to exercise professional judgment on behalf of each client. For specific Rules regarding certain concurrent conflicts of interest, *see* Rule 1.8. For former client conflicts

of interest, *see* Rule 1.9. For conflicts of interest involving prospective clients, *see* Rule 1.18. For definitions of "differing interests," "informed consent" and "confirmed in writing," *see* Rules 1.0(f), (j) and (e), respectively.

[2] Resolution of a conflict of interest problem under this Rule requires the lawyer, acting reasonably, to: (i) identify clearly the client or clients, (ii) determine whether a conflict of interest exists, *i.e.*, whether the lawyer's judgment may be impaired or the lawyer's loyalty may be divided if the lawyer accepts or continues the representation, (iii) decide whether the representation may be undertaken despite the existence of a conflict, *i.e.*, whether the conflict is consentable under paragraph (b); and if so (iv) consult with the clients affected under paragraph (a) and obtain their informed consent, confirmed in writing. The clients affected under paragraph (a) include all of the clients who may have differing interests under paragraph (a)(1) and any clients whose representation might be adversely affected under paragraph (a)(2).

[3] A conflict of interest may exist before representation is undertaken, in which event the representation must be declined, unless the lawyer obtains the informed consent of each client under the conditions of paragraph (b). *See* Rule 1.10(e), which requires every law firm to create, implement and maintain a conflict-checking system.

[4] If a conflict arises after representation has been undertaken, the lawyer ordinarily must withdraw from the representation unless the lawyer has obtained the informed consent of the client under the conditions of paragraph (b). *See* Rule 1.16(b)(1). Where more than one client is involved, whether the lawyer may continue to represent any of the clients is determined both by the lawyer's ability to comply with duties owed to the former client and by the lawyer's ability to represent adequately the remaining client or clients, given the lawyer's duties to the former client. *See* Rule 1.9; *see also* Comments [5], [29A].

[5] Unforeseeable developments, such as changes in corporate and other organizational affiliations or the addition or realignment of parties in litigation, might create conflicts in the midst of a representation, as when a company sued by the lawyer on behalf of one client is acquired by another client represented by the lawyer in an unrelated matter. Depending on the circumstances, the lawyer may have the option to withdraw from one of the representations in order to avoid the conflict. The lawyer must seek court approval where necessary and take steps to minimize harm to the clients. *See* Rules 1.16(d) and (e). The lawyer must continue to protect the confidences of the client from whose representation the lawyer has withdrawn. *See* Rule 1.9(c).

Identifying Conflicts of Interest

[6] The duty to avoid the representation of differing interest prohibits, among other things, undertaking representation adverse to a current client without that client's informed consent. For example, absent consent, a lawyer may not advocate in one matter against another client that the lawyer represents in some other matter, even when the matters are wholly unrelated. The client as to whom the representation is adverse is likely to feel betrayed and the resulting damage to the client-lawyer relationship is likely to impair the lawyer's ability to represent the client effectively. In addition, the client on whose behalf the adverse representation is undertaken may reasonably fear that the lawyer will pursue that client's case less effectively out of deference to the other client, that is, that the lawyer's exercise of professional judgment on behalf of that client will be adversely affected by the lawyer's interest in retaining the current client. Similarly, a conflict may arise when a lawyer is required to cross-examine a client appearing as a witness in a lawsuit involving another client, as when the testimony will be damaging to the client represented in the lawsuit. On the other hand, simultaneous representation in unrelated matters of clients whose interests are only economically adverse, such as representation of competing economic enterprises in unrelated litigation, does not ordinarily constitute a conflict of interest and thus may not require consent of the respective clients.

[7] Differing interests can also arise in transactional matters. For example, if a lawyer is asked to represent the seller of a business in negotiations with a buyer represented by the lawyer, not in the same transaction but in another, unrelated matter, the lawyer could not undertake the representation without the informed consent of each client.

[8] Differing interests exist if there is a significant risk that a lawyer's exercise of professional judgment in considering, recommending or carrying out an appropriate course of action for the client will be adversely affected or the representation

would otherwise be materially limited by the lawyer's other responsibilities or interests. For example, the professional judgment of a lawyer asked to represent several individuals operating a joint venture is likely to be adversely affected to the extent that the lawyer is unable to recommend or advocate all possible positions that each client might take because of the lawyer's duty of loyalty to the others. The conflict in effect forecloses alternatives that would otherwise be available to the client. The mere possibility of subsequent harm does not itself require disclosure and consent. The critical questions are the likelihood that a difference in interests will eventuate and, if it does, whether it will adversely affect the lawyer's professional judgment in considering alternatives or foreclose courses of action that reasonably should be pursued on behalf of the client.

Lawyer's Responsibilities to Former Clients and Other Third Persons

[9] In addition to conflicts with other current clients, a lawyer's duties of loyalty and independence may be adversely affected by responsibilities to former clients under Rule 1.9, or by the lawyer's responsibilities to other persons, such as fiduciary duties arising from a lawyer's service as a trustee, executor or corporate director.

Personal-Interest Conflicts

[10] The lawyer's own financial, property, business or other personal interests should not be permitted to have an adverse effect on representation of a client. For example, if the probity of a lawyer's own conduct in a transaction is in serious question, it may be difficult or impossible for the lawyer to give a client detached advice. Similarly, when a lawyer has discussions concerning possible employment with an opponent of the lawyer's client or with a law firm representing the opponent, such discussions could materially limit the lawyer's representation of the client. In addition, a lawyer may not allow related business interests to affect representation, for example, by referring clients to an enterprise in which the lawyer has an undisclosed financial interest. *See* Rule 5.7 on responsibilities regarding nonlegal services and Rule 1.8 pertaining to a number of personal-interest conflicts, including business transactions with clients.

[11] When lawyers representing different clients in the same matter or in substantially related matters are closely related, there may be a significant risk that client confidences will be revealed and that the lawyer's family relationship will interfere with both loyalty and professional judgment. As a result, each client is entitled to know of the existence and implications of the relationship between the lawyers, before the lawyer agrees to undertake the representation. Thus, a lawyer who has a significant intimate or close family relationship with another lawyer ordinarily may not represent a client in a matter where that other lawyer is representing another party, unless each client gives informed consent, as defined in Rule 1.0(j).

[12] A lawyer is prohibited from engaging in sexual relations with a client in domestic relations matters. In all other matters a lawyer's sexual relations with a client are circumscribed by the provisions of Rule 1.8(j).

Interest of Person Paying for Lawyer's Services

[13] A lawyer may be paid from a source other than the client, including a co-client, if the client is informed of that fact and consents and the arrangement does not compromise the lawyer's duty of loyalty or independent judgment to the client. *See* Rule 1.8(f). If acceptance of the payment from any other source presents a significant risk that the lawyer's exercise of professional judgment on behalf of a client will be adversely affected by the lawyer's own interest in accommodating the person paying the lawyer's fee or by the lawyer's responsibilities to a payer who is also a co-client, then the lawyer must comply with the requirements of paragraph (b) before accepting the representation, including determining whether the conflict is consentable and, if so, that the client has adequate information about the material risks of the representation.

Prohibited Representations

[14] Ordinarily, clients may consent to representation notwithstanding a conflict. As paragraph (b) indicates, however, some conflicts are nonconsentable. If a lawyer does not reasonably believe that the conditions set forth in paragraph (b) can be met, the

lawyer should neither ask for the client's consent nor provide representation on the basis of the client's consent. A client's consent to a nonconsentable conflict is ineffective. When the lawyer is representing more than one client, the question of consentability must be resolved as to each client.

[15] Consentability is typically determined by considering whether the interests of the clients will be adequately protected if the clients consent to representation burdened by a conflict of interest. Thus, under paragraph (b)(1), notwithstanding client consent, a representation is prohibited if, in the circumstances, the lawyer cannot reasonably conclude that the lawyer will be able to provide competent and diligent representation. *See* Rule 1.1 regarding competence and Rule 1.3 regarding diligence.

[16] Paragraph (b)(2) describes conflicts that are nonconsentable because the representation is prohibited by applicable law. For example, federal criminal statutes prohibit certain representations by a former government lawyer despite the informed consent of the former governmental client. In addition, there are some instances where conflicts are nonconsentable under decisional law.

[17] Paragraph (b)(3) describes conflicts that are nonconsentable because of the institutional interest in vigorous development of each client's position when the clients are aligned directly against each other in the same litigation or other proceeding before a tribunal. Whether clients are aligned directly against each other within the meaning of this paragraph requires examination of the context of the proceeding. Although this paragraph does not preclude a lawyer's multiple representation of adverse parties to mediation (because mediation is not a proceeding before a "tribunal" as defined in Rule 1.0(w)), such representation may be precluded by paragraph (b)(1).

Informed Consent

[18] Informed consent requires that each affected client be aware of the relevant circumstances, including the material and reasonably foreseeable ways that the conflict could adversely affect the interests of that client. Informed consent also requires that the client be given the opportunity to obtain other counsel if the client so desires. *See* Rule 1.0(j). The information that a lawyer is required to communicate to a client depends on the nature of the conflict and the nature of the risks involved, and a lawyer should take into account the sophistication of the client in explaining the potential adverse consequences of the conflict. There are circumstances in which it is appropriate for a lawyer to advise a client to seek the advice of a disinterested lawyer in reaching a decision as to whether to consent to the conflict. When representation of multiple clients in a single matter is undertaken, the information must include the implications of the common representation, including possible effects on loyalty, confidentiality and the attorney-client privilege, and the advantages and risks involved. *See* Comments [30] and [31] concerning the effect of common representation on confidentiality.

[19] Under some circumstances it may be impossible to make the disclosure necessary to obtain consent. For example, when the lawyer represents different clients in related matters and one client refuses to consent to the disclosure necessary to permit the other client to make an informed decision, the lawyer cannot properly ask the latter to consent. In some cases the alternative to common representation is that each party obtains separate representation with the possibility of incurring additional costs. These costs, along with the benefits of securing separate representation, are factors that may be considered by the affected client in determining whether common representation is in the client's interests. Where the fact, validity or propriety of client consent is called into question, the lawyer has the burden of establishing that the client's consent was properly obtained in accordance with the Rule.

Client Consent Confirmed in Writing

[20] Paragraph (b) requires the lawyer to obtain the informed consent of the client, confirmed in writing. Such a writing may consist of (i) a document from the client, (ii) a document that the lawyer promptly transmits to the client confirming an oral informed consent, or (iii) a statement by the client made on the record of any proceeding before a tribunal, whether before, during or after a trial or hearing. *See* Rule 1.0(e) for the definition of "confirmed in writing." *See also* Rule 1.0(x) ("writing" includes electronic transmission). If it is not feasible to obtain or transmit the writing at the time the client gives informed consent,

then the lawyer must obtain or transmit it within a reasonable time thereafter. The Rule does not require that the information communicated to the client by the lawyer necessary to make the consent "informed" be in writing or in any particular form in all cases. *See* Rules 1.0(e) and (j). The requirement of a writing does not supplant the need in most cases for the lawyer to talk with the client to explain the risks and advantages, if any, of representation burdened with a conflict of interest, as well as reasonably available alternatives, and to afford the client a reasonable opportunity to consider the risks and alternatives and to raise questions and concerns. Rather, the writing is required in order to impress upon clients the seriousness of the decision the client is being asked to make and to avoid disputes or ambiguities that might later occur in the absence of a writing. *See* Comment [18].

Revoking Consent

[21] A client who has given consent to a conflict may revoke the consent and, like any other client, may terminate the lawyer's representation at any time. Whether revoking consent to the client's own representation precludes the lawyer from continuing to represent other clients depends on the circumstances, including the nature of the conflict, whether the client revoked consent because of a material change in circumstances, the reasonable expectations of the other clients, and whether material detriment to the other clients or the lawyer would result.

Consent to Future Conflict

[22] Whether a lawyer may properly request a client to waive conflicts that might arise in the future is subject to the conditions set forth in paragraph (b). The effectiveness of advance waivers is generally determined by the extent to which the client reasonably understands the material risks that the waiver entails. At a minimum, the client should be advised generally of the types of possible future adverse representations that the lawyer envisions, as well as the types of clients and matters that may present such conflicts. The more comprehensive the explanation and disclosure of the types of future representations that might arise and the actual and reasonably foreseeable adverse consequences of those representations, the greater the likelihood that the client will have the understanding necessary to make the consent "informed" and the waiver effective. *See* Rule 1.0(j). The lawyer should also disclose the measures that will be taken to protect the client should a conflict arise, including procedures such as screening that would be put in place. *See* Rule 1.0(t) for the definition of "screening." The adequacy of the disclosure necessary to obtain valid advance consent to conflicts may also depend on the sophistication and experience of the client. For example, if the client is unsophisticated about legal matters generally or about the particular type of matter at hand, the lawyer should provide more detailed information about both the nature of the anticipated conflict and the adverse consequences to the client that may ensue should the potential conflict become an actual one. In other instances, such as where the client is a child or an incapacitated or impaired person, it may be impossible to inform the client sufficiently, and the lawyer should not seek an advance waiver. On the other hand, if the client is an experienced user of the legal services involved and is reasonably informed regarding the risk that a conflict may arise, an advance waiver is more likely to be effective, particularly if, for example, the client is independently represented or advised by in-house or other counsel in giving consent. Thus, in some circumstances, even general and open-ended waivers by experienced users of legal services may be effective.

[22A] Even if a client has validly consented to waive future conflicts, however, the lawyer must reassess the propriety of the adverse concurrent representation under paragraph (b) when an actual conflict arises. If the actual conflict is materially different from the conflict that has been waived, the lawyer may not rely on the advance consent previously obtained. Even if the actual conflict is not materially different from the conflict the client has previously waived, the client's advance consent cannot be effective if the particular circumstances that have created an actual conflict during the course of the representation would make the conflict nonconsentable under paragraph (b). *See* Comments [14]-[17] and [28] addressing nonconsentable conflicts.

Conflicts in Litigation

[23] Paragraph (b)(3) prohibits representation of opposing parties in the same litigation, regardless of the clients' consent. On the other hand, simultaneous representation of parties whose interests in litigation may conflict, such as co-plaintiffs or co-

defendants, is governed by paragraph (a)(1). A conflict may exist by reason of substantial discrepancy in the parties' testimony, incompatibility in positions in relation to an opposing party or the fact that there are substantially different possibilities of settlement of the claims or liabilities in question. Such conflicts can arise in criminal as well as civil cases. Some examples are those in which a lawyer is asked to represent co-defendants in a criminal case, co-plaintiffs or co-defendants in a personal injury case, an insured and insurer, or beneficiaries of the estate of a decedent. In a criminal case, the potential for conflict of interest in representing multiple defendants is so grave that ordinarily a lawyer should decline to represent more than one co-defendant. On the other hand, multiple representation of persons having similar interests in civil litigation is proper if the requirements of paragraph (b) are met.

[24] Ordinarily a lawyer may take inconsistent legal positions in different tribunals at different times on behalf of different clients. The mere fact that advocating a legal position on behalf of one client might create precedent adverse to the interests of a client represented by the lawyer in an unrelated matter does not create a conflict of interest. A conflict of interest exists, however, if there is a significant risk that a lawyer's action on behalf of one client will materially limit the lawyer's representation of another client in a different case; for example, when a decision favoring one client will create a precedent likely to weaken seriously the position taken on behalf of the other client. Factors relevant in determining whether the clients need to be advised of this risk include: (i) where the cases are pending, (ii) whether the issue is substantive or procedural, (iii) the temporal relationship between the matters, (iv) the significance of the issue to the immediate and long-term interests of the clients involved, and (v) the clients' reasonable expectations in retaining the lawyer. Similar concerns may be present when lawyers advocate on behalf of clients before other entities, such as regulatory authorities whose regulations or rulings may significantly implicate clients' interests. If there is significant risk of an adverse effect on the lawyer's professional judgment, then absent informed consent of the affected clients, the lawyer must decline the representation.

[25] When a lawyer represents or seeks to represent a class of plaintiffs or defendants in a class-action lawsuit, unnamed members of the class are ordinarily not considered to be clients of the lawyer for purposes of applying paragraph (a)(1). Thus, the lawyer does not typically need to get the consent of such a person before representing a client suing the person in an unrelated matter. Similarly, a lawyer seeking to represent an opponent in a class action does not typically need the consent of an unnamed member of the class whom the lawyer represents in an unrelated matter.

Nonlitigation Conflicts

[26] Conflicts of interest under paragraph (a)(1) arise in contexts other than litigation. For a discussion of such conflicts in transactional matters, *see* Comment [7]. Regarding paragraph (a)(2), relevant factors in determining whether there is a significant risk that the lawyer's professional judgment will be adversely affected include: (i) the importance of the matter to each client, (ii) the duration and intimacy of the lawyer's relationship with the client or clients involved, (iii) the functions being performed by the lawyer, (iv) the likelihood that significant disagreements will arise, (v) the likelihood that negotiations will be contentious, (vi) the likelihood that the matter will result in litigation, and (vii) the likelihood that the client will suffer prejudice from the conflict. The issue is often one of proximity (how close the situation is to open conflict) and degree (how serious the conflict will be if it does erupt). *See* Comments [8], [29] and [29A].

[27] For example, conflict questions may arise in estate planning and estate administration. A lawyer may be called upon to prepare wills for several family members, such as husband and wife, and, depending upon the circumstances, a conflict of interest may be present at the outset or may arise during the representation. In order to avoid the development of a disqualifying conflict, the lawyer should, at the outset of the common representation and as part of the process of obtaining each client's informed consent, advise each client that information will be shared (and regardless of whether it is shared, may not be privileged in a subsequent dispute between the parties) and that the lawyer will have to withdraw from one or both representations if one client decides that some matter material to the representation should be kept secret from the other. *See* Comment [31].

[28] Whether a conflict is consentable depends on the circumstances. For example, a lawyer may not represent multiple parties to a negotiation if their interests are fundamentally antagonistic to one another, but common representation is permissible where

the clients are generally aligned in interest, even though there is some difference in interest among them. Thus, a lawyer may seek to establish or adjust a relationship between clients on an amicable and mutually advantageous basis. Examples include helping to organize a business in which two or more clients are entrepreneurs, working out the financial reorganization of an enterprise in which two or more clients have an interest, and arranging a property distribution in settlement of an estate. The lawyer seeks to resolve potentially adverse interests by developing the parties' mutual interests. Otherwise, each party might have to obtain separate representation, with the possibility of incurring additional cost, complication or even litigation. Given these and other relevant factors, the clients may prefer that the lawyer act for all of them.

Special Considerations in Common Representation

[29] In civil matters, two or more clients may wish to be represented by a single lawyer in seeking to establish or adjust a relationship between them on an amicable and mutually advantageous basis. For example, clients may wish to be represented by a single lawyer in helping to organize a business, working out a financial reorganization of an enterprise in which two or more clients have an interest, arranging a property distribution of an estate or resolving a dispute between clients. The alternative to common representation can be that each party may have to obtain separate representation, with the possibility of incurring additional cost, complication or even litigation that might otherwise be avoided, or that some parties will have no lawyer at all. Given these and other relevant factors, clients may prefer common representation to separate representation or no representation. A lawyer should consult with each client concerning the implications of the common representation, including the advantages and the risks involved, and the effect on the attorney-client privilege, and obtain each client's informed consent, confirmed in writing, to the common representation.

[29A] Factors may be present that militate against a common representation. In considering whether to represent multiple clients in the same matter, a lawyer should be mindful that if the common representation fails because the potentially adverse interests cannot be reconciled, the result can be additional cost, embarrassment and recrimination. Ordinarily, absent the informed consent of all clients, the lawyer will be forced to withdraw from representing all of the clients if the common representation fails. *See* Rule 1.9(a). In some situations, the risk of failure is so great that multiple representation is plainly impossible. For example, a lawyer cannot undertake common representation of clients where contentious litigation or negotiations between them are imminent or contemplated. Moreover, because the lawyer is required to be impartial between or among commonly represented clients, representation of multiple clients is improper when it is unlikely that impartiality can be maintained. Generally, if the relationship between the parties has already assumed antagonism, it is unlikely that the clients' interests can be adequately served by common representation. For example, a lawyer who has represented one of the clients for a long period or in multiple matters might have difficulty being impartial between that client and one to whom the lawyer has only recently been introduced.

[30] A particularly important factor in determining the appropriateness of common representation is the effect on client-lawyer confidentiality and the attorney-client privilege. With regard to the attorney-client privilege, the prevailing rule is that, as between commonly represented clients, the privilege does not attach. It must therefore be assumed that if litigation eventuates between the clients, the privilege will not protect any such communications, and the clients should be so advised.

[31] As to the duty of confidentiality, continued common representation will almost certainly be inadequate if one client asks the lawyer not to disclose to the other client information relevant to the common representation. This is so because the lawyer has an equal duty of loyalty to each client, and each client has the right to be informed of anything bearing on the representation that might affect that client's interests and the right to expect that the lawyer will use that information to that client's benefit. *See* Rule 1.4. At the outset of the common representation and as part of the process of obtaining each client's informed consent, the lawyer should advise each client that information will be shared and that the lawyer will have to withdraw if one client decides that some matter material to the representation should be kept from the other. In limited circumstances, it may be appropriate for the lawyer to proceed with the representation when the clients have agreed, after being properly informed, that the lawyer will keep certain information confidential even as among the commonly represented clients. For example, the lawyer may reasonably conclude that failure to disclose one client's trade secrets to another client will not adversely affect representation involving a joint venture between the two clients and agree to keep that information confidential with the informed consent of both clients.

[32] When seeking to establish or adjust a relationship between clients, the lawyer should make clear that the lawyer's role is not that of partisanship normally expected in other circumstances and, thus, that the clients may be required to assume greater responsibility for decisions than when each client is separately represented. Any limitation on the scope of the representation made necessary as a result of the common representation should be fully explained to the clients at the outset of the representation. *See* Rule 1.2(c).

[33] Subject to the above limitations, each client in the common representation has the right to loyal and diligent representation and the protection of Rule 1.9 concerning the obligations to a former client. The client also has the right to discharge the lawyer as stated in Rule 1.16.

Organizational Clients

[34] A lawyer who represents a corporation or other organization does not, simply by virtue of that representation, necessarily represent any constituent or affiliated organization, such as a parent or subsidiary. *See* Rule 1.13(a). Although a desire to preserve good relationships with clients may strongly suggest that the lawyer should always seek informed consent of the client organization before undertaking any representation that is adverse to its affiliates, Rule 1.7 does not require the lawyer to obtain such consent unless: (i) the lawyer has an understanding with the organizational client that the lawyer will avoid representation adverse to the client's affiliates, (ii) the lawyer's obligations to either the organizational client or the new client are likely to adversely affect the lawyer's exercise of professional judgment on behalf of the other client, or (iii) the circumstances are such that the affiliate should also be considered a client of the lawyer. Whether the affiliate should be considered a client will depend on the nature of the lawyer's relationship with the affiliate or on the nature of the relationship between the client and its affiliate. For example, the lawyer's work for the client organization may be intended to benefit its affiliates. The overlap or identity of the officers and boards of directors, and the client's overall mode of doing business, may be so extensive that the entities would be viewed as "alter egos." Under such circumstances, the lawyer may conclude that the affiliate is the lawyer's client despite the lack of any formal agreement to represent the affiliate.

[34A] Whether the affiliate should be considered a client of the lawyer may also depend on: (i) whether the affiliate has imparted confidential information to the lawyer in furtherance of the representation, (ii) whether the affiliated entities share a legal department and general counsel, and (iii) other factors relating to the legitimate expectations of the client as to whether the lawyer also represents the affiliate. Where the entities are related only through stock ownership, the ownership is less than a controlling interest, and the lawyer has had no significant dealings with the affiliate or access to its confidences, the lawyer may reasonably conclude that the affiliate is not the lawyer's client.

[34B] Finally, before accepting a representation adverse to an affiliate of a corporate client, a lawyer should consider whether the extent of the possible adverse economic impact of the representation on the entire corporate family might be of such a magnitude that it would materially limit the lawyer's ability to represent the client opposing the affiliate. In those circumstances, Rule 1.7 will ordinarily require the lawyer to decline representation adverse to a member of the same corporate family, absent the informed consent of the client opposing the affiliate of the lawyer's corporate client.

Lawyer as Corporate Director

[35] A lawyer for a corporation or other organization who is also a member of its board of directors should determine whether the responsibilities of the two roles may conflict. The lawyer may be called on to advise the corporation in matters involving actions of the directors. Consideration should be given to the frequency with which such situations may arise, the potential intensity of the conflict, the effect of the lawyer's resignation from the board, and the possibility of the corporation's obtaining legal advice from another lawyer in such situations. If there is material risk that the dual role will compromise the lawyer's professional judgment, the lawyer should not serve as a director or should cease to act as the corporation's lawyer when conflicts of interest arise. The lawyer should advise the other members of the board that, in some circumstances, matters discussed at

board meetings while the lawyer is present in the capacity of director might not be protected by the attorney-client privilege and that conflict of interest considerations might require the lawyer's recusal as a director or might require the lawyer and the lawyer's firm to decline representation of the corporation in a matter.

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Client-Lawyer Relationship

Rules of Prof. Con., Rule 1.15 McK.Consol.Laws, Book 29 App.

Rule 1.15. Preserving Identity of Funds and Property of Others; Fiduciary Responsibility; Commingling and Misappropriation of Client Funds or Property; Maintenance of Bank Accounts; Record Keeping; Examination of Records

Currentness

(a) Prohibition Against Commingling and Misappropriation of Client Funds or Property.

A lawyer in possession of any funds or other property belonging to another person, where such possession is incident to his or her practice of law, is a fiduciary, and must not misappropriate such funds or property or commingle such funds or property with his or her own.

(b) Separate Accounts.

(1) A lawyer who is in possession of funds belonging to another person incident to the lawyer's practice of law shall maintain such funds in a banking institution within New York State that agrees to provide dishonored check reports in accordance with the provisions of 22 N.Y.C.R.R. Part 1300. "Banking institution" means a state or national bank, trust company, savings bank, savings and loan association or credit union. Such funds shall be maintained, in the lawyer's own name, or in the name of a firm of lawyers of which the lawyer is a member, or in the name of the lawyer or firm of lawyers by whom the lawyer is employed, in a special account or accounts, separate from any business or personal accounts of the lawyer or lawyer's firm, and separate from any accounts that the lawyer may maintain as executor, guardian, trustee or receiver, or in any other fiduciary capacity; into such special account or accounts all funds held in escrow or otherwise entrusted to the lawyer or firm shall be deposited; provided, however, that such funds may be maintained in a banking institution located outside New York State if such banking institution complies with 22 N.Y.C.R.R. Part 1300 and the lawyer has obtained the prior written approval of the person to whom such funds belong specifying the name and address of the office or branch of the banking institution where such funds are to be maintained.

(2) A lawyer or the lawyer's firm shall identify the special bank account or accounts required by Rule 1.15(b)(1) as an "Attorney Special Account," "Attorney Trust Account," or "Attorney Escrow Account," and shall obtain checks and deposit slips that bear such title. Such title may be accompanied by such other descriptive language as the lawyer may deem appropriate, provided that such additional language distinguishes such special account or accounts from other bank accounts that are maintained by the lawyer or the lawyer's firm.

(3) Funds reasonably sufficient to maintain the account or to pay account charges may be deposited therein.

(4) Funds belonging in part to a client or third person and in part currently or potentially to the lawyer or law firm shall be kept in such special account or accounts, but the portion belonging to the lawyer or law firm may be withdrawn when due unless the right of the lawyer or law firm to receive it is disputed by the client or third person, in which event the disputed portion shall not be withdrawn until the dispute is finally resolved.

(c) Notification of Receipt of Property; Safekeeping; Rendering Accounts; Payment or Delivery of Property.

A lawyer shall:

(1) promptly notify a client or third person of the receipt of funds, securities, or other properties in which the client or third person has an interest;

(2) identify and label securities and properties of a client or third person promptly upon receipt and place them in a safe deposit box or other place of safekeeping as soon as practicable;

(3) maintain complete records of all funds, securities, and other properties of a client or third person coming into the possession of the lawyer and render appropriate accounts to the client or third person regarding them; and

(4) promptly pay or deliver to the client or third person as requested by the client or third person the funds, securities, or other properties in the possession of the lawyer that the client or third person is entitled to receive.

(d) Required Bookkeeping Records.

(1) A lawyer shall maintain for seven years after the events that they record:

(i) the records of all deposits in and withdrawals from the accounts specified in Rule 1.15(b) and of any other bank account that concerns or affects the lawyer's practice of law; these records shall specifically identify the date, source and description of each item deposited, as well as the date, payee and purpose of each withdrawal or disbursement;

(ii) a record for special accounts, showing the source of all funds deposited in such accounts, the names of all persons for whom the funds are or were held, the amount of such funds, the description and amounts, and the names of all persons to whom such funds were disbursed;

(iii) copies of all retainer and compensation agreements with clients;

(iv) copies of all statements to clients or other persons showing the disbursement of funds to them or on their behalf;

(v) copies of all bills rendered to clients;

(vi) copies of all records showing payments to lawyers, investigators or other persons, not in the lawyer's regular employ, for services rendered or performed;

(vii) copies of all retainer and closing statements filed with the Office of Court Administration; and

(viii) all checkbooks and check stubs, bank statements, prenumbered canceled checks and duplicate deposit slips.

(2) Lawyers shall make accurate entries of all financial transactions in their records of receipts and disbursements, in their special accounts, in their ledger books or similar records, and in any other books of account kept by them in the regular course of their practice, which entries shall be made at or near the time of the act, condition or event recorded.

(3) For purposes of Rule 1.15(d), a lawyer may satisfy the requirements of maintaining "copies" by maintaining any of the following items: original records, photocopies, microfilm, optical imaging, and any other medium that preserves an image of the document that cannot be altered without detection.

(e) Authorized Signatories.

All special account withdrawals shall be made only to a named payee and not to cash. Such withdrawals shall be made by check or, with the prior written approval of the party entitled to the proceeds, by bank transfer. Only a lawyer admitted to practice law in New York State shall be an authorized signatory of a special account.

(f) Missing Clients.

Whenever any sum of money is payable to a client and the lawyer is unable to locate the client, the lawyer shall apply to the court in which the action was brought if in the unified court system, or, if no action was commenced in the unified court system, to the Supreme Court in the county in which the lawyer maintains an office for the practice of law, for an order directing payment to the lawyer of any fees and disbursements that are owed by the client and the balance, if any, to the Lawyers' Fund for Client Protection for safeguarding and disbursement to persons who are entitled thereto.

(g) Designation of Successor Signatories.

(1) Upon the death of a lawyer who was the sole signatory on an attorney trust, escrow or special account, an application may be made to the Supreme Court for an order designating a successor signatory for such trust, escrow or special account, who shall be a member of the bar in good standing and admitted to the practice of law in New York State.

(2) An application to designate a successor signatory shall be made to the Supreme Court in the judicial district in which the deceased lawyer maintained an office for the practice of law. The application may be made by the legal representative of the deceased lawyer's estate; a lawyer who was affiliated with the deceased lawyer in the practice of law; any person who has a beneficial interest in such trust, escrow or special account; an officer of a city or county bar association; or counsel for an attorney disciplinary committee. No lawyer may charge a legal fee for assisting with an application to designate a successor signatory pursuant to this Rule.

(3) The Supreme Court may designate a successor signatory and may direct the safeguarding of funds from such trust, escrow or special account, and the disbursement of such funds to persons who are entitled thereto, and may order that funds in such account be deposited with the Lawyers' Fund for Client Protection for safeguarding and disbursement to persons who are entitled thereto.

(h) Dissolution of a Firm.

Upon the dissolution of any firm of lawyers, the former partners or members shall make appropriate arrangements for the maintenance, by one of them or by a successor firm, of the records specified in Rule 1.15(d).

(i) Availability of Bookkeeping Records: Records Subject to Production in Disciplinary Investigations and Proceedings.

The financial records required by this Rule shall be located, or made available, at the principal New York State office of the lawyers subject hereto, and any such records shall be produced in response to a notice or subpoena duces tecum issued in connection with a complaint before or any investigation by the appropriate grievance or departmental disciplinary committee, or shall be produced at the direction of the appropriate Appellate Division before any person designated by it. All books and records produced pursuant to this Rule shall be kept confidential, except for the purpose of the particular proceeding, and their contents shall not be disclosed by anyone in violation of the attorney-client privilege.

(j) Disciplinary Action.

A lawyer who does not maintain and keep the accounts and records as specified and required by this Rule, or who does not produce any such records pursuant to this Rule, shall be deemed in violation of these Rules and shall be subject to disciplinary proceedings.

Comment

[1] A lawyer should hold the funds and property of others using the care required of a professional fiduciary. Securities and other property should be kept in a safe deposit box, except when some other form of safekeeping is warranted by special circumstances. All property that is the property of clients or third persons, including prospective clients, must be kept separate from the lawyer's business and personal property and, if monies, in one or more trust accounts, including an account established pursuant to the "Interest on Lawyer Accounts" law where appropriate. *See* State Finance Law § 97-v(4)(a); Judiciary Law § 497(2); 21 N.Y.C.R.R. § 7000.10. Separate trust accounts may be warranted or required when administering estate monies or acting in similar fiduciary capacities.

[2] While normally it is impermissible to commingle the lawyer's own funds with client funds, paragraph (b)(3) provides that it is permissible when necessary to pay bank service charges on that account. Accurate records must be kept regarding which portion of the funds belongs to the lawyer.

[3] Lawyers often receive funds from which the lawyer's fee will or may be paid. A lawyer is not required to remit to the client funds that the lawyer reasonably believes represent fees owed to the lawyer. However, a lawyer may not withhold the client's share of the funds to coerce the client into accepting the lawyer's claim for fees. While a lawyer may be entitled under applicable law to assert a retaining lien on funds in the lawyer's possession, a lawyer may not enforce such a lien by taking the lawyer's fee from funds that the lawyer holds in an attorney's trust account, escrow account or special account, except as may be provided in an applicable agreement or directed by court order. Furthermore, any disputed portion of the funds must be kept in or transferred into a trust account, and the lawyer should suggest means for prompt resolution of the dispute, such as arbitration. The undisputed portion of the funds is to be distributed promptly.

[4] Paragraph (c)(4) also recognizes that third parties may have lawful claims against specific funds or other property in a lawyer's custody, such as a client's creditor who has a lien on funds recovered in a personal injury action. A lawyer may have a duty under applicable law to protect such third-party claims against wrongful interference by the client. In such cases, when the third-party claim is not frivolous under applicable law, the lawyer must refuse to surrender the property to the client until the claims are resolved. A lawyer should not unilaterally assume to arbitrate a dispute between the client and the third party, but, when there are substantial grounds for dispute as to the person entitled to the funds, the lawyer may file an action to have a court resolve the dispute.

[5] The obligations of a lawyer under this Rule are independent of those arising from activity other than rendering legal services. For example, a lawyer who serves only as an escrow agent is governed by the applicable law relating to fiduciaries even though the lawyer does not render legal services in the transaction and is not governed by this Rule.

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Rules of Prof. Con., Rule 1.18 McK.Consol.Laws, Book 29 App.

Rule 1.18. Duties to Prospective Clients

Currentness

(a) Except as provided in Rule 1.18(e), a person who consults with a lawyer about the possibility of forming a client-lawyer relationship with respect to a matter is a prospective client.

(b) Even when no client-lawyer relationship ensues, a lawyer who has learned information from a prospective client shall not use or reveal that information, except as Rule 1.9 would permit with respect to information of a former client.

(c) A lawyer subject to paragraph (b) shall not represent a client with interests materially adverse to those of a prospective client in the same or a substantially related matter if the lawyer received information from the prospective client that could be significantly harmful to that person in the matter, except as provided in paragraph (d). If a lawyer is disqualified from representation under this paragraph, no lawyer in a firm with which that lawyer is associated may knowingly undertake or continue representation in such a matter, except as provided in paragraph (d).

(d) When the lawyer has received disqualifying information as defined in paragraph (c), representation is permissible if:

(1) both the affected client and the prospective client have given informed consent, confirmed in writing; or

(2) the lawyer who received the information took reasonable measures to avoid exposure to more disqualifying information than was reasonably necessary to determine whether to represent the prospective client; and

(i) the firm acts promptly and reasonably to notify, as appropriate, lawyers and nonlawyer personnel within the firm that the personally disqualified lawyer is prohibited from participating in the representation of the current client;

(ii) the firm implements effective screening procedures to prevent the flow of information about the matter between the disqualified lawyer and the others in the firm;

(iii) the disqualified lawyer is apportioned no part of the fee therefrom; and

(iv) written notice is promptly given to the prospective client; and

(3) a reasonable lawyer would conclude that the law firm will be able to provide competent and diligent representation in the matter.

(e) A person is not a prospective client within the meaning of paragraph (a) if the person:

(1) communicates information unilaterally to a lawyer, without any reasonable expectation that the lawyer is willing to discuss the possibility of forming a client-lawyer relationship; or

(2) communicates with a lawyer for the purpose of disqualifying the lawyer from handling a materially adverse representation on the same or a substantially related matter.

Comment

[1] Prospective clients, like current clients, may disclose information to a lawyer, place documents or other property in the lawyer's custody, or rely on the lawyer's advice. A lawyer's consultations with a prospective client usually are limited in time and depth and leave both the prospective client and the lawyer free (and sometimes required) to proceed no further. Prospective clients should therefore receive some, but not all, of the protection afforded clients.

[2] A person becomes a prospective client by consulting with a lawyer about the possibility of forming client-lawyer relationship with respect to a matter. Whether communications, including written, oral, or electronic communications, constitute a consultation depends on the circumstances. For example, a consultation is likely to have occurred of a lawyer, either in person or through the lawyer's advertising in any medium, specifically requests or invites the submission of information about a potential representation without clear and reasonably understandable warnings and cautionary statements that limit the lawyer's obligations, and a person provides information in response. In contrast, a consultation does not occur of a person provides information to a lawyer in response to advertising that merely describes the lawyer's education, experience, areas of practice, and contact information, or provides legal information of general interest. Such a person communicates information unilaterally to lawyer without any reasonable expectation that the lawyer is willing to discuss the possibility of forming a client-lawyer relationship, and is thus not a "prospective client." Moreover, a person who communicates with a lawyer for the purpose of disqualifying the lawyer is not a "prospective client" -- *see* Rule 1.18(e).

[3] It is often necessary for a prospective client to reveal information to the lawyer during an initial consultation prior to the decision about formation of a client-lawyer relationship. The lawyer often must learn such information to determine whether there is a conflict of interest with an existing client and whether the matter is one that the lawyer is willing to undertake. Paragraph (b) prohibits the lawyer from using or revealing that information, except as permitted by Rule 1.9, even if the client or lawyer decides not to proceed with the representation. The duty exists regardless of how brief the initial conference may be.

[4] In order to avoid acquiring disqualifying information from a prospective client, a lawyer considering whether to undertake a new matter should limit the initial consultation to only such information as reasonably appears necessary for that purpose. Where the information indicates that a conflict of interest or other reason for non-representation exists, the lawyer should so inform the prospective client or decline the representation. If the prospective client wishes to retain the lawyer, and if consent is possible under Rule 1.7 or Rule 1.9, then consent from all affected current or former clients must be obtained before accepting the representation. The representation must be declined if the lawyer will be unable to provide competent, diligent and adequate representation to the affected current and former clients and the prospective client.

[5] A lawyer may condition a consultation with a prospective client on the person's informed consent that no information disclosed during the consultation will prohibit the lawyer from representing a different client in the matter. *See* Rule 1.0(j) for the definition of "informed consent," and with regard to the effectiveness of an advance waiver *see* Rule 1.7, Comments [22]-[22A] and Rule 1.9, Comment [9]. If permitted by law and if the agreement expressly so provides, the prospective client may also consent to the lawyer's subsequent use of information received from the prospective client.

[6] Under paragraph (c), even in the absence of an agreement the lawyer is not prohibited from representing a client with interests adverse to those of the prospective client in the same or a substantially related matter unless the lawyer has received from the prospective client information that could be significantly harmful if used in that matter.

[7] Under paragraph (c), the prohibition in this Rule is imputed to other lawyers as provided in Rule 1.10, but, under paragraph (d)(1), imputation may be avoided if the lawyer obtains the informed consent, confirmed in writing, of both the prospective and affected clients. In the alternative, imputation may be avoided if the conditions of paragraph (d)(2) are met and all disqualified lawyers are timely screened, and written notice is promptly given to the prospective client. *See* Rule 1.10. Paragraph (d)(2)(i) does not prohibit the screened lawyer from receiving a salary or partnership share established by prior independent agreement, but that lawyer may not receive compensation directly related to the matter in which the lawyer is disqualified. Before proceeding under paragraph (d)(1) or paragraph (d)(2), however, a lawyer must be mindful of the requirement of paragraph (d)(3) that "a reasonable lawyer would conclude that the law firm will be able to provide competent and diligent representation in the matter."

[7A] Paragraph (d)(2) sets out the basic procedural requirements that a law firm must satisfy to ensure that a personally disqualified lawyer is effectively screened from participation in the matter. This Rule requires that the firm promptly: (i) notify, as appropriate, lawyers and relevant nonlawyer personnel within the firm that the personally disqualified lawyer is prohibited from participating in the representation of the current client, and (ii) implement effective screening procedures to prevent the flow of information about the matter between the personally disqualified lawyer and others in the firm.

[7B] A firm seeking to avoid disqualification under this Rule should also consider its ability to implement, maintain, and monitor the screening procedures permitted by paragraph (d)(2) before undertaking or continuing the representation. In deciding whether the screening procedures permitted by this Rule will be effective to avoid imputed disqualification, a firm should consider a number of factors, including how the size, practices and organization of the firm will affect the likelihood that any confidential information acquired about the matter by the personally disqualified lawyer can be protected. If the firm is large and is organized into separate departments, or maintains offices in multiple locations, or for any reason the structure of the firm facilitates preventing the sharing of information with lawyers not participating in the particular matter, it is more likely that the requirements of this Rule can be met and imputed disqualification avoided. Although a large firm will find it easier to maintain effective screening, lack of timeliness in instituting, or lack of vigilance in maintaining, the procedures required by this Rule may make those procedures ineffective in avoiding imputed disqualification. If a personally disqualified lawyer is working on other matters with lawyers who are participating in a matter requiring screening, it may be impossible to maintain effective screening procedures. The size of the firm may be considered as one of the factors affecting the firm's ability to institute and maintain effective screening procedures, but it is not a dispositive factor. A small firm may need to exercise special care and vigilance to maintain effective screening but, if appropriate precautions are taken, small firms can satisfy the requirements of paragraph (d)(2).

[7C] In order to prevent any other lawyer in the firm from acquiring confidential information about the matter from the disqualified lawyer, it is essential that notification be given and screening procedures implemented promptly. If any lawyer in the firm acquires confidential information about the matter from the disqualified lawyer, the requirements of this Rule cannot be met, and any subsequent efforts to institute or maintain screening will not be effective in avoiding the firm's disqualification. Other factors may affect the likelihood that screening procedures will be effective in preventing the flow of confidential information between the disqualified lawyer and other lawyers in the firm in a given matter.

[8] Notice under paragraph (d)(2), including a general description of the subject matter about which the lawyer was consulted and of the screening procedures employed, generally should be given as soon as practicable after the need for screening becomes apparent.

[9] For the duty of competence of a lawyer who gives assistance on the merits of a matter to a prospective client, *see* Rule 1.1. For a lawyer's duties when a prospective client entrusts valuables or papers to the lawyer's care, *see* Rule 1.15.

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Maintaining the Integrity of the Profession

Rules of Prof. Con., Rule 8.3 McK.Consol.Laws, Book 29 App.

Rule 8.3. Reporting Professional Misconduct

Currentness

(a) A lawyer who knows that another lawyer has committed a violation of the Rules of Professional Conduct that raises a substantial question as to that lawyer's honesty, trustworthiness or fitness as a lawyer shall report such knowledge to a tribunal or other authority empowered to investigate or act upon such violation.

(b) A lawyer who possesses knowledge or evidence concerning another lawyer or a judge shall not fail to respond to a lawful demand for information from a tribunal or other authority empowered to investigate or act upon such conduct.

(c) This Rule does not require disclosure of:

(1) information otherwise protected by Rule 1.6; or

(2) information gained by a lawyer or judge while participating in a bona fide lawyer assistance program.

Comment

[1] Self-regulation of the legal profession requires that members of the profession initiate disciplinary investigation when they know of a violation of the Rules of Professional Conduct. Lawyers have a similar obligation to cooperate with authorities empowered to investigate judicial misconduct. An apparently isolated violation may indicate a pattern of misconduct that only a disciplinary investigation can uncover. Reporting a violation is especially important where the victim is unlikely to discover the offense.

[2] A report about misconduct is not required where it would result in violation of Rule 1.6. However, a lawyer should encourage a client to consent to disclosure where prosecution would not substantially prejudice the client's interests.

[3] If a lawyer were obliged to report every violation of the Rules, the failure to report any violation would itself be a professional offense. Such a requirement existed in many jurisdictions, but proved to be unenforceable. This Rule limits the reporting obligation to those offenses that a self-regulating profession must vigorously endeavor to prevent. A measure of judgment is therefore required in complying with the provisions of this Rule. The term "substantial" refers to the seriousness of the possible offense and not the quantum of evidence of which the lawyer is aware. A report should be made to a tribunal or other authority empowered to investigate or act upon the violation.

[3A] Paragraph (b) requires a lawyer in certain situations to respond to a lawful demand for information concerning another lawyer or a judge. This Rule is subject to the provisions of the Fifth Amendment to the United States Constitution and corresponding provisions of state law. A person relying on such a provision in response to a question, however, should do so openly and not use the right of nondisclosure as a justification for failure to comply with this Rule.

[4] The duty to report professional misconduct does not apply to a lawyer retained to represent a lawyer whose professional conduct is in question. Such a situation is governed by the Rules applicable to the client-lawyer relationship.

[5] Information about a lawyer's or judge's misconduct or fitness may be received by a lawyer in the course of that lawyer's participation in a bona fide assistance program for lawyers or judges. In that circumstance, providing for an exception to the reporting requirements of paragraphs (a) and (b) encourages lawyers and judges to seek assistance and treatment through such a program. Without such an exception, lawyers and judges may hesitate to seek assistance and treatment from these programs, and this may result in additional harm to their professional careers and additional injury to the welfare of clients and the public.

Rules of Prof. Con., Rule 8.3 McK. Consol. Laws, Book 29 App., NY ST RPC Rule 8.3
Current with amendments through Oct. 1, 2020.

End of Document

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Committee on Professional Ethics

Opinion 816 (10/26/07)

Topic: Advance payment retainer; client trust account.

Digest: A lawyer may ethically accept an advance payment retainer, place such funds in the lawyer's own account, and retain any interest earned. The Lawyer may require the client to forward an advance payment retainer to pay for final fees that accrue at the end of the relationship.

Rules: DR 2-106(C), DR 2-110(A); DR 9-102(A), (C).

QUESTION

1. May a lawyer ethically accept an advance payment retainer and place such funds in the lawyer's own account while retaining any interest earned from such amount?

2. If so, may a lawyer request the client to forward an advance payment retainer to pay for final fees that accrue at the very end of the relationship, with interim fees billed out as they are performed?

OPINION

3. Recently, we have received inquiries regarding the continued validity of our opinion in N.Y. State 570 (1985), which addressed the ethical propriety of what is commonly known as an advance payment retainer. An advance payment retainer is a sum provided by the client to the lawyer to cover payment of legal fees expected to be earned during the representation. To the extent the fees advanced are not earned during the representation, the lawyer agrees to return them to the client. This form of retainer should be distinguished from a general retainer, which is a sum paid to the

lawyer for being available to the client. A general retainer is earned upon receipt.[1] The recent inquiries regarding advance payment retainers may stem from the fact that since we issued Opinion 570 in 1985, there have been several significant developments on the subject of retainer agreements and the language in DR 9-102 has been substantially amended. Therefore, it is now appropriate to revisit the principles stated in N.Y. State 570.

4. In New York State 570 we concluded that fees paid to a lawyer in advance of services rendered are not necessarily client funds and need not be deposited in a client trust account. Therefore, any interest earned on these fee advances may be retained by the lawyer. The opinion cautioned, however, that the lawyer is obliged to return any portion of the fee advance that is not earned during the representation.[2]

5. If the parties agree to treat advance payment of fees as the lawyer's own, the lawyer may not deposit the fee advances in a client trust account, as this would constitute impermissible commingling.[3] "On the other hand, the lawyer may agree to treat advance payment of legal fees as client funds and deposit them in a client trust account; in that event any interest earned on the funds while in the client trust account must be remitted to the client."[4]

6. Since 1985, we have cited N.Y. State 570 on several occasions.[5] N.Y. State 570 has also been cited with approval by the Appellate Division, Fourth Department and the New York city Bar ethics committee.[6] The validity of such an advance payment retainer has also been recently recognized by the Supreme Court of Illinois.[7]

7. In opinion 570, we noted that "it appears that the drafters of the Code of Professional Responsibility did not consider advance payments of fees to be client funds necessitating their deposit in a trust account." Although DR 9-102 has been substantially amended since 1985, the changes do not affect the reasoning of that opinion. DR 2-110(A)(3) requires a lawyer who withdraws from representing a client to "refund promptly any part of a fee paid in advance that has not been earned." As we observed in Opinion 570, this provision does not require that the advance be deposited in a client rust account until earned. This conclusion is supported by the language in DR 2-110(A), which still separately classifies fee advances and client property. DR 2-110(A)(2) requires a lawyer planning to withdraw from representing a client to "deliver to

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[1] *See* N.Y. State 570 n. 1.

[2] *See* DR 2-110(A)(3) ("A lawyer who withdraws from employment shall refund promptly any part of a fee paid in advance that has not been earned.").

[3] *See* DR 9-102(A)(lawyer may not commingle client funds on property with his or her own).

[4] N.Y. State 570

[5] See, .e.g., N.Y. State 599 (1989) discussing nonrefundable minimum fee provisions); N.Y. State 693 (1997); N.Y. State 764 (2003).

[6] See Matter of Aquilo, 162 A.D.2d 58, 560 N.Y.S.2d 583 (4th Dep't 1990) ("Moneys advanced by clients for disbursements need not, unless expressly agreed, but held in trust and may be placed in a general account."); N.Y. City 2002-2.

[7] Dowling v. Chicago Options Associates, Inc., ___N.E.2d ___, 2007 WL 1288279, at *7 (Ill., May 3, 2007) ("we recognize advance payment retainers as one of three retainers available to lawyers and their clients").

the client all papers and property to which the client is entitled" while DR 2-110(A)(3) separately provides for the refund of any unearned "fee paid in advance." In sum, the standards delineated in N.Y. State 570 for advance payment retainers are still valid today.

8. We note that advance payment retainer agreements, like any other fee agreement between a lawyer and client, must be "fair, reasonable, and fully know and understood by the client."[8] These agreements must also comply with other relevant provisions of the Code. In this respect, we construe DR 9-12 to require the lawyer to maintain complete records of any advance payment retainer received and to render appropriate account to the client regarding the retainer.[9] Although the advance payment retainer is not client property, the client retains an interest in that portion of the retainer that is not yet earned by the lawyer. Furthermore, at the conclusion of the representation the lawyer must promptly return any portion of the advance payment retainer that is not earned.[10] Finally, it would be inappropriate for a lawyer to negotiate a nonrefundable advance payment retainer with the client.[11]

9. An advance payment retainer will obviously benefit the lawyer by helping to ensure that he or she will be paid for services rendered, at least to the extent of the advance. This form of arrangement can also benefit the client, who may wish to hire counsel to defend the client from judgment creditors. If the lawyer deposited such a retainer in a client trust account, the funds would remain the property of the client and might be subject to claims of the client's creditors, thereby making it difficult for the client to retain counsel.[12] Therefore, it is imperative for a lawyer at the outset of the representation to discuss the advantages and disadvantages of advance payment retainers and to reach an agreement about the treatment of any such advances. These agreements should be confirmed in writing in the engagement letter where one is required.[13]

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[8] *Jacobson v. Sassower*, 66 N.Y.2d 991, 993, 489 N.E.2d 1283, 1284, 499 N.Y.S.2d 381 (1985); see N.Y. State 599 ("The essence of the matter is clarity").

[9] DR 9-102©(3) requires a lawyer to "[m]aintain complete records of all funds, securities, and other properties of a client or third person coming into possession of the lawyer and render appropriate accounts to the client or third person regarding them."

[10] DR 9-102©(4) (requiring a lawyer to "pay or deliver to the client or third person as requested by the client or third person the funds, securities or other properties in the possession of the lawyer which the client or third person is entitled to receive").

[11] *See* DR 2-106©(2)(b) (prohibiting use of a nonrefundable fee clause in a domestic relations matter); Matter of Cooperman, 83 N.Y.2d 465, 633 N.E.2d 1069, 611 N.Y.S.2d (1994) (holding that the payment of a nonrefundable fee for specific services, in advance and irrespective of whether professional services are actually rendered, is per se violative of public policy).

[12] *See, e. g.*, Dowling, ___N.E.2d at___, 2007 wl 1288279, AT *8 ("Paying the lawyer a security retainer means the funds remain the property of the client and may therefore be subject to the claims of the client's creditors. This could make it difficult for the client to hire legal counsel. Similarly, a criminal defendant whose property may be subject to forfeiture may wish to use an advance payment retainer to ensure that he or she has sufficient funds to secure legal representation.").

[13] *See* 22 NYCRR Part 1215 (engagement letters are to include, among other things, an [e]xplanation of attorney's fees to be charged, expenses and billing practices").

10. We also conclude that an attorney may request an advance payment retainer for final fees that accrue at the very end of the relationship, with interim fees filled out as they are performed. While such an arrangement is permissible, it must comply with the standards outlined in *Jacobson* and our prior opinions. If the advance payment retainer is intended to be payable only once specific services use performed, it must describe the services that it is intended to cover. If the services outlined in the agreement are not provided, that portion of the advance payment retainer must be promptly returned to the client.[14]

CONCLUSION

11. A lawyer may ethically accept an advance payment retainer and need not place such funds in a client trust account. If the advance payment retainer is placed in the lawyer's account, the lawyer may retain any interest earned from such amount. A lawyer may request an advance payment retainer for final fees that accrue at the very end of the relationship.

(14-07)

[14] *See* DR 2-110(A)(3); DR 9-102(C)(4); N.Y. State 570.

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Committee on Professional Ethics

Opinion 854 (3/11/11)

Topic: Reporting known or suspected violation of Rules of Professional Conduct by another lawyer.

Digest: Lawyer who was employed by another lawyer must report knowledge of former employer's violation of the Rules of Professional Conduct if the violation raises a substantial question about the employer's honesty, trustworthiness, or fitness as a lawyer and if the report does not disclose confidential information. If the former employee lacks knowledge, he may report a good faith belief or suspicion of the former employer's professional misconduct to an appropriate authority if the report does not disclose confidential information, but may not communicate that belief or suspicion to the employer's clients.

Rules: 1.6, 8.3(a) & (c).

FACTS

1. Lawyer A (for "Associate") was formerly employed by another lawyer, Lawyer P (for "Partner"). Lawyer A believes that Lawyer P wrongfully failed to pay wages and premiums on employer-provided health insurance, overbilled clients, and misrepresented to his clients the services that he could perform for them. (Lawyer A does not suggest that any of the clients were his personal clients, and we assume for purposes of this inquiry that they were not.)

QUESTION

2. Lawyer A (the inquirer) has raised two related questions:

> A. May (or must) Lawyer A report Lawyer P's alleged misconduct to a disciplinary authority?
>
> B. May (or must) Lawyer A inform Lawyer P's clients about Lawyer P's alleged misconduct?

OPINION

Question A: May (or must) Lawyer A report Lawyer P's alleged misconduct to a disciplinary authority?

3. The most relevant rule in the New York Rules of Professional Conduct (the "Rules") is Rule 8.3. That rule provides, in pertinent part:

> (a) A lawyer who knows that another lawyer has committed a violation of the Rules of Professional Conduct that raises a substantial question as to that lawyer's honesty, trustworthiness or fitness as a lawyer shall report such knowledge to a tribunal or other authority empowered to investigate or act upon such violation.
>
> * * * * *
>
> (c) This Rule does not require disclosure of:
>
> (1) information otherwise protected by Rule 1.6; or
>
> (2) information gained by a lawyer or judge while participating in a bona fide lawyer assistance program.

4. In N.Y. State 635 (1992), which construed DR 1-103 (the nearly identical predecessor to Rule 8.3), this Committee opined that a lawyer in Lawyer A's situation *must* report professional misconduct by another lawyer (here, Lawyer P) if four criteria are satisfied. Those criteria are consistent with the New York Rules of Professional Conduct that took effect on April 1, 2009. The four criteria are as follows:

A. Lawyer A has "actual knowledge" or a "clear belief" as to the pertinent facts, *i.e.,* more than a "mere suspicion" or a "reasonable belief";
B. None of the information that would be essential for Lawyer A's report is protected as confidential information (see Rule 8.3(c)(1)) and none of the information was gained while participating in a bona fide lawyer assistance program (see Rule 8.3(c)(2));

C. Based upon Lawyer A's knowledge about the facts, Lawyer A knows or has a "clear belief" that Lawyer P has violated one or more Rules of Professional Conduct; and
D. The violation "raises a substantial question" as to Lawyer P's "honesty, trustworthiness or fitness as a lawyer" (Rule 8.3(a)).

5. As in N.Y. State 635, we express no opinion here on the question whether Lawyer P's alleged conduct was a "violation of the Rules of Professional Conduct" or, if it was, whether the violation raises a "substantial question" as to Lawyer P's "honesty, trustworthiness or fitness as a lawyer ...." Rule 8.3(a). Answering those questions would require us to make factual determinations about circumstances that may well be disputed, and would require us to evaluate the past conduct of an attorney other than the inquirer. As in N.Y. State 635, "It is for [Lawyer A] to determine, based on his knowledge of all the pertinent facts and circumstances, whether the foregoing prerequisites have been met" and, therefore, whether Lawyer A *must* report Lawyer P's misconduct to an appropriate tribunal or disciplinary authority.

6. Even if Lawyer A determines that he is not *required* to report lawyer P, he is nevertheless *permitted* to report his reasonable suspicions of misconduct if the report does not reveal confidential information protected by Rule 1.6. "As a general proposition, a lawyer is always free to report evidence of what may constitute improper conduct by another attorney, subject to the obligations to preserve client confidences and secrets. The lawyer need not have actual proof of misconduct; a good faith belief or suspicion that misconduct has been committed is a sufficient basis for making a report." N.Y. State 635 at p. 4, *citing* N.Y. State 480 (1978.) *See also* SIMON'S NEW YORK CODE OF PROFESSIONAL RESPONSIBILITY ANNOTATED 77 (2008 ed.) ("a lawyer may report another lawyer based on rumor, suspicion, or hearsay, and may report activities raising less-than-substantial questions about a lawyer's fitness as a lawyer").

7. But the freedom to report a good faith belief or suspicion of misconduct should not become a pretext for a report intended "to gain advantages or concessions from other lawyers in the course of litigation, in private business transactions, or in interpersonal relationships, or by attorneys acting purely out of spite." N.Y. State 635 at p. 4. Even though disciplinary complaints are confidential under Judiciary Law §90, "it would be patently improper for a lawyer to make a report of misconduct and subject another lawyer to investigation without having a reasonable basis for doing so or solely to gain a tactical advantage in a matter." *Id.* (citations omitted). *See also* SIMON'S NEW YORK CODE OF PROFESSIONAL RESPONSIBILITY ANNOTATED, *supra,* at 78 (mandatory reporting rule "should not be used as a weapon against opposing lawyers or competing law firms").

Question B: May (or must) Lawyer A inform Lawyer P's clients about Lawyer P's alleged misconduct?

8. Lawyer A is not *required* to inform Lawyer P's clients about Lawyer P's alleged misconduct. However, assuming Lawyer A does not improperly disclose confidential information concerning any client, and assuming Lawyer A acts in good faith, Lawyer A is

permitted to disclose knowledge (as distinguished from a suspicion) of Lawyer P's misconduct to the affected client or clients. (Whether such a disclosure could violate the dictate of § 90 of the New York Judiciary Law that disciplinary complaints shall be confidential unless and until professional discipline is publically imposed is a question of law as to which we offer no opinion.)

9. However, before making any such discretionary report to Lawyer P's clients, Lawyer A should carefully consider the dangers of informing another lawyer's clients about that lawyer's misconduct. As this Committee observed in N.Y. State 480 (1978), the dangers inherent in reporting another lawyer's misconduct to that lawyer's clients are greater than the dangers of reporting the lawyer's misconduct to appropriate authorities. In particular, divulging another lawyer's alleged misconduct to that lawyer's clients may unnecessarily endanger that lawyer's attorney-client relationships.

10. Moreover, a lawyer may not inform another lawyer's clients about mere suspicions of the other lawyer's misconduct. We recognized in N.Y. State 480 that a lawyer may properly report mere suspicions to an appropriate authority, but we perceived "a substantial danger in permitting a lawyer to approach present clients of the suspected counsel" because in that instance "the sanctity of the attorney-client relationship weighs far more heavily in favor of proscribing the communication. ... Usually the interests of all can best be served by reporting suspicious conduct to an appropriate authority. The former client's confidence in his present counsel should not be jeopardized unnecessarily."

11. In deciding whether to disclose either actual knowledge or a clear, good faith belief of misconduct by another lawyer to anyone other than an appropriate tribunal or disciplinary authority, therefore, a lawyer should carefully weigh (i) the certainty or uncertainty of his belief (*i.e.,* whether the belief rises to the level of knowledge or a clear belief, as opposed to a mere suspicion), (ii) the risk of unnecessary and perhaps unwarranted damage to the other lawyer's attorney-client relationships, and (iii) the countervailing risks of irreparable injury to the interests of the other lawyer's clients absent prompt and effective disclosure to them.

CONCLUSION

12. Lawyer A must report the conduct of his former employer, Lawyer P, to an appropriate authority if all four of the following criteria are met: (1) Lawyer A has knowledge or a clear belief concerning the pertinent facts (*i.e.,* he has more than a reasonable belief or mere suspicion); (2) Lawyer A's report will not reveal confidential information protected by Rule 1.6 or information that Lawyer A gained while participating in a bona fide lawyer assistance program; (3) the conduct by Lawyer P constitutes a violation of one or more Rules of Professional Conduct; and (4) the violation raises a substantial question as to Lawyer P's honesty, trustworthiness or fitness as a lawyer.

13. If all four of those criteria are met, Lawyer A may also report such misconduct to the affected clients of Lawyer P – but before informing the clients, Lawyer A should carefully weigh both dangers to Lawyer P's attorney-client relationships if the affected

clients are informed against the countervailing dangers to the clients if they are not informed.

14. Even if Lawyer A is not satisfied that all four criteria have been met, Lawyer A may nevertheless report a good faith belief or suspicion of Lawyer P's alleged misconduct to an appropriate authority, provided that the report of the suspected misconduct does not require the disclosure of confidential information or information that Lawyer A gained while participating in a bona fide lawyer assistance program. But Lawyer A may not inform Lawyer P's clients about mere suspicions of Lawyer P's misconduct.

(17-10)

Compilation of Codes, Rules and Regulations of the State of New York
Title 22. Judiciary
Subtitle B. Courts.
Chapter IV. Supreme Court
Subchapter E. All Departments
Part 1215. Written Letter of Engagement (Refs & Annos)

22 NYCRR 1215.1

Section 1215.1. Requirements

Currentness

(a) Effective March 4, 2002, an attorney who undertakes to represent a client and enters into an arrangement for, charges or collects any fee from a client shall provide to the client a written letter of engagement before commencing the representation, or within a reasonable time thereafter:

(1) if otherwise impractible; or

(2) if the scope of services to be provided cannot be determined at the time of the commencement of representation.

For purposes of this rule, where an entity (such as an insurance carrier) engages an attorney to represent a third party, the term *client* shall mean the entity that engages the attorney. Where there is a significant change in the scope of services or the fee to be charged, an updated letter of engagement shall be provided to the client.

(b) The letter of engagement shall address the following matters:

(1) explanation of the scope of the legal services to be provided;

(2) explanation of attorney's fees to be charged, expenses and billing practices; and

(3) where applicable, shall provide that the client may have a right to arbitrate fee disputes under Part 137 of this Title.

(c) Instead of providing the client with a written letter of engagement, an attorney may comply with the provisions of subdivision (a) of this section by entering into a signed written retainer agreement with the client, before or within a reasonable time after commencing the representation, provided that the agreement addresses the matters set forth in subdivision (b) of this section.

Credits
Sec. filed Jan. 22, 2002; amd. filed May 6, 2002 eff. April 3, 2002. Amended (a), (b)(3).

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 1215.1, 22 NY ADC 1215.1

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Compilation of Codes, Rules and Regulations of the State of New York
Title 22. Judiciary
Subtitle B. Courts.
Chapter IV. Supreme Court
Subchapter E. All Departments
Part 1215. Written Letter of Engagement (Refs & Annos)

22 NYCRR 1215.2

Section 1215.2. Exceptions

Currentness

This section shall not apply to:

(a) representation of a client where the fee to be charged is expected to be less than $3,000;

(b) representation where the attorney's services are of the same general kind as previously rendered to and paid for by the client;

(c) representation in domestic relations matters subject to Part 1400 of this Title; or

(d) representation where the attorney is admitted to practice in another jurisdiction and maintains no office in the State of New York, or where no material portion of the services are to be rendered in New York.

Credits
Sec. filed Jan. 22, 2002; amd. filed May 6, 2002 eff. April 3, 2002. Added (d).

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 1215.2, 22 NY ADC 1215.2

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Compilation of Codes, Rules and Regulations of the State of New York
Title 22. Judiciary
Subtitle A. Judicial Administration.
Chapter I. Standards and Administrative Policies
Subchapter C. Rules of the Chief Administrator of the Courts
Part 137. Fee Dispute Resolution Program (Refs & Annos)

22 NYCRR 137.0

Section 137.0. Scope of program

Currentness

This Part establishes the New York State Fee Dispute Resolution Program, which provides for the informal and expeditious resolution of fee disputes between attorneys and clients through arbitration and mediation. In accordance with the procedures for arbitration, arbitrators shall determine the reasonableness of fees for professional services, including costs, taking into account all relevant facts and circumstances. Mediation of fee disputes, where available, is strongly encouraged.

Credits

Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.0, 22 NY ADC 137.0

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Compilation of Codes, Rules and Regulations of the State of New York
Title 22. Judiciary
Subtitle A. Judicial Administration.
Chapter I. Standards and Administrative Policies
Subchapter C. Rules of the Chief Administrator of the Courts
Part 137. Fee Dispute Resolution Program (Refs & Annos)

22 NYCRR 137.1

Section 137.1. Application

Currentness

(a) This Part shall apply where representation has commenced on or after January 1, 2002, to all attorneys admitted to the bar of the State of New York who undertake to represent a client in any civil matter.

(b) This Part shall not apply to any of the following:

(1) representation in criminal matters;

(2) amounts in dispute involving a sum of less than $1,000 or more than $50,000, except that an arbitral body may hear disputes involving other amounts if the parties have consented;

(3) claims involving substantial legal questions, including professional malpractice or misconduct;

(4) claims against an attorney for damages or affirmative relief other than adjustment of the fee;

(5) disputes where the fee to be paid by the client has been determined pursuant to statute or rule and allowed as of right by a court; or where the fee has been determined pursuant to a court order;

(6) disputes where no attorney's services have been rendered for more than two years;

(7) disputes where the attorney is admitted to practice in another jurisdiction and maintains no office in the State of New York, or where no material portion of the services was rendered in New York; and

(8) disputes where the request for arbitration is made by a person who is not the client of the attorney or the legal representative of the client.

Credits

Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.1, 22 NY ADC 137.1

End of Document

Compilation of Codes, Rules and Regulations of the State of New York
Title 22. Judiciary
Subtitle A. Judicial Administration.
Chapter I. Standards and Administrative Policies
Subchapter C. Rules of the Chief Administrator of the Courts
Part 137. Fee Dispute Resolution Program (Refs & Annos)

22 NYCRR 137.2

Section 137.2. General

Currentness

(a) In the event of a fee dispute between attorney and client, whether or not the attorney already has received some or all of the fee in dispute, the client may seek to resolve the dispute by arbitration under this Part. Arbitration under this Part shall be mandatory for an attorney if requested by a client, and the arbitration award shall be final and binding unless *de novo* review is sought as provided in section 137.8 of this Part.

(b) The client may consent in advance to submit fee disputes to arbitration under this Part. Such consent shall be stated in a retainer agreement or other writing that specifies that the client has read the official written instructions and procedures for this Part, and that the client agrees to resolve fee disputes under this Part.

(c) The attorney and client may consent in advance to arbitration pursuant to this Part that is final and binding upon the parties and not subject to *de novo* review. Such consent shall be in writing in a form prescribed by the board of governors.

(d) The attorney and client may consent in advance to submit fee disputes for final and binding arbitration to an arbitral forum other than an arbitral body created by this Part. Such consent shall be in writing in a form prescribed by the board of governors. Arbitration in that arbitral forum shall be governed by the rules and procedures of that forum and shall not be subject to this Part.

Credits
Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.2, 22 NY ADC 137.2

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Compilation of Codes, Rules and Regulations of the State of New York
Title 22. Judiciary
Subtitle A. Judicial Administration.
Chapter I. Standards and Administrative Policies
Subchapter C. Rules of the Chief Administrator of the Courts
Part 137. Fee Dispute Resolution Program (Refs & Annos)

22 NYCRR 137.3

Section 137.3. Board of governors

Currentness

(a) There shall be a Board of Governors of the New York State Fee Dispute Resolution Program.

(b) The board of governors shall consist of 18 members, to be designated from the following: 12 members of the bar of the State of New York and six members of the public who are not lawyers. Members of the bar may include judges and justices of the New York State Unified Court System.

(1) The members from the bar shall be appointed as follows: four by the Chief Judge from the membership of statewide bar associations and two each by the Presiding Justices of the Appellate Divisions.

(2) The public members shall be appointed as follows: two by the Chief Judge and one each by the Presiding Justices of the Appellate Divisions.

Appointing officials shall give consideration to appointees who have some background in alternative dispute resolution.

(c) The Chief Judge shall designate the chairperson.

(d) Board members shall serve for terms of three years and shall be eligible for reappointment. The initial terms of service shall be designated by the Chief Judge such that six members serve one-year terms, six members serve two-year terms, and six members serve three-year terms. A person appointed to fill a vacancy occurring other than by expiration of a term of office shall be appointed for the unexpired term of the member he or she succeeds.

(e) A majority of current members of the board of governors shall constitute a quorum.

(f) Members of the board of governors shall serve without compensation but shall be reimbursed for their reasonable, actual and direct expenses incurred in furtherance of their official duties.

(g) The board of governors, with the approval of the four Presiding Justices of the Appellate Divisions, shall adopt such guidelines and standards as may be necessary and appropriate for the operation of programs under this Part, including, but not

limited to: accrediting arbitral bodies to provide fee dispute resolution services under this Part; prescribing standards regarding the training and qualifications of arbitrators; monitoring the operation and performance of arbitration programs to insure their conformance with the guidelines and standards established by this Part and by the board of governors; and submission by arbitral bodies of annual reports in writing to the board of governors.

(h) The board of governors shall submit to the Administrative Board of the Courts an annual report in such form as the Administrative Board shall require.

Credits

Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002; Amd. by Court Notices in NY State Register, Volume XXXI, Issue 23, June 10, 2009; amd. through Court Notices in the April 27, 2016 Register.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.3, 22 NY ADC 137.3

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Compilation of Codes, Rules and Regulations of the State of New York
Title 22. Judiciary
Subtitle A. Judicial Administration.
Chapter I. Standards and Administrative Policies
Subchapter C. Rules of the Chief Administrator of the Courts
Part 137. Fee Dispute Resolution Program (Refs & Annos)

22 NYCRR 137.4

Section 137.4. Arbitral bodies

Currentness

(a) A fee dispute resolution program recommended by the board of governors, and approved by the Presiding Justice of the Appellate Division in the judicial department where the program is established, shall be established and administered in each county or in a combination of counties. Each program shall be established and administered by a local bar association (the arbitral body) to the extent practicable. The New York State Bar Association, the Unified Court System through the District Administrative Judges, or such other entity as the board of governors may recommend also may be designated as an arbitral body in a fee dispute resolution program approved pursuant to this Part.

(b) Each arbitral body shall:

(1) establish written instructions and procedures for administering the program, subject to the approval of the board of governors and consistent with this Part. The procedures shall include a process for selecting and assigning arbitrators to hear and determine the fee disputes covered by this Part. Arbitral bodies are strongly encouraged to include nonlawyer members of the public in any pool of arbitrators that will be used for the designation of multi-member arbitrator panels;

(2) require that arbitrators file a written oath or affirmation to faithfully and fairly arbitrate all disputes that come before them;

(3) be responsible for the daily administration of the arbitration program and maintain all necessary files, records, information and documentation required for purposes of the operation of the program, in accordance with directives and procedures established by the board of governors;

(4) prepare an annual report for the board of governors containing a statistical synopsis of fee dispute resolution activity and such other data as the board shall prescribe; and

(5) designate one or more persons to administer the program and serve as a liaison to the public, the bar, the board of governors and the grievance committees of the Appellate Division.

Credits

Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.4, 22 NY ADC 137.4

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22 NYCRR 137.5

Section 137.5. Venue

Currentness

A fee dispute shall be heard by the arbitral body handling disputes in the county in which the majority of the legal services were performed. For good cause shown, a dispute may be transferred from one arbitral body to another. The board of governors shall resolve any disputes between arbitral bodies over venue.

Credits
Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.5, 22 NY ADC 137.5

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22 NYCRR 137.6

Section 137.6. Arbitration procedure

Currentness

Editorial Note: This rule was updated pursuant to court order dated November 13, 2017.

(a)

(1) Except as set forth in paragraph (2), where the attorney and client cannot agree as to the attorney's fee or where the attorney seeks to commence an action against the client for attorney's fees, the attorney shall forward a written notice to the client, entitled Notice of Client's Right to Arbitrate, by certified mail or by personal service. The notice:

(i) shall be in a form approved by the board of governors;

(ii) shall contain a statement of the client's right to arbitrate;

(iii) shall advise that the client has 30 days from receipt of the notice in which to elect to resolve the dispute under this Part;

(iv) shall be accompanied by the written instructions and procedures for the arbitral body having jurisdiction over the fee dispute, which explain how to commence a fee arbitration proceeding; and

(v) shall be accompanied by a copy of the "request for arbitration" form necessary to commence the arbitration proceeding.

(2) Where the client has consented in advance to submit fee disputes to arbitration as set forth in section 137.2(b) and (c) of this Part, and where the attorney and client cannot agree as to the attorney's fee, the attorney shall forward to the client, by certified mail or by personal service, a copy of the request for arbitration form necessary to commence the arbitration proceeding along with such notice and instructions as shall be required by the rules and guidelines of the board of governors, and the provisions of subdivision (b) of this section shall not apply.

(b) If the attorney forwards to the client by certified mail or personal service a notice of the client's right to arbitrate, and the client does not file a request for arbitration within 30 days after the notice was received or served, the attorney may commence an action in a court of competent jurisdiction to recover the fee and the client no longer shall have the right to request arbitration pursuant to this Part with respect to the fee dispute at issue. An attorney who institutes an action to recover a fee must allege in the complaint:

(1) that the client received notice under this Part of the client's right to pursue arbitration and did not file a timely request for arbitration; or

(2) that the dispute is not otherwise covered by this Part.

(c) In the event the client determines to pursue arbitration on the client's own initiative, the client may directly contact the arbitral body having jurisdiction over the fee dispute. Alternatively, the client may contact the attorney, who shall be under an obligation to refer the client to the arbitral body having jurisdiction over the dispute. The arbitral body then shall forward to the client the appropriate papers set forth in subdivision (a) of this section necessary for commencement of the arbitration.

(d) If the client elects to submit the dispute to arbitration, the client shall file the request for arbitration form with the appropriate arbitral body, and the arbitral body shall mail a copy of the request for arbitration to the named attorney together with an attorney fee response to be completed by the attorney and returned to the arbitral body within 15 days of mailing. The attorney shall include with the attorney fee response a certification that a copy of the response was served upon the client.

(e) Upon receipt of the attorney's response, the arbitral body shall designate the arbitrator or arbitrators who will hear the dispute and shall expeditiously schedule a hearing. The parties must receive at least 15 days notice in writing of the time and place of the hearing and of the identify of the arbitrator or arbitrators.

(f) Either party may request the removal of an arbitrator based upon the arbitrator's personal or professional relationship to a party or counsel. A request for removal must be made to the arbitral body no later than five days prior to the scheduled date of the hearing. The arbitral body shall have the final decision concerning the removal of an arbitrator.

(g) The client may not withdraw from the process after the arbitral body has received the attorney fee response. If the client seeks to withdraw at any time thereafter, the arbitration will proceed as scheduled whether or not the client appears, and a decision will be made on the basis of the evidence presented.

(h) If the attorney without good cause fails to respond to a request for arbitration or otherwise does not participate in the arbitration, the arbitration will proceed as scheduled and a decision will be made on the basis of the evidence presented.

(i) Any party may participate in the arbitration hearing without a personal appearance by submitting to the arbitrator testimony and exhibits by written declaration under penalty of perjury.

Credits

Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002; amd. eff. Jan. 1, 2018.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.6, 22 NY ADC 137.6

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22 NYCRR 137.7

Section 137.7. Arbitration hearing

Currentness

(a) Arbitrators shall have the power to:

(1) take and hear evidence pertaining to the proceeding;

(2) administer oaths and affirmations; and

(3) compel, by subpoena, the attendance of witnesses and the production of books, papers and documents pertaining to the proceeding.

(b) The rules of evidence need not be observed at the hearing.

(c) Either party, at his or her own expense, may be represented by counsel.

(d) The burden shall be on the attorney to prove the reasonableness of the fee by a preponderance of the evidence and to present documentation of the work performed and the billing history. The client may then present his or her account of the services rendered and time expended. Witnesses may be called by the parties. The client shall have the right of final reply.

(e) Any party may provide for a stenographic or other record at the party's expense. Any other party to the arbitration shall be entitled to a copy of said record upon written request and payment of the expense thereof.

(f) The arbitration award shall be issued no later than 30 days after the date of the hearing. Arbitration awards shall be in writing and shall specify the bases for the determination. Except as set forth in section 137.8 of this Part, all arbitration awards shall be final and binding.

(g) Should the arbitrator or arbitral body become aware of evidence of professional misconduct as a result of the fee dispute resolution process, that arbitrator or body shall refer such evidence to the appropriate grievance committee of the Appellate Division for appropriate action.

(h) In any arbitration conducted under this Part, an arbitrator shall have the same immunity that attaches in judicial proceedings.

Credits

Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.7, 22 NY ADC 137.7

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22 NYCRR 137.8

Section 137.8. De novo review

Currentness

(a) A party aggrieved by the arbitration award may commence an action on the merits of the fee dispute in a court of competent jurisdiction within 30 days after the arbitration award has been mailed. If no action is commenced within 30 days of the mailing of the arbitration award, the award shall become final and binding.

(b) Any party who fails to participate in the hearing shall not be entitled to seek *de novo* review absent good cause for such failure to participate.

(c) Arbitrators shall not be called as witnesses nor shall the arbitration award be admitted in evidence at the trial *de novo*.

Credits
Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

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22 NYCRR 137.9

Section 137.9. Filing fees

Currentness

Upon application to the board of governors, and approval by the Presiding Justice of the Appellate Division in the judicial department where the arbitral program is established, an arbitral body may require payment by the parties of a filing fee. The filing fee shall be reasonably related to the cost of providing the service and shall not be in such an amount as to discourage use of the program.

Credits
Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

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N.Y. Comp. Codes R. & Regs. tit. 22, § 137.9, 22 NY ADC 137.9

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22 NYCRR 137.10

Section 137.10. Confidentiality

Currentness

All proceedings and hearings commenced and conducted in accordance with this Part, including all papers in the arbitration case file, shall be confidential, except to the extent necessary to take ancillary legal action with respect to a fee matter.

Credits
Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.10, 22 NY ADC 137.10

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22 NYCRR 137.11

Section 137.11. Failure to participate in arbitration

Currentness

All attorneys are required to participate in the arbitration program established by this Part upon the filing of a request for arbitration by a client in conformance with these rules. An attorney who without good cause fails to participate in the arbitration process shall be referred to the appropriate grievance committee of the Appellate Division for appropriate action.

Credits
Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.11, 22 NY ADC 137.11

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22 NYCRR 137.12

Section 137.12. Mediation

Currentness

(a) Arbitral bodies are strongly encouraged to offer mediation services as part of a mediation program approved by the board of governors. The mediation program shall permit arbitration pursuant to this Part in the event the mediation does not resolve the fee dispute.

(b) All mediation proceedings and all settlement discussions and offers of settlement are confidential and may not be disclosed in any subsequent arbitration.

Credits
Sec. filed: Jan. 12, 2001; March 26, 2001 eff. June 1, 2001; June 14, 2001 eff. Jan. 1, 2002.

Current with amendments included in the New York State Register, Volume XLIII, Issue 9 dated March 3, 2021. Court rules under Title 22 and Executive Orders under Title 9 may be more current.

N.Y. Comp. Codes R. & Regs. tit. 22, § 137.12, 22 NY ADC 137.12

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1. PROSPECTIVE CLIENTS

You are at a cocktail party over the weekend. The host/hostess introduces you to John Kelly, a person whom you don't know, and tells Mr. Kelly that you are a lawyer. Kelly says that he has a legal problem and were hoping you could help. You know your firm would be thrilled if you brought in some business. How do you proceed?

A. Tell him to give you a call in the office on Monday and give him your business card.

B. Pull him aside to a quiet place, and ask him to tell you everything he would want his lawyer to know about his case.

C. Ask for the names of all of the potential parties and other lawyers involved in his legal problem.

D. Have a general conversation about his legal problem, and tell him you'll follow up with him in the office next week.

Authorities: CPLR 4503; RPC 1.6, 1.7, and following.

2. THE INITIAL CLIENT ENGAGEMENT

If you don't get retained and instead had a brief conversation with Kelly where you pass on the matter, is there any scenario where you could represent the bank if the bank called you and wanted to hire you?

Anyway, you end up being retained by Kelly. What's the first thing that you should do when you get retained?

What are the consequences if you don't get a written engagement letter?

Authorities: RPC 1.18, 22 NYCRR § 1215, Part 137.

3. WHERE DOES THE MONEY GO?

Kelly hires you and gives you a $25,000 retainer. Your practice has been to put retainer payments into your firm's escrow account. In discussing the matter with some fellow attorneys from outside of your firm, one attorney expressed the opinion that a retainer payment should not be put into an escrow account and instead should be deposited into a firm's operating account. The other attorney said that the retainer payment belongs to the client and must be put into an escrow account.

Which is it?

Authorities: R. 1.15(a), NYSBA Ethics Opinion 816:

4. REPORTING OBLIGATIONS

You are at a party on a weekend that your adversary, the bank's lawyer, is also attending. You don't know each other outside of work. You see her, among many others at the party, using recreational drugs several times during the course of the evening. Do you report her to the disciplinary committee?

A. Yes.

B. No.

C. It depends.

Aouthorities: NYSBA Ethics Opinion 854, RPC Rule 1.6, 8.3.

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The Evolution of Sanctions Under Rule 3002.1(i)

Federal Rule of Bankruptcy Procedure 3002.1 was adopted in December, 2011, to address "a growing problem that had arisen in Chapter 13 cases throughout the country: debtors who had successfully completed their Chapter 13 plans, and paid all of their mortgage arrears and post-petition installments payments, would find themselves in renewed foreclosure proceedings due to undisclosed and unpaid post-petition charges and fees."[1] In various ways, the Rule requires holders of claims secured by a Chapter 13 debtor's principal residence to file notices related to incurred post-petition fees, expenses, and charges. *See generally* Rule 3002.1. Subsection (i), entitled "Failure to notify," details the consequences of ignoring the Rule's mandates. It provides:

> If the holder of a claim fails to provide any information as required by subdivision (b), (c), or (g) of this rule, the court may, after notice and hearing, take either or both of the following actions:
>
> (1) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or
>
> (2) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure.

Since its enactment, many bankruptcy courts have considered and defined the contours of 3002.1(i), giving entities subject to 3002.1 some idea of what to expect. This article highlights some relevant opinions and provides a cautionary tale as to willful noncompliance with Rule 3002.1's directives.

A. The Rule regards a failure to provide notice, not the submission of incorrect information.

By its terms, Rule 3002.1 concerns itself with providing notice to Chapter 13 debtors. *See* Rule 3002.1(a) ("the notice requirements of this rule … ."); Rule 3002.1(b) ("The holder of the claim shall file and serve … a notice of any change in the payment amount … ."); Rule 3002.1(c) ("The notice shall be served … ."); Rule 3002.1(d) ("A notice filed and served under subdivision (b) or (c) shall be prepared as prescribed by the appropriate Official Form … ."). Consequently, Rule 3002.1's penalty provision is only invoked when notice is not given as required by the Rule.[2]

In *Trevino*,[3] the debtors asked the bankruptcy court to use Rule 3002.1 to declare certain pre-petition tax payments not owed and unenforceable.[4] The debtors based their request upon the alleged inaccuracy of notices provided by defendants U.S. Bank Trust, N.A., Caliber Home Loans, Inc, and HSBC Mortgage Services, Inc. Judge Marvin Isgur denied the debtors' request and noted that the debtors did not allege that any party failed to comply with Rule 3002.1. Per the court, the debtors' request was problematic "[b]ecause Rule 3002.1(i) provides relief in situations involving a lack of notice, rather than incorrect notice, … ."[5]

The relief sought must fit the Rule.

The bankruptcy court in *Tollios*,[6] determined that JP Morgan Chase ("Chase") violated Rule 3002.1 by failing to file a required notice indicating an increase in the debtors' mortgage payment due to an escrow increase. However, the court decided that the sanctions the debtors sought for that violation were inappropriate. The debtors sought "as a sanction a declaration that they need never repay Chase for the property taxes Chase paid on their behalf and that they will never have to pay taxes on the property in the future for the entire loan period."[7] The debtors also sought attorneys' fees and punitive damages.[8]

In light of the debtors' sweeping request for relief, the bankruptcy court analyzed the terms of Section 3002.1(i) and determined that the "debtors never attempt[ed] to fit the relief sought regarding their tax liability into the potential remedies available under

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subsection (i)."[9] Rule 3002.1(i) provides two avenues of relief for violations of Rule 3002.1: (1) preclusion of evidence related to the omitted (not properly noticed) information, or (2) an award of "other appropriate relief, including reasonable expenses and attorney's fees caused by the failure." The debtors in *Tollios* were entitled to neither. In making that determination, the court took into account (1) that Chase had taken no action related to the debtors' failure to pay the increased escrow amount, (2) that the debtors knew that property tax payments were required, and that Chase was paying them on their behalf, and (3) that the debtors had not established why elimination of their ongoing property tax responsibilities would constitute "other appropriate relief" for Chase's violation.[10] In doing so, the court in *Tollios* placed the burden on the debtors to request relief specifically allowed by Rule 3002.1(i), and to provide support for the requested relief.[11]

B. It is unclear whether Rule 3002.1(i) applies to untimely notices.

The bankruptcy court in *Salazar*,[12] held that a late Rule 3002.1(c) notice is subject to disallowance irrespective of Rule 3002.1(i). In that case, a claim-holder filed an untimely Rule 3002.1(c) notice related to post-petition attorney's fees and expenses. The debtor objected to the notice as untimely since it was not served within 180 days after the fees and expenses were incurred. The debtor asked the court to disallow the claim-holder's 3002.1(c) notice, and the court acquiesced. The court characterized the issue in the case as deciding "the consequences of the violation"—the untimely filing.[13] After engaging in some detailed statutory construction, the court determined that Rule 3002.1(i)(1), which excuses a failure to provide "information" pursuant to Rules 3002.1(b), (c), and (g) if harmless or substantially justified, did not apply to save the untimely filing because Rule 3002.1(c) required a "notice" to be filed—not "information" as referenced in Rule 3002.1(i).[14] In accordance, the court adopted the conclusion that the consequence of a claim-holder's failure to file a Rule 3002.1(c) notice is waiver of the post-petition fees or other charges made the subject of the untimely notice.[15] The Court reasoned "If subparagraph (i) does not apply to a claimant's failure to timely file notice, those postpetition fees and expenses set forth in the notice would be uncollectable as against the debtor because they were noticed in violation of the rule, and there is no rule that provides for curing the failure."

In the context of Rule 3002.1(g), the bankruptcy court in *Kreidler*,[16] applied subsection (i) to an untimely response to a notice of final cure and declined to award attorney's fees as a sanction for the claim-holder's tardiness. The court reasoned that Rule 3002.1(i)'s "limitations" did not allow sanctions where a response to the notice was actually filed, even if late. The court also noted that the debtor was not prejudiced by the tardiness of the submission.[17]

C. "Other appropriate relief" can be significant.

Rule 3002.1(i)(2) empowers a bankruptcy court considering a violation of Rule 3002.1(b), (c), or (g), to "award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure." Of that language, the phrase "other appropriate relief" jumps off the page as an obvious attempt by Congress to allow bankruptcy courts the latitude and discretion to fashion appropriate relief for a Rule 3002.1 violation.

The bankruptcy court in *Gravel*,[18] took Congress's invitation and issued an award which included $375,000 in monetary sanctions. In that case, creditor PHH Mortgage Corporation ("PHH") sat squarely in the court's crosshairs for failing to comply with Rule 3002.1(c) in three separate bankruptcy cases pending before the court. According to the bankruptcy court's findings of fact, PHH repeatedly failed to comply with its duties under Rule 3002.1(c) and ignored court orders. Moreover, the court explained that PHH previously violated Rule 3002.1(c) in another published decision and was therefore on notice of the likelihood of sanctions for future transgressions.[19]

The court in *Gravel* explained that, at the time its opinion was authored, no court had "imposed sanctions under Rule 3002.1(i) or explained how sanctions arising under that rule should be computed." In accordance, and working on a somewhat blank slate, the court developed a list of "salient factors" to guide its analysis: "whether PHH had notice of the need to comply with Rule 3002.1(c); (2) whether this is the first time PHH failed to fulfill its duties under Rule 3002.1(c) and/or has previously been sanctioned for similar misconduct; and (3) whether PHH was given an opportunity to rectify processes leading to and/or causing the defalcations, and if so, whether it fulfilled its commitment to do so."[20] The court determined that it was not the first time PHH failed to fulfill its duties under Rule 3002.1 and answered all other questions in the affirmative. The large sanctions award followed.

It is apparent that the court in *Gravel* was concerned with what it characterized as repeated violations by PHH. Moreover, the court had an extensive record of its own dealings with PHH, which clearly impacted the ultimate award. That fact, in addition to the court's finding that PHH had failed to comply with other court orders beyond its Rule 3002.1(c) violations, made the

Gravel decision unique. Even so, other similarly situated creditors should take note of the size of the award in the *Gravel* case and truly consider the importance of being vigilant with regard to compliance with Rule 3002.1. ◉

Footnotes

[1] *See In re Gravel*, 556 B.R. 561, 568 (Bankr. D. Vt. 2016); *In re Fuentes*, 509 B.R. 832, 835 (Bankr. S.D. Tex. 2014) ("The purpose of Rule 3002.1 is to aid in the implementation of § 1322(b)(5)'s requirement that a debtor be allowed to cure a default and maintain payments of a home mortgage over the life of a chapter 13 plan.").

[2] *See In re Trevino*, 535 B.R. 110 (Bankr. S.D. Tex. 2015).

[3] Id.

[4] *id*. at 131.

[5] *id*. *See also In re Gutierrez*, 2012 WL 5355964, at *4 (Bankr. D.N.M. Oct. 30, 2012) ("Rule 3002.1(i) provides for sanctions *for a creditor's failure to provide information* as required by subsections (b), (c), or (g) of the Rule." (emphasis added)); *In re Bodrick*, 498 B.R. 793, 800 (Bankr. N.D. Ohio 2013) ("The only ramifications in Rule 3002.1 are for the creditor's failure to comply.").

[6] 491 B.R. 886, 891-92 (Bankr. N.D. Ill. 2013)

[7] *id*. at 891.

[8] *id*.

[9] *id*.

[10] *id*. at 892-93.

[11] *See also In re Howard*, 2016 WL 8222181, at *7 - *8 (Bankr. N.D. Ca. June 1, 2016) (declining a debtor's request that her mortgage be deemed post-petition current pursuant to Rule 3002.1(i)(2) as a result of a Rule 3002.1 violation because a different subsection of 3002.1 should be used for such a request and would have "a better chance of standing up to judicial scrutiny").

[12] 2016 WL 6068819 (Bankr. S.D. Tex. Oct. 14, 2016)

[13] *id*. at *1.

[14] *id*. at *1 - *2.

[15] *id*. at *3

[16] 494 B.R. 201, 204-05 (Bankr. M.D. Pa. 2013)

[17] *id*. at 205.

[18] 556 B.R. 561 (Bankr. D. Vt. 2016)

[19] *In re Owens*, 2014 WL 184781, at *4 (Bankr. W.D.N.C. Jan. 15, 2014) ("Since this is a matter of first impression, the Court will not assess costs or fines pursuant to Rule 3002.1(i)(2). … However, the court may consider awarding relief as against PHH under Rule 3002.1(i) should it come up in the future.")

[20] *See Gravel* at 571

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NEW YORK
---------- X
In re:

Thomas Haemmerle, Case No.: 06-71530-ast
Chapter 7

Debtor.
----------X

DECISION AND ORDER GRANTING IN PART DEBTOR'S MOTION TO HOLD WELLS FARGO BANK, N.A. IN CONTEMPT FOR VIOLATION OF DEBTOR'S DISCHARGE INJUNCTION

Pending before the Court is the motion of debtor, Thomas Haemmerle, ("Debtor"), seeking to hold Wells Fargo Bank, N.A. ("Wells Fargo") in civil contempt for willfully and repeatedly violating his discharge injunction (the "Motion"). Debtor seeks sanctions, actual and punitive damages, emotional distress damages and attorney's fees. After review of the parties' stipulated facts, exhibits and extensive briefing, and for the reasons set forth herein, the Motion is granted in part.

JURISDICTION

This Court has jurisdiction over this core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A), (I) and (O), and 1334(b), and the Standing Orders of Reference in effect in the Eastern District of New York dated August 28, 1986, and as amended on December 5, 2012, but made effective *nunc pro tunc* as of June 23, 2011.

FINDINGS OF FACT[1] AND CONCLUSIONS OF LAW

This decision constitutes the Court's findings of fact and conclusions of law in accordance with Rule 7052 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules").

[1] The factual background and procedural history are derived from the pleadings, exhibits submitted by the parties as well as the *Stipulation of Undisputed Facts* filed on July 8, 2014 at docket item 28 ("Undisputed Facts")

BACKGROUND AND PROCEDURAL HISTORY

Factual Background

i. Debtor's Bankruptcy and Discharge

On June 30, 2006, Debtor filed a voluntary petition for relief under Chapter 7 of the Bankruptcy Code[2]. [dkt item 1] Debtor's case was denominated as a no asset case and creditors were instructed to not file proofs of claim[3]. Wells Fargo was neither scheduled as a creditor nor listed on Debtor's creditor matrix filed under Rule 1007-1 of the Local Bankruptcy Rules for the Eastern District of New York. [dkt item 1] Thus, Wells Fargo did not receive notice of the commencement of Debtor's bankruptcy case.

On August 14, 2006, Debtor was examined at a § 341 meeting. Undisputed Facts, ¶ 12. The § 341 meeting was closed and the Trustee filed a Report of No Distribution. *Id*., ¶ 14.

On October 16, 2016, Debtor received his discharge (the "Discharge Order"). *Id*., ¶¶ 15, 16; [dkt item 11]. On October 18, 2006, the Clerk of the Court mailed notice of the Discharge Order to the creditors disclosed by Debtor and to all other parties-in-interest. [dkt item 12] Wells Fargo did not receive notice of the Discharge Order. Undisputed Facts, ¶¶ 10, 17.

ii. Debtor's Pre-Petition Mortgage Loan and Subsequent Divorce Proceedings

On April 15, 2005, Debtor obtained a loan in the principal amount of $337,000 from World Savings Bank, FSB ("WSB") (the "Loan"). Undisputed Facts, ¶¶ 1, 3. Debtor executed a note (the "Note") in connection with the Loan and contemporaneously therewith Debtor and his then-wife, Josette Infozino ("Infozino"), executed a mortgage to secure the Note (the "Mortgage"). The Note and Mortgage were executed in connection with the refinance of a lien

[2] Unless otherwise indicated, all statutory references herein are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532.
[3] "Rule 2002(e) allows the clerk to issue what has become known as the 'no asset' notice. In a chapter 7 case when there appear to be no distributable assets, the notice of the meeting of creditors may contain a statement to that effect. Creditors are requested not to file proofs of claim and are informed that, should assets later become available, notice of such assets and notice of the bar date for filing proofs of claim will be mailed." 8 COLLIER ON BANKRUPTCY P. 2002.06 (Alan N. Resnick & Henry J. Sommer eds., 16th ed.); *see* FED. R. BANKR. P. 2002(e).

against Debtor's home located at 650 Avenue, Massapequa, New York (the "Real Property"). Undisputed Facts, ¶ 2. According to Wells Fargo and Debtor, Infonzino "didn't sign the note." *See* Exhibit D to Undisputed Facts, page 18, line 2.

WSB later changed its name to Wachovia Bank. Undisputed Facts, ¶ 3. Through a series of mergers, Wachovia Bank merged into Wells Fargo. *Id.*

Pursuant to a separation agreement between Debtor and Infozino dated November 18, 2005 (the "Separation Agreement"), Debtor deeded his interest in the Real Property to Infozino, but neither sought permission from nor notified Wells Fargo of the transfer. Undisputed Facts, ¶¶ 6, 7. Infozino did not assume the Loan, nor did Wells Fargo relieve Debtor from his obligation to repay the Loan. *Id*., ¶ 8. However, Debtor believed, based on discussions with his matrimonial lawyer, that the Separation Agreement terminated his interest in the Real Property and relieved him of his obligation to pay the Loan. *Id*., ¶ 11.

iii. Collection Activities by Wells Fargo

Beginning sometime in 2011, after the Loan went into default, Debtor began receiving telephone calls from Wells Fargo regarding the Loan; no exact date has been provided to the Court. Undisputed Facts, ¶¶ 18, 19. On April 24, 2013, Debtor's counsel attempted to contact Wells Fargo's CEO by telephone, and left a message at the customer service center regarding Debtor's bankruptcy and discharge. Undisputed Facts, ¶¶ 24, 25.[4] That same day, Debtor's counsel sent Wells Fargo a letter outlining its collection efforts during the two year period of 2011 through 2013, and advising Wells Fargo of Debtor's discharge (the "April 24 Letter"); however, Debtor's counsel did not attach a copy of the Discharge Order.[5] Undisputed Facts, ¶

[4] Debtor does not explain why it took him well over a year to advise Wells Fargo of his bankruptcy discharge.
[5] *See* Exhibit B to Undisputed Facts (Debtor's Counsel's letter dated April 24, 2013 addressed to John G. Stumpf, CEO of Wells Fargo in San Francisco and Wells Fargo's P.O. Box and postal address in Des Moines, Iowa).

26.

On April 29, 2013, Wells Fargo sent Debtor a letter seeking to collect the Loan. Undisputed Facts, ¶ 27.

On May 1, 2013, Wells Fargo telephoned Debtor directly to discuss the April 24 Letter. *Id*., ¶ 28. During the conversation, a representative from the Office of Executive Complaints confirmed Wells Fargo's receipt of the April 24 Letter. Debtor explained to the representative that he had filed a Chapter 7 bankruptcy, received a discharge, and that his ex-wife was supposed to pay the Loan as part of their Separation Agreement; Debtor also requested Wells Fargo contact his bankruptcy counsel. *Id.* The Wells Fargo representative explained that "as it stands right now you're the only name on the loan and you're still responsible for the loan," and that Wells Fargo would research the issue and let Debtor know of their conclusions. *Id*., ¶¶ 28, 29.

On May 14, 2013, Wells Fargo ignored Debtor's request to contact his attorney, and again telephoned Debtor directly and stated that if "your debt has been discharged in bankruptcy, Wells Fargo Home Mortgage is only exercising this right against your property and is not attempting to hold you personally liable on the note." *id*., ¶¶ 30, 31, but also stated that "as long as your name appears on the loan … the phone calls and collection activity continue…." *Id*., ¶ 35.

On May 17, 2013, Wells Fargo directly sent Debtor a letter (the "May 17 Letter") which acknowledged that "[o]nce Chapter 7 Bankruptcy is filed and discharged, creditors cannot attempt to collect the debt," *id.* ¶ 37, but also stated that "as you were the only person who signed the Note, [Wells Fargo] holds only you financially responsible for repayment of the loan." *See* May 17 Letter, Exhibit F to Undisputed Facts. The May 17 Letter went on to state: "[a]s [Wells Fargo] was not notified of the bankruptcy a review of this file was conducted. Upon completion

of our review it was determined that [Wells Fargo] was not included in the bankruptcy; therefore; the bankruptcy does not release you from your obligation to [Wells Fargo]." Undisputed Facts, ¶ 38.

On June 7, 2013, Debtor's counsel wrote a letter (the "June 7 Letter") to the Druckman Law Group, counsel for Wells Fargo at the time, advising them that their attempt to collect the Loan was a violation of the Discharge Order. *Id*., ¶ 40. While the June 7 Letter contained Debtor's name and bankruptcy case number, it did not indicate in which bankruptcy court Debtor's Chapter 7 bankruptcy case was filed, nor (once again) did Debtor's counsel provide a copy of the Discharge Order.

On November 1, 2013, Wells Fargo sent Debtor's counsel a letter acknowledging the April 24 Letter, advising that the matter was being reviewed, and that the results of its inquiry would be completed on or before November 25, 2013. *Id*., ¶ 45.

To that point, from May 1, 2013 through November 5, 2013, Wells Fargo, either *via* a person or through its automated collection system, initiated approximately 137 calls to Debtor, each one related to the Loan. *Id*. ¶¶ 43, 44.

On November 26, 2013, Wells Fargo sent Debtor another letter, reiterating its position that because Debtor failed to schedule the Loan, "…the bankruptcy [did] not release [him] from [his] obligation to the debt. As such; [Wells Fargo] is not in violation of the discharge order and collection attempts will continue per the terms of the Note." *Id*., ¶ 46; quotation in Exhibit K to Undisputed Facts.

Debtor's Motion to Reopen the Bankruptcy Case

On December 10, 2013, Debtor filed his Motion. [dkt item 13]

On March 24, 2014, the Court entered an order reopening Debtor's bankruptcy case. [dkt

item 18]

On April 15, 2014, Wells Fargo filed a *Memorandum of Law in Support of Wells Fargo Bank, N.A.'s Opposition to Debtor's Motion for Contempt* (the "Opposition"). [dkt item 22]

On April 22, 2014, Debtor filed its *Reply to Wells Fargo's Memorandum of Law in Opposition to Debtor's Motion for Contempt*. [dkt item 24]

On July 28, 2014, Debtor submitted a *Memorandum of Law in Support of Debtor's Motion to Hold Wells Fargo in Contempt* (the "Debtor's Memo of Law"). [dkt item 33] Also on July 28, 2014, Wells Fargo filed a *Supplemental Memorandum of Law in Further Support of Wells Fargo Bank, N.A.'s Opposition to Debtor's Motion for Contempt* (the "Wells Fargo Supplemental Memo of Law"). [dkt item 34]

On August 11, 2014, Debtor filed a *Memorandum of Law in Reply to Wells Fargo's Opposition to Debtor's Motion for Contempt* (the "Debtor's Supplemental Memo of Law"). [dkt item 35] Also on August 11, 2014, Wells Fargo filed a *Reply Memorandum in Further Support of Wells Fargo Bank, N.A's Opposition to Debtor's Motion for Contempt* (the "Wells Fargo Second Supplemental Memo of Law"). [dkt item 36]

On August 11, 2014, this Court took the Motion on submission.

Arguments of the Parties

While the pleadings filed in this proceeding are numerous and voluminous, the arguments of the parties can be summarized as follows. Debtor asserts that: (1) the Loan was discharged in spite of Wells Fargo having not been included in his schedules and not having received notice of this case before it was initially closed; and (2) Wells Fargo violated the Discharge Order by repeatedly seeking to collect on the Loan after it had knowledge of the discharge.

Wells Fargo asserts that: (1) the Loan was not discharged because it had no notice or

knowledge of Debtor's bankruptcy case prior to the case being closed; (2) Debtor has not proved by clear and convincing evidence that Wells Fargo willfully violated the Discharge Order; (3) it did not act in bad faith; (4) and it was entitled to exercise its *in rem* rights in the Real Property regardless of Debtor's discharge.

Debtor does not challenge Wells Fargo's right to exercise its *in rem* rights post-discharge. *See Johnson v. Home State Bank*, 501 U.S. 78, 82-83 (1991) (a secured creditor retains and may seek to enforce its *in rem* rights as against its collateral post-discharge).

Thus, the threshold issues are: (1) whether Debtor's *in personam* liability to Wells Fargo was discharged despite Wells Fargo's lack of notice and knowledge of the bankruptcy case prior to the case being closed; and (2) if the Loan was discharged, whether Wells Fargo violated the discharge injunction.

ANALYSIS

A. *Prevailing law in this district is that a debt is discharged in a no asset chapter 7 despite the lack of notice to a creditor*

Notice and an opportunity to be heard are fundamental aspects of procedural due process. *See DPWN Holdings (USA), Inc. v. United Airlines, Inc. d/b/a United Airlines*, 871 F. Supp. 2d 143, 153 (E.D.N.Y. 2012) (In this chapter 11 case, the court noted that "[b]efore a claim may be discharged in a bankruptcy proceeding, the claimant must therefore be afforded notice and an opportunity to be heard."). When a debtor files a bankruptcy petition, he or she is obligated to, among other things, list all of his or her creditors along with their addresses, and file schedules that delineate all assets and liabilities. *See* 11 U.S.C. § 521 and FED. R. BANKR. P. Rule 1007. This court's Local Rule 1007-3 requires a debtor to also "file a mailing matrix which shall include, in alphabetical order, the name and last known mailing address (including zip codes) for every scheduled creditor." The court clerk's office generates a notice of the filing of the case to

be sent to all creditors listed in debtor's schedules and other parties in interest; this notice specifies the time and place of the § 341 meeting, and the deadlines to file a proof of claim, object to the debtor receiving a discharge and/or object to the dischargeability of a specific debt. In a no asset case, creditors are told to not file a claim, unless later advised to do so. *See* FED. R. BANKR. P. Rule 2002(e) (allowing the clerk of court to provide a notice of commencement of a no dividend chapter 7 case, which notice advises creditors "that it is unnecessary to file claims").

Section 523(a)(3) of the Bankruptcy Code[6] "seeks to protect the rights of an unlisted creditor from having its debts discharged by a debtor without having had notice of the case….". *In re Delafield 246 Corp.*, Case No. 05-13634, Adv. Proc. No. 05-01834 (ALG), 2007 Bankr. LEXIS 2804, at *6 (Bankr. S.D.N.Y. Aug. 14, 2007) (citing *In re Cruz*, 254 B.R. 801, 807 (Bankr. S.D.N.Y. 2000)). However, it is also "well accepted that the failure to give notice to a creditor will be disregarded in a Chapter 7 no asset case and that in such cases failure to schedule a prepetition debt will not preclude the discharge of that debt." *Id*. *See also In re Herzig*, 238 B.R. 5 (E.D.N.Y. 1998).

The Second Circuit Court of Appeals has not yet ruled on whether an unscheduled debt is discharged in a no asset chapter 7 case. However, courts in the Eastern and Southern Districts of New York have adopted the "mechanical approach" utilized by the Third, Sixth, Ninth and Tenth Circuit Courts of Appeals, which have held that the "failure to schedule a prepetition debt in a

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[6] A discharge …does not discharge an individual debtor from any debt – (3) neither listed nor scheduled …, in time to permit –

> (A) if such debt is not of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim, unless such creditor had notice or actual knowledge of the case in time to permit such timely filing; or
>
> (B) if such debt is of a kind specified in paragraph (2), (4), or (6) of this sub-section, timely filing of a proof of claim and timely request for a determination of dischargeability of such debt under one of such paragraphs, unless such creditor had notice or actual knowledge of the case in time for such timely filing and request…

11 U.S.C. § 523(a)(3)(A)-(B).

Chapter 7 no asset case has no impact on the dischargeability of the debt…." *Delafield*, 2007 Bankr. LEXIS 2804, at *6-7. This "mechanical approach" is based on a plain meaning analysis; that an unscheduled debt is discharged by operation of law because § 523(a)(3) only excludes unscheduled debts from being discharged "if such debt is not of a kind specified in paragraph (2), (4), or (6) of this subsection," and the creditor did not have "notice or actual knowledge of the case in time to permit" timely filing of a claim. *See Cruz*, 254 B.R. at 808, 810. *But see In re Stark*, 717 F.2d 322, 324 (7th Cir. 1983) (adopting an "equitable approach" that examines the circumstances surrounding a debtor's failure to list a certain creditor in their determination to reopen a debtor's case and schedule an omitted creditor). Said otherwise, where there is no deadline set to file a claim in a no asset chapter 7 case, if the debt at issue does not fall within the category of non-dischargeable debts listed in Sections 523(a)(2), (4) or (6), there is no deadline for the creditor to file a timely claim, and, therefore, the creditor could not have notice of actual knowledge of a deadline to file a claim that has not been set. Claims that fall within Sections 523(a)(2), (4) or (6) would be discharged unless a timely adversary proceeding is filed as required by Section 523(c) and Bankruptcy Rule 4007 (60 days after the date first set for the creditors meeting held under § 341(a)) and, therefore, due process requires the creditor have notice or knowledge of the dischargeability deadline before the otherwise non-dischargeable claim could be discharged.

In *Herzig*, the Eastern District of New York district court directly held that an unscheduled debt was discharged in a no asset chapter 7 case. 238 B.R. at 8-9. This Court accepts *Herzig* as binding precedent. Thus, in this no asset Chapter 7 case, because the court did not establish a deadline for creditors to timely file claims, and because Wells Fargo has not

argued that the Loan is a debt specified in § 523(a)(2), (4) or (6), Wells Fargo's unscheduled Loan claim has been discharged by operation of law.[7]

B. ***A discharge injunction violation can arise from attempts to collect a debt which is discharged despite a lack of notice***

Section 524(a)(2) of the Bankruptcy Code, which creates the discharge injunction, is unambiguous and makes no distinction between debts which are discharged following notice to a creditor and those that are discharged despite a lack of notice. Section 524 provides:

> (a) A discharge in a case under this title—
>
> (2) operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a personal liability of the debtor, whether or not discharge of such debt is waived

See 11 U.S.C. § 524(a)(2). *See generally Green v. Welsh*, 956 F.2d 30, 32 (2d Cir. 1992). Wells Fargo has not cited any authority for the proposition that§ 524 does not protect a debtor from any attempts to collect on a personal liability which has been discharged in a no asset case despite a lack of notice to the creditor.

Thus, here, because Debtor's personal liability on the Loan was discharged, any attempt by Wells Fargo to collect on Debtor's discharged personal liability is a violation of § 524(a)(2); what damages may be appropriate, however, can only be determined once Debtor has established by clear and convincing evidence whether and when Wells Fargo knowingly attempted to collect on the discharged personal liability.

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[7] Although the courts in this circuit have not applied an equitable standard for discharge of an unscheduled debt, this Court notes that Debtor was forthcoming about the Real Property during the bankruptcy case. During his § 341 meeting, Debtor informed the trustee about the Real Property and his pre-petition transfer that occurred as a result of his Separation Agreement. Debtor did not hide an interest in the Real Property, and his belief that he was somehow relieved of his obligations to Wells Fargo was clearly mistaken, but apparently held in good faith. Undisputed Facts, ¶ 13.

C. *A party can only be held liable for a knowing violation of the discharge injunction*

The discharge injunction is intended to further one of the primary purposes of the Bankruptcy Code: giving the debtor an opportunity to make a financial fresh start, unburdened by efforts to collect debts she no longer owes. *Green*, 956 F.2d at 33 (citing *In re Jet Florida Systems, Inc.*, 883 F.2d 970, 972 (11th Cir. 1989)); *In re Otten*, Case No. 10-74946, Adv. Proc. No. 12-8045 (AST), 2013 Bankr. LEXIS 1920, at *20 (Bankr. E.D.N.Y. May 3, 2013). S*ee also In re Szenes*, 515 B.R. 1, 6 (Bankr. E.D.N.Y. 2014); *In re Nicholas*, 457 B.R. 202, 224 (Bankr. E.D.N.Y. 2014). Although § 524 does not include an explicit mechanism to enforce this injunction, § 105 of the Bankruptcy Code has been widely accepted as providing statutory authority to enforce the discharge injunction by holding a party who violates the injunction in contempt, and assessing appropriate punishment.[8] *In re Nassako*, 405 B.R. 515 (Bankr. S.D.N.Y. 2009) (citing *In re Thompson*, Case No. 06-32633 (SDG), 2007 Bankr. LEXIS 2830, at *6 (Bankr. N.D.N.Y. Aug. 21, 2007) (quoting § 105)); *Szenes*, 515 B.R. at 6; *Nicholas* 457 B.R. at 225 (enforcement of a debtor's discharge is a core proceeding and "[b]ankruptcy courts retain jurisdiction to enforce and interpret their own orders.") (citations omitted).

A discharge injunction violation may be punished as a civil contempt of court, and requires a two part inquiry: "(1) did the party know of the lawful order of the court, and (2) did the defendant comply with it." *Nicholas* 457 B.R. at 225; *In re McKenzie-Gilyard*, 388 B.R. 474, 481 (Bankr. E.D.N.Y. 2007) (citation omitted)*; In re DiGeronimo*, 354 B.R. 625, 642 (Bankr. E.D.N.Y. 2006) (holding that a violation of the discharge injunction is willful where "the creditor (1) knew that the discharge had issued, and (2) intended the actions which violated the

[8] Because Debtor does not assert that this Court has inherent authority to impose sanctions for a violation of the Discharge Order, this Court will only analyze its authority under § 105 to enforce the discharge injunction of § 524. *See, e.g., In re Campora*, Case No. 14-70330 (AST), 2014 Bankr. LEXIS 4276, at * 24-25 (Bankr. E.D.N.Y. Oct. 6, 2014) (citing, among others, *Int'l United Mine Workers of Am. v. Bagwell*, 512 U.S. 821, 831 (1994), *M.A. Salazar, Inc. v. Inc. Vill. of Atl. Beach*, 499 B.R. 268, 274 (E.D.N.Y. 2013)).

discharge injunction."); *see also* 4 Collier on Bankruptcy P 524.02[2][c] ("A creditor's actions in violation of the discharge injunction are willful if the creditor knows the discharge has been entered and intends the actions which violated the discharge injunction."). Thus, while Debtor's personal liability on the Loan was discharged despite a lack of notice, Wells Fargo could not be held liable for a discharge injunction violation unless and until it knew Debtor had received a discharge. A creditor's knowledge of the discharge injunction may be actual or constructive. *Nassoko*, 405 B.R. at 522.

Further, as contempt is at issue, the burden is on Debtor to prove Wells Fargo knowingly violated the Discharge Order by clear and convincing evidence. *Nicholas*, 457 B.R. at 224-225; *Nassako*, 405 B.R. at 520 (quoting *In re Torres*, 367 B.R. 478, 490 (Bankr. S.D.N.Y. 2007) (internal citations omitted)).

Sanctions for civil contempt may be imposed both to "coerce future compliance" with a court order issued for another party's benefit and to "compensate for any harm that previously resulted" from the noncompliance. *Chief. Exec. Officers Clubs, Inc.* 359 B.R. 527, 534 (Bankr. S.D.N.Y. 20007) (citing *New York State Nat'l Org. for Women v. Terry*, 159 F.3d 86, 93 (2d Cir. 1998). In fashioning an appropriate remedy, courts must consider "the nature of the harm and the probable effect of alternative sanctions." *Id.* at 536 (citing *EEOC v. Local 28, Sheet Metal Workers*, 247 F.3d 333, 336 (2d Cir. 2001)). If a party is held in contempt, various forms of compensatory damages may be awarded; attorneys' fees; litigation costs; travel expenses; other actual losses, such as wages or business income; and possibly emotional distress damages. *See In re American Medical Utilization Management Corp.*, 494 B.R. 626, 636-638 (Bankr. E.D.N.Y. 2013) (awarding costs and fees as a contempt sanction for violation of the automatic stay); *Russell v. Chase Bank USA, NA (In re Russell)*, 378 B.R. 735, 743-744 (Bankr. E.D.N.Y.

2007) (noting that compensatory damages and attorney's fees may be awarded as a contempt sanction for violation of the discharge injunction); *In re Manzaneres*, 345 B.R. 773, 794-95 (Bankr. S.D. Fla. 2006) (awarding damages for lost wages, attorney's fees and emotional distress); *In re Feldmeier*, 335 B.R. 807, 814 (Bankr. D. Or. 2005) (holding imposition of emotional distress damages is appropriate as compensatory damages for a willful violation of the discharge injunction); *In re Reno*, 299 B.R. 823, 829-30 (Bankr. N.D. Tex. 2003) (awarding debtor emotional distress damages because of attorney's willful violation of a court order); *Torres*, 367 B.R. at 490 (internal citations omitted); *but see In re Walters*, 868 F.2d 665, 670 (4th Cir. 1989) (vacating emotional distress damage award because no authority was cited to support emotional distress damages for civil contempt). In addition, punitive damages may be appropriate if there is "some sort of nefarious or otherwise malevolent conduct" that demonstrates a "complete and utter disrespect for the bankruptcy laws." *In re Perviz*, 302 B.R. 357, 369 (Bankr. N.D. Ohio 2003) (holding that a creditor, who willfully violated the discharge injunction, could be held in contempt and ordered to pay $8,000 in punitive damages).

D. ***Wells Fargo knowingly attempted to collect on Debtor's discharged personal liability***

Debtor has shown by clear and convincing evidence that Wells Fargo knew of the Discharge Order and thereafter knowingly violated the discharge injunction by trying to collect on his discharged personal liability. The conduct at issue in this decision is: (i) the 137 phone calls Wells Fargo made to Debtor between May 1, 2013 through November 5, 2013, after Wells Fargo had knowledge of the Discharge Order and; (ii) the May 17, 2013 Letter and the November 26, 2013 Letter which explicitly state that Debtor was personally liable for the Loan; this Court is not called upon to assess damages for the nearly two years of collection activities that preceded the April 24, 2013 Letter. Undisputed Facts, ¶¶ 43, 44.

First, while Wells Fargo does not concede when it knew about Debtor's discharge, it admits knowing of Debtor's bankruptcy filing by May 17, 2013, as it had researched Debtor's bankruptcy and found this case. Undisputed Facts, ¶ 38. Wells Fargo asserts that since Debtor's April 24 Letter did not attach a copy of the Discharge Order, Wells Fargo was not adequately notified of the bankruptcy proceedings and the discharge.[9] This Court disagrees. While Debtor's counsel could have been more specific in his April 24 Letter, he did expressly state that Debtor had been discharged in bankruptcy and provided the case number and name of Debtor. Wells Fargo clearly knew Debtor lived in Nassau County, New York, based on the address it used to send collection letters to Debtor and the address Debtor used in writing to Wells Fargo. Upon receiving the April 24 Letter, Wells Fargo could have suspended its collection efforts for long enough to conduct a simple, on line Pacer search of this court's bankruptcy records and found this case and the Discharge Order; it is simply not credible to argue it took as large and sophisticated a financial institution as Wells Fargo 23 days to find the records of this case. Thus, for the period between May 1 and May 17, 2013, Wells Fargo, at a minimum, had constructive knowledge of the Discharge Order.

Second, Wells Fargo's assertions that it was only seeking to enforce its lien and not collect a personal debt[10] is also not plausible. Wells Fargo explicitly stated it was collecting on a personal debt, and its representative specifically informed Debtor that "as long as your name appears on the loan … the phone calls and collection activity continue…" Undisputed Facts, ¶ 35. In addition, the May 17 Letter informed Debtor that "as long as you were the only person who signed the Note, [Wells Fargo] holds only you financially responsible for repayment of the loan…." *See* Exhibit F to Undisputed Facts. These clear and explicit statements leave no doubt

[9] *See* Opposition, pages 3-5; Wells Fargo Second Supplemental Memo of Law, page 3.
[10] *See* Opposition, pages 5-6; Wells Fargo Supplemental Memo of law, page 5; Wells Fargo Second Supplemental Memo of Law, page 3-4.

that Wells Fargo sought to collect the Loan from Debtor personally, not just assert its *in rem* rights.

Wells Fargo is correct that, as a general matter, technical or unintended violations of the discharge injunction, as well as violations that are quickly remedied, should not be punished as contempt. *Nicholas*, 457 B.R. at 226; *Cruz*, 254 B.R. at 816. Wells Fargo correctly cites *In re Garske*[11] for the proposition that a post-discharge phone call is not a *per se* violation under § 524(a)(2) of the Bankruptcy Code. However, the facts in *Garske* are quite different. The *Garske* debtor agreed to retain a secured debt on a vehicle during her Chapter 7 bankruptcy and the secured creditor, on notice of the bankruptcy case, made between 14 and 36 phone calls regarding that debt once the debtor defaulted on the payments post-bankruptcy.[12] Here, Debtor did not attempt to reaffirm any debt to Wells Fargo and clearly mistakenly, but in good faith, believed that his Separation Agreement made the Loan his ex-wife's responsibility.

This Court also rejects Wells Fargo's assertions that its "informational statements" do not constitute a discharge injunction violation. Although Wells Fargo sent Debtor a letter dated February 24, 2014 informing Debtor of the interest rate change on the Loan pursuant to RESPA requirements, which is technical and informational,[13] the many statements in May 17 Letter and November 26 Letter informing Debtor that (i) he is not released from his personal obligations on the Loan and (ii) collection attempts will continue per the terms of the Note, illustrate that Wells Fargo intended to assert *in personam* rights, in addition to enforcing its *in rem rights*.

Wells Fargo's arguments that any of its communications were "technical", "unintended" and not done in bad faith are also rejected. The explicit statements in the voluminous phone calls

[11] 287 B.R. 537 (9th Cir. 2002).
[12] The *Garske* parties disputed the number of phone calls; debtor argued 36 calls, while the secured creditor argued that it only made 14 calls. *Garske*, 287 B.R. at 539.
[13] Wells Fargo Second Supplemental Memo of Law, page 4-5.

and letters demonstrate a conscious and deliberate effort by Wells Fargo to collect on the Loan even after being informed of Debtor's bankruptcy and the Discharge Order.

In addition, this Court rejects Wells Fargo's argument that Debtor should have informed it of case law which is contrary to the position Wells Fargo took in its May 17 Letter that its debt had not been discharged.[14] Wells Fargo's May 17 Letter does not refer to any cases it relies on. It is a large and sophisticated financial institution, and is represented by sophisticated counsel whose research of Second Circuit case law would have yielded *Herzig*, which is directly on point, as well as the other decisions within this circuit which are contrary to Wells Fargo's legal conclusion.

Finally, after nearly 2 years of unsuccessful collection activities prior to May 1, 2013, Wells Fargo had numerous opportunities throughout the 6 months after learning of Debtor's discharge during within it which it could have ceased collection efforts long enough to seek to reopen this case, and ask this Court if Debtor's liability on the Loan had been discharged.

Thus, Debtor has proven by clear and convincing evidence that Wells Fargo repeatedly violated the Discharge Order. This Court next addresses the appropriate damages to award as a result of these violations.

i. Debtor has no out of pocket expense or lost income or wages

According to the record before the Court, Debtor has not incurred any out of pocket losses, other than attorney's fees (addressed below), and has not suffered a loss of income or wages. Therefore, those types of damages will not be awarded here.

ii. Debtor has incurred and should recover reasonable attorney's fees

Courts have awarded attorneys' fees when a party (1) willfully disobeys a court order,

[14] *See* Wells Fargo Supplemental Memo of law, pages 5-7; Wells Fargo Second Supplemental Memo of Law, pages 6-7.

and (2) is found to have acted in bad faith, vexatiously, wantonly or for oppressive reasons. *Szenes*, 515 B.R. at 7; *Nicholas*, 457 B.R. at 225; *Nassoko*, 405 B.R. at 520; *Dabrowski*, 257 B.R. at 416; *Watkins*, 240 B.R. at 678. An award of attorneys' fees may also be warranted where an offending party not only willfully violated the discharge injunction but also acted in bad faith or in a vexatious or oppressive manner. *Watkins v. Guardian Loan Co. of Massapequa, Inc. (In re Watkins)*, 240 B.R. 668, 678 (Bankr. E.D.N.Y. 1999); *DiGeronimo*, 354 B.R. at 642 (Bankr. E.D.N.Y. 2006); *Russell v. Chase Bank USA, NA (In re Russell)*, 378 B.R. 735, 743-744 (Bankr. E.D.N.Y. 2007). Willfulness requires a showing that the creditor intended the actions that violated the discharge injunction, rather than a specific intent to violate the debtor's discharge. *DiGeronimo*, 354 B.R. at 642. One court has described willfulness as "knowingly going forward with collection activity … knowing or having reason to know that the debtor was in bankruptcy and has received a discharge." *In re Ramos*, Case No. 10-23019 (RDD), 2013 WL 5461859, at *2 (Bankr. S.D.N.Y. Oct. 1, 2013). Relevant here, the "mistaken belief that a debt at issue was not discharged…does not negate a finding that a creditor wilfully violated the discharge injunction." *DiGeronimo*, 354 B.R. at 643. As noted above, Wells Fargo's 137 calls were not technical, unintended, or quickly remedied, but were in fact wanton and oppressive, and thus, warrant an award of reasonable attorneys' fees. *Szenes*, 515 B.R. at 7; *Nicholas*, 457 B.R. at 226; *Dabrowski*, 257 B.R. at 416.

Debtor incurred attorney's fees as a result of Wells Fargo's actions by having the bankruptcy case reopened, filing the Motion, and responding to Wells Fargo's extensive pleadings. This Court will award Debtor reasonable attorneys' fees and costs under the following protocol: (i) Debtor's counsel shall have 21 days from the date of the entry of this Decision and Order to file a statement of fees and costs, supported by time records and/or billing

summaries and/or invoices; and (ii) Wells Fargo shall have 14 days from service of Debtor's counsel's statement of fees and costs to file an objection and/or other response. The Court will then take the issue of attorney's fees and costs on submission.

iii. Debtor is not entitled to emotional distress damages

Debtor asserts a claim for emotional distress damages as a result of Wells Fargo's continued violations of the Discharge Order. *See* Debtor's Memo of Law, pages 14-16. Debtor argues that he told Wells Fargo as early as May 1, 2013 that he had epilepsy and was on medication, that he stated during one of the many calls that "you [Wells Fargo] all are really stressing me out over the last 3 years", and that "[i]t was incumbent on Wells Fargo to insure they did not further increase his emotional distress." *See* Exhibit D, page 2, lines 13-14 to Undisputed Facts; Debtor's Memo of Law, page 15. Debtor asserts that he should be permitted to present testimonial and medical evidence of the emotional distress at a damages hearing. *See* Debtor's Memo of Law, page 15.

In order to sustain a claim for emotional distress damages, a debtor must prove "a close causal connection between the harm and the stay/discharge violation." *In re McCool*, 446 B.R. 819, 824 (Bankr. N.D. Ohio 2010). *See also In re Burkart*, Case No. 08-61077 (DD), 2010 Bankr. LEXIS 385, at *12-18 (Bankr. N.D.N.Y. Feb. 9, 2010). Debtor did not meet this burden. According to the record before the Court, Debtor had a medical condition prior to the repeated discharge injunction violations by Wells Fargo, and there is no evidence in the record that Wells Fargo directly or proximately caused his condition to worsen. Therefore, it would be unnecessary for the Court to conduct a hearing to determine the amount of emotional distress damages to award.

iv. Debtor is entitled to punitive damages

Where a clear violation of the discharge injunction has been found, the court may also impose a punitive civil contempt sanction. *Szenes*, 515 B.R. at 7; *In re Velo Holdings Inc.*, 500 B.R. 693, 700 (Bankr. S.D.N.Y. 2013); *Nicholas*, 457 B.R. at 227; *DiGeronimo*, 354 B.R. at 644. A mere showing that the actions were deliberate is not sufficient for punitive damages; rather, the actions must have been taken with "either malevolent intent or a clear disregard and disrespect of the bankruptcy laws." *Szenes*, 515 B.R. at 7-8; *Nicholas*, 457 B.R. at 227; *Watkins*, 240 B.R. at 680 (finding punitive damages for violation of a discharge injunction also appropriate where there was malicious and egregious behavior).

The purpose of punitive damages is not only to punish the creditor but to also deter that creditor and others from similar conduct in the future. *Szenes*, 515 B.R. at 8; *Nicholas*, 457 B.R. at 227 (citing *Vasbinder v. Scott*, 976 F.2d 118, 121 (2d Cir. 1992)). Courts have found sanctions for civil contempt appropriate "to coerce the defendant into compliance with the court's order, and to compensate the complainant for losses sustained." *Torres*, 367 B.R. at 490.

Wells Fargo's conduct exhibits a clear disregard for the bankruptcy process and the sanctity of Debtor's discharge. *See Szenes*, 515 B.R at 8 (imposing attorney's fees and a $500 punitive sanction for a bank which not only violated the discharge injunction by sending a letter after it received notice of the discharge order but continued to violate the discharge injunction by sending another letter after it received a letter from debtor's counsel notifying it of its violation); *Nicholas*, 457 B.R. at 227 (assessing a $5,000 punitive sanction against a pro se litigant who violated the discharge injunction by making payment demands and pursuing state court litigation on discharged claims).

The cases in this area have not established a formulaic approach to determine how much in punitive sanctions should be assessed; rather, courts are called upon to exercise their discretion to determine what punitive sanction is appropriate and reasonable. *Szenes*, 515 B.R. at 8. The number of phone calls Wells Fargo made and letters it sent were solely within its control, and it has failed to provide any credible explanation of why, after nearly 2 years of unsuccessfully pursuing Debtor for collection, it made 137 phone calls between May 1, 2013 and November 5, 2013 and sent 2 letters. This Court agrees with Judge Scarcella's approach in *Szenes*, and concludes that a proper and reasonable punitive sanction under the facts and circumstances here, in order to deter Wells Fargo from further efforts to collect a discharged debt from this Debtor or from any other debtor, should be assessed at $500 for each knowing discharge violation. Thus, Wells Fargo should be and is sanctioned $500 for each of its 137 knowing discharge injunction violations by telephone, and for each of the May 17 Letter and the November 26 Letter, for a total punitive award of $69,500.00. This sanction should be paid within sixty (60) days.

CONCLUSION

Based upon the foregoing, it is hereby

ORDERED, that Debtor's Motion is granted to the extent set forth herein; and it is further

ORDERED, that Debtor's counsel is entitled to his reasonable attorneys' fees and costs incurred in connection with the Motion, and shall file and serve a fee and cost statement in affidavit form within **twenty-one (21) days** after entry of this order, supported by time records and/or billing summaries and/or invoices; and it is further

ORDERED, that Wells Fargo may submit an objection within **fourteen (14) days** after

service of Debtor's counsel's fee and cost statement, after which the calculation of and the reasonableness of Debtor's attorney's fees and costs will be on submission with the Court; and it is further

ORDERED, that Wells Fargo is also assessed punitive sanctions in the amount of $69,500.00, which it shall pay to Debtor within **sixty (60) days** of entry of this Order; and it is further

ORDERED, that the Clerk of the Court shall serve a copy of this Decision and Order on Debtor, counsel for Debtor, Wells Fargo, all counsel of record for Wells Fargo, the chapter 7 trustee, and the Office of the United States Trustee.

Dated: April 16, 2015
Central Islip, New York

Alan S. Trust
United States Bankruptcy Judge

SHORT FORM ORDER ORIGINAL INDEX NO. 617340/2017

SUPREME COURT - STATE OF NEW YORK
I.A.S. PART 54 - SUFFOLK COUNTY

PRESENT:

Hon. MICHAEL A. GAJDOS JR.
Justice of the Supreme Court

MOTION DATE: 09/24/2018 (001)
MOTION DATE: 01/09/2019 (002)
ADJ. DATE: 04/30/2019
Mot. Seq. #001- MD
Mot. Seq. #002- MotD

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WILMINGTON SAVINGS FUND SOCIETY, FSB, DOING BUSINESS AS CHRISTIANA TRUST, NOT IN ITS INDIVIDUAL CAPACITY AS CERTIFICATE TRUSTEE FOR NNPL TRUST SERIES 2012-1,

Plaintiff,

- against -

EDWARD KLEYNOWSKI; NANCY KLEYNOWSKI A/K/A NANCY B. KLEYNOWSKI; MIDLAND FUNDING LLC; CAPITAL ONE BANK, USA N.A.; "JOHN DOE #1" through "JOHN DOE #10" inclusive the names of the ten last name Defendants being fictitious, real names unknown to the Plaintiff, the parties intended being persons or corporations having an interest in, or tenants or persons in possession of, portions of the mortgaged premises in the Complaint,

Defendants.

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KNUCKLES, KOMOSINSKI & MANFRO, LLP
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Elmsford, NY 10523

LAW OFFICE OF CRAIG D. ROBINS, ESQ.
Attorney for Defendants
Edward Kleynowski and Nancy Kleynowski
35 Pinelawn Road, Suite 218-E
Melville, NY 11747

Upon the following papers: Notice of Motion by Plaintiff, dated August 28, 2018, with supporting papers; Notice of Cross-Motion by Defendants Edward Kleynowski and Nancy Kleynowski, dated December 4, 2018, with supporting papers including the addendum dated December 16, 2018 and the second addendum dated December 17, 2018; Affirmation in Opposition to Cross-Motion by Plaintiff, dated February 14, 2019; Reply Affirmation by Defendants, dated April 25, 2019, with supporting papers; correspondence from the moving parties dated October 24, 2018 through April 25, 2019; and upon due consideration; it is

ORDERED that this motion (001) by the plaintiff for, *inter alia*, an order: (1) pursuant to CPLR 3212 awarding summary judgment in its favor and against the answering defendants Edward Kleynowski and Nancy Kleynowski, striking their answer and dismissing the affirmative defenses and counterclaims set forth therein; (2) fixing the defaults of the non-answering defendants; (3) pursuant to RPAPL § 1321 appointing a referee to (a) compute amounts due under the subject mortgage; and (b) examine and report whether the subject premises should be sold in one parcel or multiple parcels; and (4) amending the caption, is denied; and it is further

ORDERED that this cross-motion (002) by defendants Edward Kleynowski and Nancy Kleynowski for, *inter alia*, an order: (1) awarding partial summary judgment on their counterclaims for breach of the duties of good faith and fair dealing, breach of GBL 349, rescission of the subject note and mortgage and dismissal of the complaint, and for attorney fees, costs and punitive damages; (2) imposing sanctions against plaintiff pursuant to CPLR 3408 and 22 NYCRR 130-1; and alternatively (3) directing specific performance of a loan modification agreement and awarding attorney fees, costs and punitive damages, is granted in part and denied in part; and it is further

ORDERED that so much of the cross-motion that seeks an order pursuant to CPLR 3212 awarding partial summary judgment in favor of the cross-moving defendants and dismissing the complaint, is granted; and it is further

ORDERED that so much of the cross-motion that seeks specific performance of a loan modification agreement, recorded in the Office of the Suffolk County Clerk, at Liber M00022593, page 640, on May, 2015, is granted, and plaintiff is directed to report to the Court regarding same at the conference directed herein; and it is further

ORDERED that so much of the cross-motion that seeks sanctions against plaintiff for failure to negotiate in good faith pursuant to CPLR 3408(f), is granted as set forth in this order; and it is further

ORDERED that so much of the cross-motion that seeks sanctions against plaintiff and plaintiff's counsel pursuant to 22 NYCRR 130-1.1, is granted to the extent that a hearing shall be held to determine the amount of such sanctions; and it is further

ORDERED that so much of the cross-motion that seeks an award of legal fees is granted, the amount of same to be determined following submission to the Court of an affirmation from counsel for defendants on or before the date of the conference directed herein; and it is further

ORDERED that so much of the cross-motion that seeks damages pursuant to GBL 349, is denied; and it is further

ORDERED that so much of the cross-motion that seeks punitive damages for breach of the duty of good faith and fair dealing, is referred to a hearing; and it is further

ORDERED that the attorneys for the parties shall appear for a virtual conference in **Part 54 via Microsoft Teams,** on November 17, 2020. A link with the conference time will be emailed to the parties prior to that date, and it is further

ORDERED that cross-moving defendants are directed to serve a copy of this order with notice of entry upon the plaintiff within thirty (30) days of the date of this order, and to promptly file the affidavit of service with the Clerk of the Court.

This is an action to foreclose a mortgage on real property situate in Suffolk County, New York. On September 30, 2004, defendant-mortgagors Edward Kleynowski and Nancy Kleynowski executed a note in favor of ABN AMRO Mortgage Group, Inc. ("ABN AMRO") in the amount of $307,000. To secure said note, on the same date, defendant-mortgagors gave the lender a mortgage on the property. A loan modification agreement in favor of Citimortgage, Inc. s/b/m to ABN AMRO ("Citimortgage") in the

aggregate amount of $364,427 was executed by defendant-mortgagors on August 21, 2014 and by Citimortgage on September 15, 2014, and was recorded in the Office of the Suffolk County Clerk on May 20, 2015. The recorded loan modification is accompanied by an affidavit under New York Tax Law 255, dated March 19, 2015, from Bethany D. Litle of Citimortgage, Inc., attesting that the instrument recorded is a modification of the above-described mortgage, effective August 1, 2014. By way of a blank endorsement with physical delivery, the note was transferred to plaintiff prior to commencement of this action. Transfer of the note to the plaintiff was memorialized by an assignment of the mortgage, duly recorded in the Office of the Suffolk County Clerk. The plaintiff's complaint alleges that defendant-mortgagors defaulted on the note, mortgage and loan modification agreement by failing to make monthly payments of principal and interest which had come due on October 1, 2014. Plaintiff commenced the instant action by the filing of a lis pendens, summons and complaint on September 7, 2017. Issue was joined by the interposition of defendant- mortgagors' answer dated May 23, 2018. The remaining defendants have not answered the complaint.

By their answer, the defendant-mortgagors generally deny the material allegations set forth in the complaint, and assert fourteen affirmative defenses (erroneously numbered as fifteen) and eleven counterclaims (erroneously numbered as twelve). In its reply, the plaintiff denies all of the allegations contained in the counterclaims, and asserts seven affirmative defenses. Plaintiff now moves for, *inter alia*, summary judgment and an order of reference. Defendant-mortgagors oppose plaintiff's motion with a cross-motion seeking, *inter alia*, partial summary judgment on several of their counterclaims and damages. In sum and substance, the grounds for the cross-motion are primarily that plaintiff wrongfully attempted to rescind the 2014 loan modification agreement after it had been executed, breached the agreement by refusing to accept payments tendered pursuant thereto, wrongfully declared defendant-mortgagors in default, wrongfully commenced the present action, and engaged in a sustained pattern of conflicting/deceptive communications and bad faith conduct. Defendant-mortgagors also argue that plaintiff lacks standing.

PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT IS DENIED

A plaintiff seeking summary judgment in a foreclosure action is required to produce the mortgage, the unpaid note, and evidence of default (*see* ***DLJ Mtg. Capital, Inc. v Sosa,*** 153 AD3d 666, 60 NYS3d 278 [2d Dept 2017]; ***Pennymac Holdings, LLC v Tomanelli***, 139 AD3d 688, 32 NYS3d 181 [2d Dept 2016]). Here, plaintiff produced, *inter alia*, the note, mortgage and loan modification agreement. Contrary to defendant-mortgagors' contention, plaintiff established its standing as the holder of the note by attaching it to the summons and complaint, demonstrating that the note was in its possession prior to the commencement of the action (*see* ***Wells Fargo Bank v Thomas,*** 150 AD3d 1312, 52 NYS3d 894 [2d Dept 2017]; ***U.S. Bank, N.A. v Saravanan***, 146 AD3d 1010, 45 NYS3d 547 [2d Dept 2017]; ***Nationstar Mtge., LLC v Catizone***, 127 AD3d 1151, 1152, 9 NYS3d 315 [2d Dept 2015]).

However, plaintiff failed to submit satisfactory evidentiary proof that defendant-mortgagors defaulted in payment under the subject note and mortgage and particularly under the loan modification agreement. Plaintiff submitted an affidavit, dated August 16, 2018, from Carli Jo Wilcox, an employee of New Penn Financial, LLC d/b/a Shellpoint Mortgage Servicing ("Shellpoint"), plaintiff's loan servicing agent. Said affidavit was based upon personal knowledge acquired by a review of business records kept by Shellpoint in the ordinary course of business, including records of prior loan servicers which were fully incorporated and relied upon by Shellpoint in the routine course of business. Based upon those records, the Wilcox affidavit avers that the subject mortgage loan went into default on October 1, 2014. However, Ms. Wilcox

does not identify the business records relied upon and the records are not attached to the affidavit nor otherwise included in the motion papers. Defendant-mortgagors' default in payment has therefore not been established (*see* ***Bank of N.Y. Mellon v Gordon***, 171 AD3d 197, 97 NYS3d 286 [2d Dept 2019]; ***Wells Fargo Bank, N.A. v Kohli***, 173 AD3d 941, 104 NYS3d 124 [2d Dept 2019]).

Further, despite alleging compliance with RPAPL 1304 in its complaint, a condition precedent to commencement of a foreclosure action, plaintiff failed to meet its burden to establish satisfaction of that condition (*see* ***Bank of N.Y. Mellon v Zavolunov,*** 157 AD3d 754, 69 NYS3d 356 [2d Dept 2018]; ***Aurora Loan Servs. LLC v Weisblum,*** 85 AD3d 95, 923 NYS2d 609 [2d Dept 2011]). Plaintiff submitted neither affidavits of service, nor an affidavit from one with personal knowledge of the practices and procedures customarily used in the ordinary course of business for mailing of statutory notices (*see* ***Citibank v Wood,*** 150 AD3d 813, 55 NYS3d 109 [2d Dept 2017]; ***Citimortgage v Papas***, 147 AD3d 900, 47 NYS3d 415 [2d Dept 2017]; ***JPMorgan Chase Bank, Nat. Ass'n v. Kutch***, 142 A.D.3d 536, 537, 36 N.Y.S.3d 235, 236 [2d Dept 2016]). The Wilcox affidavit averred, in conclusory fashion, that the notices were sent by certified and first class mail. Such conclusory statements are insufficient (*see* ***Citimortgage v Espinal,*** 134 AD3d 876, 23 NYS3d 251 [2d Dept 2015]). While Ms. Wilcox averred that she had personal knowledge of the records maintained by Shellpoint, she did not describe and plaintiff otherwise failed to submit proof of "a standard office mailing procedure designed to ensure that items are properly addressed and mailed, sworn to by someone with personal knowledge of the procedure" (***Wells Fargo Bank, N.A. v Mandrin***, 160 AD3d 1014, 1016, 76 NYS3d 182 [2d Dept 2018]; *see also* ***Bank of America v Guillaume***, 169 AD3d 625, 94 NYS3d 114 [2d Dept 2019]; ***Bank of America N.A. v Wheatley,*** 158 AD3d 736 [2d Dept 2018]; ***Wells Fargo Bank, N.A. v Trupia***, 150 AD3d 1049, 55 NYS3d 134 [2d Dept 2017]; ***Wells Fargo Bank, N.A. v Lewczuk***, 153 AD3d 890, 61 NYS3d 244 [2d Dept 2017]).

As plaintiff failed to produce sufficient evidentiary proof that defendant-mortgagors defaulted on the note, its motion must be denied regardless of the sufficiency of the opposing papers (*see* ***Winegrad v New York Univ. Med. Ctr.***, 64 NY2d 851, 487 NYS2d 316 [1985]; ***Citibank N.A. v Abraham***, 138 AD3d 1053, 31 NYS3d 517 [2d Dept 2016]). Accordingly, plaintiff's objection to defendant-mortgagors having been untimely in filing their opposition to plaintiff's motion is academic. As plaintiff was not prejudiced by the purportedly late opposition, it may be disregarded in the Court's discretion pursuant to CPLR 2001. Likewise, although defendant-mortgagors styled their motion as a cross-motion, it may, in view of plaintiff's objection as to when it was filed, be properly deemed a motion in its own right in compliance with CPLR 2214.

DEFENDANTS' CROSS-MOTION IS GRANTED IN PART AND DENIED IN PART

Defendant-mortgagors cross-move for partial summary judgment in their favor pursuant to several of their counterclaims, including claims for declaratory relief, and various forms of damages. Defendant-mortgagors allege, among other things, that plaintiff breached the loan modification agreement of August 2014, breached their duty of good faith and fair dealing, wrongfully declared the borrowers to be in default under the agreement, and wrongfully commenced the instant action. Defendant-mortgagors further allege that plaintiff committed deceptive practices under GBL 349, and a pattern of bad faith conduct under CPLR 3408. Plaintiff's actions allegedly resulted in harm to defendant-mortgagors, including the accrual of unnecessary fees and costs and emotional distress. Defendant-mortgagors seek dismissal of the complaint and rescission of the subject note and mortgage or alternatively specific performance of the loan modification agreement, sanctions under CPLR 3408, sanctions against plaintiff and plaintiff's attorneys

pursuant to 22 NYCRR 130-1, punitive damages, costs and attorneys fees pursuant to RPL 282. It is noted that although defendant-mortgagors' notice of motion does not explicitly request dismissal of the complaint, their affirmation in support does explicitly make that request. In any event, as the request for dismissal of the complaint directly relates to the issues before the Court, the Court may "search the record" and consider the request (CPLR 3212(b); ***Dunton v Hilco Constr. Co.***, 89 NY2d 425, 429, 654 NYS2d 335 [1996]).

Statement of Facts

Plaintiff's complaint alleges "That on or about August 1, 2014, Defendants Kleynowski duly executed, acknowledged, and delivered to a [sic] mortgage modification and agreement to the mortgagee named therein which among other things, modified the principal balance, interest rate and monthly payment of the original indebtedness (Exhibit "E")" and, that said loan modification was duly recorded in the Office of the Suffolk County Clerk. Plaintiff's affidavit in support of summary judgment from Carli Jo Wilcox, referenced above, supports those allegations, as does a copy of the fully executed and recorded loan modification agreement provided as an exhibit. Additionally, in a certificate of merit pursuant to CPLR 3012-b, plaintiff's counsel Richard F. Komosinski, Esq. affirmed, among other things, that he reviewed all pertinent documents including the loan modification agreement, and certified that plaintiff was entitled to enforce its rights under those documents. As mentioned above, the August 2014 loan modification was actually executed by plaintiff on September 15, 2014. It is entitled "Home Affordable Modification Agreement." The salient terms of the loan modification include a new principal balance of $364, 427.39; an interest rate of 2% for 60 months, 3% for the following 12 months, 4% for the following 12 months, and 4.125% for the remaining 210 months. The initial monthly payment for principal, interest and escrow for the first 60 months was set at $2,339.91. The monthly payments for the entire term of the agreement were subject to periodic adjustments for escrow.

The subject loan modification was preceded by a trial loan modification offered by plaintiff's predecessor Citimortgage by letter dated February 4, 2014, which required trial payments on the first day of March, April and May 2014. Following successful completion of the trial loan modification, Citimortgage and defendant-mortgagors executed the permanent loan modification. The approval by Citimortgage of the trial and permanent loan modifications was in settlement of a prior action, Citimortgage v. Kleynowski, #19299/11, which was discontinued in January 2014. After completion of the trial loan modification in May 2014, plaintiff did not provide borrowers with a permanent loan modification for execution until August 2014. Although not required to do so, the borrowers made two additional monthly payments prior to receipt of the permanent loan modification. When the borrowers received the permanent loan modification documents in August, they immediately signed and returned them to Citimortgage along with the payment for September 1, 2014, as called for by the terms of the agreement and despite Citimortgage not having executed it yet. Subsequently, Citimortgage sent the borrowers a monthly mortgage statement, dated September 8, 2014, reflecting the terms of the loan modification, to wit: the new principal balance, the absence of arrears, the new 2% initial interest rate, and the monthly payment that was due on October 1, 2014. In a letter to the borrowers dated September, 15, 2014 (the same date Citimortgage executed the loan modification), Citimortgage stated "Thank you for returning your signed modification documents... In accordance with your Modification program guidelines, we have enclosed a copy of your modification agreement signed by a CitiMortgage, Inc. officer. This agreement is for your records and no further action is necessary."

In direct contradiction of those written communications affirming the loan modification, Citimortgage sent defendant-mortgagors a letter dated October 1, 2014 advising them that they were in default for a past due amount of $83,822.25, which must be paid by November 5, 2014. In another letter, one day later on October 2, 2014, Citimortgage advised defendant-mortgagors that they were in default in the amount of $85,601.95, which if not paid by November 6, 2014 may result in foreclosure. According to the affirmation of defendant-mortgagors' counsel Craig D. Robins, Esq., his office communicated with three different representatives of Citimortgage by telephone on October 23, 2014, and received varying explanations as to the reason for their conflicting correspondence. According to Mr. Robins, those explanations included "internal issues," that the modification was "booked and unbooked" due to an omitted $125 legal fee, and that "the processor made a mistake." Mr. Robins's office explained that the fully executed loan modification was a legally binding contract and that performance was expected. Mr. Robins's office was also told that Citimortgage had received the October 2014 monthly payment, that the matter was being escalated to the "Executive Response Unit," and that the borrowers should continue to "follow the original agreement." Plaintiff does not dispute any of those communications.

Near the end of October 2014, Citimortgage sent the borrowers a letter, dated October 1, 2014, which included a newly proposed loan modification agreement. This correspondence contained at least one ambiguity in that it stated that the borrowers were eligible for a loan modification if they complied with the terms of a trial period plan, however its terms indicated that a permanent loan modification was actually intended, commencing November 1, 2014. Moreover, the newly proposed loan modification contained a higher interest rate for the last 216 months of the loan, a longer term, and a higher new principal balance. According to Mr. Robins, his office communicated by telephone with Patrick Hadican of Citimortgage's Customer Research Team, on October 28 and 29, 2014. Mr. Hadican stated that the previously executed loan modification of August 2014 contained incorrect interest rates and dates; he could not explain why default notices were sent on October 1 and 2, 2014; and instructed that the borrowers make their November 2014 payment in accord with the "original" agreement. In a follow-up telephone conversation on November 6, Mr. Hadican stated that the original loan modification was a "mistake," and that the proposed modification of October 2014 "is the offer." When asked if Citimortgage's legal department had researched the issue, Mr. Hadican responded that it had not. Later in the afternoon on November 6, 2014, Mr. Hadican sent an e-mail to Mr. Robins's office stating "As we discussed earlier on the phone, there were issues with the documents that were sent and that is why we had to have a new set sent...After the second set went out, the maturity terms were incorrect, which caused the third set to have to be regenerated and sent to the borrower. The third set of documents, with a longer maturity date, are the correct documents, and the final offer." (Evidently, the "third set" is the proposed loan modification included in the October 1, 2014 correspondence). Plaintiff does not dispute any of the foregoing communications.

A letter from Citimortgage, dated November 6, 2014, informed the borrowers that they were unfortunately not eligible for an alternative to foreclosure, that Citimortgage was "disappointed" that it could not approve borrowers for a loan modification, that late charges have accrued, and that arrears in the amount of $90,261.09 were due immediately. The letter further stated that a modification could not be offered because "On 11/3/2014 you either withdrew your request to be considered for a Home Affordable Modification or did not accept an offer of a Trial Period Plan or Home Affordable Modification." The letter goes on to state that in reviewing the request for modification, the net present value (NPV) of the modification was calculated, and four pages of generic NPV information were attached. There had been no prior indication that NPV was ever in issue. There was nothing in this letter to indicate that the borrowers' concerns regarding repudiation of an executed loan modification were reviewed. To the contrary, it appears

to be little more than a largely generic and ambiguous denial letter as might be sent to any unsuccessful loan modification applicant.

In a six-page letter dated November 14, 2014 addressed to Mr. Hadican, described as a good faith effort to resolve the matter, Mr. Robins set forth in detail the chronology of events which had transpired thus far, his concerns with Citimortgage's breach of the executed loan modification, and the fact that the borrowers never rejected the executed loan modification. By letter dated November 28, 2014, Citimortgage (generically through no particular individual) acknowledged receipt of Mr. Robins's letter and stated that the matter was being referred for review by Homeowners Support Specialist Tori Dye. In a second letter dated November 28, 2014, Citimortgage advised Mr. Robins that it did not have an authorization to speak with his office (patently disingenuous as Mr. Robins had been representing and negotiating on the borrowers' behalf since the onset of the prior action in 2011). Having received no substantive response to his letter of November 14, Mr. Robins sent Mr. Hadican another letter, dated January 7, 2015, requesting a response. On January 20, 2015, Mr. Robins received a letter from Citimortgage stating again that it did not have an authorization to speak with him. By letter dated January 21, 2015, Citimortgage acknowledged receipt of Mr. Robins's letter, stated that the modification process had been closed as of November 3, 2014 because the borrowers failed to return the proposed loan modification of October 1, 2014, and referring any questions to Homeowners Support Specialist Jean Baker. This letter simply repeated old information and contained no indication that a review of the particular circumstances, as promised, had taken place.

Despite all the foregoing, the borrowers continued to make and Citimortgage continued to accept all monthly payments under the executed loan modification through April 2015. That fact is amply demonstrated by copies of the cancelled checks provided by the borrowers and the affidavits of defendant Nancy Kleynowski, dated December 4, 2018 and April 25, 2019. Plaintiff provided no countervailing evidentiary proof regarding the payments tendered and accepted under the loan modification. Citimortgage refused to accept the monthly payment for May 2015 tendered by the borrowers, the same month it recorded the executed loan modification agreement with the Office of the Suffolk County Clerk. The tender and rejection of the May 2015 payment is also amply substantiated by the April 25, 2019 Kleynowski affidavit, and is uncontroverted with any evidentiary proof from plaintiff.

The motion papers do not disclose precisely when Citimortgage transferred the note and mortgage to plaintiff, however according to the complaint, the transfer was subsequently memorialized by a written assignment dated March 28, 2016. According to a Limited Power of Attorney submitted by plaintiff, Shellpoint became plaintiff's loan servicer as of September 17, 2015. After transfer of servicing responsibilities to Shellpoint, Mr. Robins continued his efforts to get plaintiff to abide by the terms of the executed loan modification. In a nine-page letter dated March 23, 2016 addressed to Shellpoint, Mr. Robins set forth a detailed chronology of events, objected to the continued default notices and threats of foreclosure being sent to the borrowers, and requested that the terms of the loan modification be followed. Shellpoint responded with a letter dated May 2, 2016, stating that the executed loan modification agreement contained errors, that a newly proposed agreement correcting those errors was sent to the borrowers, but since it was not signed and returned, the agreement was cancelled. Mr Robins responded back with a letter dated May 4, 2016, reiterating that the loan modification had been fully executed and enclosing a copy of same. In a letter dated June 13, 2016, Shellpoint stated that its stance on the matter remained unchanged and that it was "unable to apply the modified terms based on the signed agreement."

After plaintiff commenced the present action and obtained new legal counsel, Mr. Robins thought the new attorneys would be receptive to investigating and resolving the matter. In a five-page letter dated

February 13, 2018, addressed to Mark Golab, Esq., the supervising litigation attorney at Knuckles, Komosinski & Manfro, LLP, Mr. Robins explained the circumstances, referenced and enclosed some copies of the exhaustive correspondence which had been exchanged, and requested that a pragmatic resolution be explored. In particular, Mr. Robins pointed out that plaintiff was now suing upon the same executed loan modification that for years it had attempted to avoid. According to Mr. Robins, despite that letter and numerous phone conversations with plaintiff's attorneys, plaintiff maintained its position. Plaintiff does not dispute those good faith efforts on the borrowers' part to seek a pragmatic resolution.

The above facts are demonstrated by a comprehensive record of written documentation submitted by defendant-mortgagors, including loan documents, bank statements and correspondence from plaintiff, and the affidavits of defendant Nancy Kleynowski dated December 4, 2018 and April 25, 2019, with supporting papers. In response to defendant-mortgagors' showing, plaintiff provided only the affirmation of plaintiff's counsel Edward L. Poff, Esq. dated February 14, 2019. The Poff affirmation has no probative value (*e.g.* ***Zuckerman v City of New York***, 49 NY2d 557, 427 NYS2d 595 [1980]), and in any event does not refute defendant-mortgagors' proof. Plaintiff's opposition does not respond to the graveman of defendant-mortgagors' allegations of bad faith and breach of contract, etc. The opposition does not explain how plaintiff went from repudiating the loan modification to suing for its enforcement. Instead, the opposition argues that the reason for holding borrowers in default under the loan modification was their failure to make the first due monthly payment under the agreement of September 1, 2014. That is completely different from the purported reason previously communicated to borrowers. Plaintiff's opposition also baldly argues that the borrowers failed to demonstrate that they made eight payments under the loan modification, without offering any evidentiary proof to controvert the documentary proof provided by the borrowers.

Breach of contract

The pleadings alone and the evidentiary proof adduced by both parties establishes that there was in fact a fully executed loan modification agreement/contract in existence between the parties herein, upon which plaintiff now seeks enforcement, to wit: the above-described loan modification of August 2014, recorded in the Office of the Suffolk County Clerk, at Liber M00022593, page 640, on May 20, 2015. The evidentiary proof also establishes that the plaintiff breached said contract by repudiating it, both verbally and in writing, multiple times between October 2014 and June 2016, and moreover by the act of refusing a timely payment tendered by the borrowers in attempted fulfillment of their obligations under the contract in May 2015. The Court therefore declares plaintiff to be in breach of contract and directs specific performance of the unfulfilled obligations under the loan modification (*see* ***EMC Mortg. Corp. v Gross***, 289 AD2d 438, 735 NYS2d 581 [2d Dept 2001]). Accordingly, plaintiff is directed to calculate a new principal balance, using the principal balance of $364,427.39 stated in the August 2014 loan modification as a starting point, crediting borrowers for eight payments made under that agreement, and subtracting the interest, costs and all fees accrued between May 1, 2015 and the date of this order, as will be further addressed below. Further, plaintiff is directed to calculate the amount of monthly payments going forward at an interest rate of no more than 2% for at least 52 months, and subsequent monthly payments for the remainder of the term of the agreement in accord with the interest rates set forth in the agreement and as specified above. Plaintiff is further directed to report these recalculations to the Court at the above-directed Court conference.

Because the evidentiary proof establishes that plaintiff is the defaulting party under the loan modification agreement and that the borrowers did not default under the agreement, plaintiff is as a matter of law unable to meet the elements of proof for a foreclosure action (*see e.g.* ***DLJ Mtg. Capital, Inc. v Sosa***, *supra*). Accordingly, the complaint is dismissed.

Failure to negotiate in good faith under CPLR 3408

CPLR 3408(f) mandates that the parties shall negotiate in good faith. Under CPLR 3408(i) the court is authorized to "determine whether either party fails to comply with the duty to negotiate in good faith ... and order remedies pursuant to subdivisions (j) and (k) ..." Under CPLR 3408(j), "[u]pon a finding by the court that the plaintiff failed to negotiate in good faith ... the court shall, at a minimum, toll the accumulation and collection of interest, costs, and fees during any undue delay caused by the plaintiff ..." "Compliance with the obligation to negotiate in good faith ... shall be measured by the totality of circumstances" (***US Bank N.A. v Sarmiento***, 121 AD3d 187, 200, 991 NYS2d 68 [2d Dept 2014]). The Court has broad discretion in determining questions regarding good faith under CPLR 3408(f) (*see* ***Wells Fargo Bank, N.A. v Meyers***, 108 AD3d 9, 15, 966 NYS2d 108 [2d Dept 2013]). Among the specified factors to be considered by the court under 3408(f) are "compliance with applicable mortgage servicing laws, rules, regulations, investor directives, and loss mitigation standards ... avoiding unreasonable delay ... and providing accurate information to the court and parties." Furthermore, "[a] foreclosure action is equitable in nature and triggers the equitable powers of the court ... Once equity is invoked, the court's power is as broad as equity and justice require (internal citations and quotation marks omitted)" (***U.S. Bank Natl. Assn. v Losner***, 145 AD3d 935, 937, 44 NYS3d 467 [2d Dept 2016]; *see also* ***U.S. Bank N.A. v Williams***, 121 AD3d 1098, 1101-2, 995 NYS2d 172 [2d Dept 2014]; ***Wells Fargo Bank, N.A. v Meyers***, *supra*). Further, as plaintiff did not controvert defendants' account of the settlement negotiations, which was supported by evidentiary proof, with evidentiary proof of it own, a hearing on the matter is not required (*see* ***LaSalle Bank, N.A. v Dono***, 135 AD3d 827, 24 NYS3d 144 [2d Dept 2016]).

Here, the evidentiary proof shows a pattern of bad faith conduct on plaintiff's part over the course of over three years. First, plaintiff failed to honor its obligations under a fully executed permanent loan modification agreement. Plaintiff repudiated the agreement without cause almost immediately after executing it. Two weeks after executing and accepting the first payment under the agreement, plaintiff sent the borrowers notices demanding payment of the full amount of the arrears which had accumulated prior to the agreement (over $80,000), and threatening a foreclosure action. The borrowers attorney contacted plaintiff numerous times in an effort rectify the situation, including a request that plaintiff seek review from its legal department. Plaintiff continued to repudiate and abandon its obligations and attempted to substitute the executed agreement with another newly proposed loan modification bearing less favorable terms for the borrowers. In one notice, dated November 6, 2014, after the borrowers rejected the newly proposed agreement, plaintiff informed them that they did not qualify for a loan modification, that past due arrears in the amount of over $90,000 were due immediately, and that a loan modification could not be offered because the borrowers had either withdrawn their request or failed to accept a loan modification offer. This was obviously a perfunctory response that did not address the real issue at hand, which was the abandonment of the executed loan modification not the rejection of a substitute agreement. Despite having numerous opportunities to rectify its untenable position, Citimortgage failed to do so and instead gave the borrowers conflicting information and shifted responsibility for oversight of the borrowers' loan to multiple different internal departments and at least six different individuals. Plaintiff accepted eight monthly payments under the executed loan modification and then refused a ninth payment tendered in May 2015. After transfer of loan servicing to Shellpoint and substitution of new counsel on plaintiff's behalf, the borrowers' attorney made renewed, concerted good faith efforts with Shellpoint and counsel to rectify the situation, yet plaintiff remained intransigent. Then, despite claiming for years that it would not honor the executed loan modification, and breaching the agreement by refusing a tender of payment, plaintiff commenced the instant action on the basis of that very agreement and declared the borrowers in default.

The uncontroverted facts amply demonstrates a pattern of inattentiveness and flawed management, oversight and evaluations on plaintiff's part, resulting in among other things, serious errors, miscommunications, and an unnecessary accumulation of costs throughout the course of settlement negotiations. On this record, the Court finds that plaintiff's conduct constituted a failure to negotiate and otherwise exercise good faith in this matter from October 2014 forward, and that sanctions under CPLR 3408 are therefore warranted. As plaintiff met the terms of the loan modification in so far as accepting monthly payments through April 2015, the Court orders that all interest, fees and costs accrued on the subject loan between May 1, 2015 and the date of this order, are cancelled (*see* ***US Bank N.A. v Sarmiento***, *supra*; ***U.S. Bank N.A. v Williams,*** *supra;* ***U.S. Bank N.A. v Smith***, 123 AD3d 914, 999 NYS2d 468 [2d Dept 2014]; ***Aurora Loan Services, LLC v Diakite***, 148 AD3d 662, 48 NYS3d 490 [2d Dept 2017]).

Breach of duty of good faith and fair dealing
Punitive Damages

Defendant-mortgagors also argue that the plaintiff's breach of its contractual duty of good faith and fair dealing warrant an award of punitive damages. "Implicit in every contract is an implied covenant of good faith and fair dealing (citation omitted)... a pledge that neither party to the contract shall do anything which shall have the effect of destroying or injuring the right of the other party to receive the fruit of the contract... (citations omitted)" (***Gutierrez v Government Empls. Ins. Co.***, 136 AD3d 975, 976, 25 NYS3d 625 [2d Dept 2016]; *see also* ***Dalton v Educ. Testing Serv.***, 87 NY2d 384, 639 NYS2d 977 [1995]). Under certain limited circumstances, a breach of the duty of good faith and fair dealing may result in an award of compensatory and punitive damages (*see* ***Racanova v Equitable Life Assur. Soc'y***, 83 NY2d 603, 612 NYS2d 339 [1994]).

The Court here is informed by the case of *Shaw v Citimortgage, Inc.*, 201 F.Supp.3d 1222 [D. Nev. 2016], cited by defendant-mortgagors. That case also involved Citimortgage and facts that are remarkably similar to those present here. The *Shaw* court awarded punitive damages against Citimortgage. In support of that award the court highlighted the following factors:

> "The lack of company policies and management oversight in this action allowed CMI [Citimortgage], through its Loss Mitigation, underwriting, and Executive Response Unit departments, to take the offensive position that CMI was entitled to require Shaw to abandon the fully executed May 2011 Modification Agreement in favor of the proposed July 2011 Modification Agreement ... In essence, CMI chose to ignore its own agreement ... Beyond the above, the court also finds that there was a serious lack of practices, policies and procedures to deal with and explain the company's positions and actions to the borrower/homeowner. Here, despite repeated requests for information as to why Shaw received contradictory and inconsistent communications, CMI never provided any meaningful explanations... CMI's failures in this action are exacerbated by the frustration and unexplained revolving door of CMI personnel with whom Shaw was required to deal.... Moreover, the evidence established that Shaw informed each new CMI representative of the history of his mortgage account and rather than investigate the matter further - ... - these representatives continued to push forward with CMI's untenable position that there was no valid and binding loan modification ... CMI willfully ignored the harm it was causing to Shaw despite clear warning signs from Shaw that its conduct was improper..."

id. at 1264.

On the record in the present case, the circumstances to support an award of punitive damages against plaintiff has not been satisfactorily established. However, subject to possible further discovery and fact-finding, which will be discussed at the Court conference directed above, defendant-mortgagors' counterclaim for punitive damages, as well as their related counterclaims for intentional and negligent infliction of emotional distress, remain viable.

General Banking Law 349

Defendant-mortgagors' fifth counterclaim alleges that plaintiff violated the "Deceptive Practices Act" by "[e]xtending credit to Defendants based on the erroneous valuation of their collateral, rather than on their genuine ability to repay the obligations, thus putting Defendants at risk of foreclosure." In their present cross-motion, defendant-mortgagors do not argue the allegations of the counterclaim, but instead argue that plaintiff's repudiation of an executed loan modification, acceptance of payments thereunder, and subsequent commencement of this foreclosure action, constituted deceptive practices under New York General Business Law 349. GBL 349(a) provides that "deceptive acts or practices in the conduct of any business, trade or commerce or in the furnishing of any service in this state" is unlawful. GBL 349(h) provides for a private cause of action by any person who has been injured by a violation of the statute. "To assert a viable claim under General Business Law 349(a), a plaintiff must *plead* that (1) the challenged conduct was consumer-oriented, (2) the conduct or statement was materially misleading, and (3) damages" (emphasis added) (***Lum v New Century Mtge. Corp.***, 19 AD3d 558, 559, 800 NYS2d 408 [2d Dept 2005; *see also* ***Emigrant Mtge. Co., Inc. v Fitzpatrick***, 95 AD3d 1169, 945 NYS2d 697 [2d Dept 2012]). "[A]s a threshold matter, plaintiffs claiming the benefit of section 349 must *charge* conduct that is consumer-oriented" (emphasis added) (***Oswego Laborers' Local 214 Pension Fund v Marine Midland Bank***, 85 NY2d 20, 25, 623 NYS2d 529 [1995]). The conduct need not be repetitive or recurring but "must have a broader impact on consumers at large. Private contract disputes unique to the parties, for example, would not fall within the ambit of the statute" (*id.* at 25). Defendant-mortgagors failed to satisfactorily plead a claim under GBL 349, and in any event, did not make out a prima facie showing to support such a claim (*id.*; *see also* ***New York Univ. v Cont'l Ins. Co.***, 87 NY2d 308, 639 NYS2d 283 [1995]).

Attorney fees

RPL 282 provides in pertinent part that a mortgagor under a mortgage contract on residential property is entitled to an award of attorney's fees "in the successful defense of any action or proceeding commenced by the mortgagee against the mortgagor arising out of the contract." As defendant-mortgagors here have been successful in the defense of plaintiff's action, they are entitled to an award of attorney fees under RPL 282 (*see* ***Deutsche Bank Natl. Trust Co. v Gordon***, 2020 NY Slip Op 00261 [2d Dept]; ***21st Mtge. Corp. v Nweke***, 165 AD3d 616, 85 NYS3d 127 [2d Dept 2018]). As ordered above, defendants' counsel is directed to provide the Court and plaintiff's counsel with an affirmation of legal fees prior to the upcoming conference directed herein.

Sanctions under 22 NYCRR 130-1.1

Defendants' cross-motion includes a request to impose sanctions against plaintiff and plaintiff's counsel for their frivolous conduct under 22 NYCRR 130-1.1. Under subsection (a) of that regulation, courts, in their discretion, may award reasonable costs and attorney's fees and may impose additional financial sanctions upon any party or attorney resulting from frivolous conduct. Under subsection (c), frivolous conduct includes conduct which "is completely without merit in law and cannot be supported by a reasonable argument for an extension, modification or reversal of existing law." Subsection (c) further

provides: "In determining whether the conduct undertaken was frivolous, the court shall consider, among other issues the circumstances under which the conduct took place, including the time available for investigating the legal or factual basis of the conduct, and whether or not the conduct was continued when its lack of legal or factual basis was apparent, or should have been apparent, or was brought to the attention of counsel or the party."

Here, plaintiff repudiated the loan modification agreement and refused to accept monthly payments. Despite maintaining that position for years and being the party in default, plaintiff declared the borrowers in default and commenced the present foreclosure action based on that very agreement. Defendant-mortgagors' counsel sent several detailed letters to plaintiff and plaintiff's counsel advising them of the circumstances and the legally untenable nature of their position. Both before and after commencement of the action, plaintiff and plaintiff's counsel were given ample opportunity to investigate the factual and legal basis of their position. Plaintiff and plaintiff's counsels' intransigence is all the more egregious considering that they were aware, or should have been aware, of the *Shaw* case described above, where quite significant punitive damages were imposed for conduct remarkably similar to that here. The Court finds that plaintiff and plaintiff's counsel engaged in frivolous conduct by, among other things, commencing this action, and therefore defendant-mortgagors' cross motion for sanctions under 22 NYCRR 130-1.1 is granted to the extent that a hearing shall be held to determine the amount of such sanctions (*see* ***Miller v Falco***, 170 AD3d 707, 95 NYS3d 334 [2d Dept 2019]; ***Nicotra v Dignam***, 2020 NY Slip Op 31934(U) [Sup Ct, New York County]).

Accordingly, the decision and order of the Court is that plaintiff's motion for summary judgment is denied; defendant-mortgagors' cross-motion for partial summary judgment is granted in part as set forth herein, and is otherwise denied; and the parties are directed to appear for a Court conference as directed above.

Dated: 10/27/2020

HON. MICHAEL A. GAJDOS, JR., J.S.C.

____ **FINAL DISPOSITION** __X__ **NON-FINAL DISPOSITION**

Hearing Date: April 20, 2017; 10:00 a.m.

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NEW YORK

----------X

In re: Case No.: 1-13-42618-ESS

DANIEL MATOVINOVIC Chapter 7

Judge Elizabeth S. Stong

Debtor.

----------X

NOTICE OF MOTION SEEKING TO HOLD GROSS POLOWY LLC IN CONTEMPT FOR VIOLATING ORDER OF DISCHARGE AND SEEKING SANCTIONS

PLEASE TAKE NOTICE, that upon the annexed papers, on **April 20, 2017, at 10:00 a.m.** or as soon thereafter as counsel can be heard, Debtor, **DANIEL MATOVINOVIC**, by and through his attorneys, the Law Offices of Craig D. Robins, will move before the Honorable Elizabeth S. Stong, United States Bankruptcy Judge, United States Bankruptcy Court, Courtroom 1595, 271 Cadman Plaza East, Brooklyn, New York 11201, seeking the entry of an Order finding respondent, **Gross Polowy, LLC,** as counsel for creditor, The Bank of New York Mellon f/k/a The Bank of New York as Trustee for the Certificate Holders of the CWMBS Inc. CHL Mortgage Pass-Through Trust 2005-28, Mortgage Pass-Through Certificates, Series 2005-28 ("Bank of New York" or "Mortgagee"), in contempt for willfully violating the discharge injunction, and imposing sanctions for civil contempt, and awarding actual and punitive damages,

attorney's fees, and for such other and further relief as this Court deems just and proper.

PLEASE TAKE FURTHER NOTICE, objections to the Debtor's application shall be filed as follows: (a) (i) through the Bankruptcy Court's electronic filing system which may be accessed through the Internet at the Bankruptcy Court's website: www.nyeb.uscourts.gov, using Netscape Navigator software version 3.0 or higher, and (ii) in portable document format (PDF) using Adobe Exchange software for conversion; or (b) if a party is unable to file electronically such party shall submit the objection in PDF format on a diskette in an envelope with the case name, case number, type and title of document, document number of the document to which the objection refers, and the file name on the outside of the envelope; or (c) if a party is unable to file electronically or use PDF format, such party shall submit the objection on a diskette in either Word, WordPerfect, or DOS test (ASCII) format. An objection filed by a party with no legal representation shall comply with section (b) or (c) as set forth in this paragraph. A hard copy of the objection, whether filed pursuant to section (a), (b) or (c), as set forth in this paragraph, shall be hand-delivered directly to the Chambers of the Honorable Elizabeth S. Stong, and a hard copy shall be served upon the Debtor's counsel, Law Offices of Craig D. Robins, 35 Pinelawn Road, Suite 218-E, Melville, New York, New York, and filed with the Clerk of the Bankruptcy Court, at least seven (7) days before the scheduled hearing date.

PLEASE TAKE FURTHER NOTICE, if no objections are timely filed, the Court may grant the relief requested without further notice.

Dated: Melville, New York
March 6, 2017

/s/ Craig D. Robins, Esq.
Craig D. Robins, Esq. (CR5938)
LAW OFFICES OF CRAIG D. ROBINS
Attorneys for the Debtor
35 Pinelawn Road, Suite 218-E
Melville, New York 11747
(516) 496-0800

To:

Gross Polowy LLC
1775 Wehrle Drive
Suite 100
Williamsville, NY 14221

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NEW YORK

----------X

In re: Case No.: 1-13-42618-ESS

DANIEL MATOVINOVIC Chapter 7

Debtor.

----------X

AFFIRMATION IN SUPPORT OF MOTION SEEKING TO HOLD GROSS POLOWY LLC IN CONTEMPT

Craig D. Robins, Esq., an attorney duly admitted to practice law in the State of New York and before this Court, affirms the following to be true under the penalty of perjury:

1. I am the attorney of record for Daniel Matovinovic (the "Debtor"), and as such, I am fully familiar with the facts and circumstances of this matter.

SUMMARY

2. This application was precipitated by what seems to be a very disturbing and alarming trend. Many creditors and/or their attorneys engage in collection activity and utilize footnotes and bankruptcy disclaimers that essentially say "this is an attempt to collect a debt, but if you've filed for bankruptcy, then never mind."
3. However, the situation in the instant case is much more serious as the lender already commenced suit against Debtor. The lender is Debtor's mortgagee, The Bank of New York Mellon f/k/a The Bank of New York as Trustee for the Certificate Holders of the CWMBS Inc. CHL Mortgage Pass-Through Trust 2005-28, Mortgage Pass-Through Certificates, Series 2005-28 ("Bank of New York" or

"Mortgagee"), and it brought a foreclosure proceeding, also seeking a deficiency on the note, even though the prior bankruptcy filing discharged Debtor's obligation on the note, and the mortgagee and its attorney received notice of the discharge at that time, and actually knew that the Debtor had filed for bankruptcy and received a discharge.

4. The mortgagee's attorneys who drafted the complaint, Gross Polowy LLC ("Gross Polowy"), essentially stated in their mortgage foreclosure pleadings, utilizing *pro-forma* language in an ill-conceived disclaimer, that if the defendant received a bankruptcy discharge, then the defendant should ignore that requested relief.
5. However, this places an unfair and improper burden on Debtor to defend the foreclosure law suit, as Debtor must now defend the action and assert that the debt was discharged in bankruptcy. Debtor suffered great stress and anxiety because of Gross Polowy's violation of the order of discharge and was forced to retain counsel to defend the foreclosure proceeding. Accordingly, the Mortgagee's actions and those of its attorneys are a violation of the discharge order, and contempt of court. Also, because Gross Polowy knew of Debtor's bankruptcy filing and discharge, its violation was willful.
6. In August 2015, for the above reasons, Debtor brought a motion seeking to re-open this case for the purpose of seeking sanctions against the Mortgagee for having violated the order of discharge. Over the course of more than a year, involving about ten court conferences and court-mandated discovery and disclosure, it became apparent that most of the culpability can be attributed to

Mortgagee's counsel, Gross Polowy, LLC ("Gross Polowy"), as they engaged in an incredibly large-scale operation and regular pattern of conduct of using the offensive disclaimer in what appears to be hundreds and hundreds of cases involving not only the Debtor-homeowner in this matter, buy many other homeowners as well.

7. Debtor recently settled his claim against the Mortgagee and now seeks to proceed against its counsel, Gross Polowy. Accordingly, this proceeding is strictly against the mortgagee's counsel, and not against Mortgagee.
8. Incidentally, Gross Polowy defended the Mortgagee for about a year before this Court with the prior motion litigation, up through June 2016. However, a different firm, Blank Rome LLP, actively represented Mortgagee for the remainder of that litigation, up through and including the recent settlement of the claim against the Mortgagee.

JURISDICTIONAL PREDICATE

9. This Court has jurisdiction over this core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A), (I) and (O), and 1334(b), and the Standing Orders of Reference in effect in the Eastern District of New York dated August 28, 1986, and as amended on December 5, 2012, but made effective *nunc pro tunc* as of June 23, 2011.
10. In addition, "[w]here… a debtor thinks a creditor is acting in violation of a bankruptcy court's § 524 discharge order, relief is properly sought in the first

instance from the bankruptcy court…" *Eastern Equip. & Servs. Corp. v. Factory Point Nat'l Bank*, 236 F.3d 117, 121 (2d Cir. 2001).

11. It is clear that the enforcement of the discharge order may be made by means of a contempt motion as opposed to an adversary proceeding. See *In re Nassoko*, 405 B.R. 515, 520 (Bankr. S.D.N.Y. 2009), *In re: Thomas Haemmerle,* Case No.: 06-71530-ast, (Bankr. E.D.N.Y. April 16, 2015).

BACKGROUND

12. Debtor filed a voluntary petition for relief under Chapter 7 of the Bankruptcy Code on April 30, 2013 (the "Petition Date"). Your affirmant represented Debtor in that proceeding.

13. Debtor previously brought motion similar to this one directly against the mortgagee-creditor and also sought to re-open the bankruptcy case for cause, for the purpose of enforcing the discharge injunction against the creditor who holds the mortgage on the Debtor's home. That creditor is The Bank of New York Mellon f/k/a The Bank of New York as Trustee for the Certificate Holders of the CWMBS Inc. CHL Mortgage Pass-Through Trust 2005-28, Mortgage Pass-Through Certificates, Series 2005-28 ("Bank of New York" or "Mortgagee" or "Creditor").

14. Debtor owns the premises commonly referred to as 23-11 154th Street, Whitestone, New York (the "Premises") as tenants by the entirety with his wife, and he reside there as his primary residence together with his wife and children.
15. The Debtor purchased this property in 2005 and financed the purchase with a mortgage from Mortgage World Bankers, Ltd. ("Mortgage World"). However, upon information and belief, all servicing of the mortgage and all communications from this mortgagee to the Debtor were done through either Countrywide Home Loans ("Countrywide") or Bank of America Home Loans ("Bank of America"), who ultimately acquired Countrywide. The Debtor is the sole person who executed the mortgage note ("Note").
16. Upon information and belief, the original mortgagee, Mortgage World, sold and assigned the mortgage to Countrywide, and Countrywide was eventually acquired by Bank of America.
17. In April 2013, just prior to filing, Bank of America identified the account for the subject mortgage as a Bank of America loan and designated a Bank of America loan number to the mortgage.
18. The Debtor listed Bank of America as holding a secured claim on "Schedule D" to the petition. The Debtor also listed Countrywide Home Loans in Schedule D for noticing purposes. A copy of "Schedule D" of the Debtor's petition is annexed hereto as "**Exhibit B**".
19. Prior to the Petition Date, Bank of America was represented by Druckman Law Group. My firm engaged in an extensive amount of communication with the Druckman Law Group for over a year prior to the filing of the petition in an effort

to obtain a mortgage modification for the Debtor. Bank of America declined to offer Debtor a modification at that time. Debtor also listed the Druckman Law Group on Schedule D of the petition as representing Bank of America.

20. Debtor received a full Chapter 7 discharge on August 8, 2013 pursuant to an order of discharge ("Discharge Order.") See "**Exhibit C**" for a copy of the Discharge Order.

21. The Bankruptcy Court generated certain notices to all creditors and parties in interest in this case. These notices included the notice of commencement ("Notice of Commencement") and the Discharge Order. With each such notice, the Bankruptcy Court issued a "certificate of notice" indicating what parties the Court served notice upon, and what address the Court served the party at. The Court Clerk files such notices and certificates of notice as docket entries in this case.

22. The certificates of notice indicate that the Court served Bank of America, Countrywide, and the Druckman Law Group with the Notice of Commencement and the Discharge Order. A copy of the certificate of notice for the Notice of Commencement is annexed hereto as "**Exhibit A**". A copy of the certificate of notice for the Discharge Order is annexed hereto as "**Exhibit D**".

23. On or about May 2, 2015, which is almost two years after the Debtor received a discharge, a process server served the Debtor with a summons and complaint seeking to foreclose on the Debtor's Home. The plaintiff in that complaint is Bank of New York. The Summons is dated March 12, 2015. The law firm that drafted the complaint is Gross Polowy. The complaint was signed by an attorney

in that firm, Laura M. Strauss. Attached to the complaint is a Certificate of Merit Pursuant to CPLR 3012-B.

24. It is unclear how Bank of New York came to own the subject mortgage, but it alleges in its foreclosure complaint that it is the owner of the subject mortgage and note. Presumably, Bank of New York acquired the mortgage from Bank of America.

25. The Complaint contains a "wherefore clause" in which Bank of New York enumerated ten types of relief it is seeking through the foreclosure action ("Wherefore Clause"). In particular, Bank of New York sought the following:

> WHEREFORE, PLAINTIFF DEMANDS… (h) That a deficiency judgment against all obligors on the note, for the amount that remains due after distribution of the sale proceeds, unless the debt was discharged in a bankruptcy, be granted if requested by Plaintiff.

(hereinafter referred to as the "Deficiency Judgment Wherefore Clause"). A copy of the Summons and Complaint, and Certificate of Merit, is annexed hereto as "**Exhibit E**", although exhibits to the Summons and Complaint, consisting of about 50 pages of copies of the mortgage, note and assignments, and other documents, are not annexed.

26. In the prior motion proceeding, the Mortgagee admitted that Mortgagee's servicer knew of the Debtor's bankruptcy filing and Discharge in December 2013, which was well over a year prior to the issuance of the foreclosure summons and complaint, which were dated March 12, 2015.

27. Up through March 1, 2016, Residential Credit Solutions, Inc. serviced the subject mortgage. Effective March 1, 2016, Ditech Financial LLC began servicing the subject mortgage.

28. As indicated in that attached Debtor's Affidavit in support of this motion, Debtor suffered great stress and anxiety because of Gross Polowy's violation of the order of discharge, and it was necessary for Debtor to retain counsel to defend the foreclosure proceeding and demonstrate that he had discharged the mortgage debt.

PRIOR LITIGATION OF THIS ISSUE IN THIS COURT

29. Debtor initially filed a motion, similar to this one, against the Mortgagee, on August 12, 2015. That motion was amended on September 1, 2015.

30. On October 2, 2015 Dennis Jose, Esq. ("Jose") of Gross Polowy, LLC, on behalf of Mortgagee, filed a Notice of Appearance and an affirmation of opposition. Debtor filed a Reply Affirmation on October 8, 2015. Jose filed a Response to Debtor's reply on October 12, 2015 and an additional Affirmation in Opposition on December 29, 2015.

31. On October 20, 2015, this Court issued an order pursuant to 11 U.S.C. § 350(b) reopening this case and determined that it was not necessary to re-appoint a trustee.

32. On June 28, 2016, a different law firm took over representation of the Mortgagee in this matter when Blank Rome LLP filed a Notice of Appearance indicating that they were appearing, as co-counsel, to Residential Credit Solutions, Inc. as

servicer for the Bank of New York Mellon FKA The Bank of New York as Trustee for the Certificate Holder of the CWMBS Inc. CHL Mortgage Pass-Through Trust 2005-28, Mortgage Pass-Through Certificates, Series 2005-28. The attorney who signed that Notice of Appearance, and who actually appeared on behalf of the mortgagee in all matters in this Court after that date, was Jonathan M. Robbin.

33. The Court took a great interest in the prior motion. The parties appeared for conferences on October 13, 2015, January 5, 2016, March 8, 2016, April 12, 2016, April 27, 2016, June 16, 2016, August 16, 2016, and September 20, 2016. Your honor stated on several occasions on the record that the Court was most interested in determining whether the mortgagee's conduct was "an anomaly or a practice."

34. In that regard, the parties engaged in court-ordered discovery and disclosure, the fruits of which and subsequent investigation by Debtor, revealed that Gross Polowy was primarily culpable for a large-scale operation in which it used the problematic Deficiency Judgment Wherefore Clause in what appears to be, at least, many hundreds of cases. This demonstrated that its use of the disclaimer in the instant case was not an anomaly, but instead a regular practice.

35. During the course of the prior motion, the Mortgagee offered Debtor a mortgage modification which Debtor accepted. This modification offer was not part of any settlement or offer of settlement. Although the modification provided Debtor with an opportunity to continue to stay in his home, it also greatly benefited

Mortgagee by returning the mortgage to a performing status rather than forcing it to exercise it *in rem* remedies against the property.

36. In December, 2016, Debtor and Mortgagee settled their issues pursuant to a written "Confidential Settlement Agreement." The settlement agreement provided, among other things, that it did not preclude Debtor from bringing a claim against Gross Polowy, and that certain aspects of the settlement and litigation shall remain confidential, including the settlement amount and any discovery previously exchanged between the parties.

37. On March 6, 2017, Debtor formally withdrew the prior motion and filed the instant motion.

GROSS POLOWY ENGAGED IN A GRAND SCALE OPERATION AND REGULAR PRACTICE OF USING THE IMPROPER BANKRUPTCY DISCLAIMER IN MANY HUNDREDS OF CASES

38. Gross Polowy's use of the bankruptcy disclaimer language in the Deficiency Judgment Wherefore Clause is not an isolated occurrence in the instant case. Instead, it is part of a regular practice that this firm engages in with a great number of its foreclosure cases.

39. Gross Polowy is a foreclosure mill. Upon information and belief, it is one of the largest foreclosure firms in New York. The firm was created in 2011 or 2012 by two senior attorneys from the ashes of notorious giant foreclosure firm, the Steven J. Baum law firm, which had just folded after paying a fine of two million dollars for egregiously improper foreclosure practices. Prior to folding, the Baum firm had handled over half of all foreclosure cases then filed in the State of New

York. Gross Polowy has filed thousands of foreclosure cases against homeowners in New York.

40. After engaging in discovery and disclosure in the prior motion proceeding, and further engaging in many additional hours of investigative work, your affirmant learned the following about Gross and Polowy's mortgage foreclosure practices.

41. Gross Polowy has a number of associate attorneys who regularly churn out foreclosure complaints on behalf of a number of institutional and banking mortgagee clients.

42. Gross and Polowy's associates utilize several different mortgage foreclosure complaint templates that they regularly use over and over again for the various mortgage proceedings that they bring against homeowners. There does not seem to be any rhyme or reason as to which foreclosure complaint template a particular associate uses.

43. One of the most popular templates is the one that Gross and Polowy used to prepare its foreclosure complaint against Debtor. It is that template that contains the offensive bankruptcy disclaimer language in the Deficiency Judgment Wherefore Clause.

44. Different associates have used this foreclosure complaint template in a great number of foreclosure cases involving many different institutional lenders and banks including Bank of New York Mellon, who is the mortgagee in the instant case, HSBC Bank, U.S. Bank, Wells Fargo Bank, Deutsche Bank, and Federal National Mortgage Association (Fannie Mae).

45. New York State has a version of electronic case filing similar to our Bankruptcy Court ECF which is called eFile. That system makes public various legal documents filed in the case. Some New York counties have mandatory eFiling for foreclosure case and some do not. Your affirmant utilized eFile records to manually review a select sampling of cases filed by Gross and Polowy in the Kings County Supreme Court during 2014 to 2016. In doing so, your affirmant discovered that Gross and Polowy engaged in an incredible wholesale practice of regularly commencing foreclosure proceedings with foreclosure complaints containing the offensive bankruptcy disclaimer language in the Deficiency Judgment Wherefore Clause.

46. Attached as "**Exhibits G-1" through "G-25"** are a sampling of 25 typical Gross and Polowy foreclosure complaints located during this search. Each complaint contains the offensive bankruptcy disclaimer language in the Deficiency Judgment Wherefore Clause. These complaints are being offered as a mere sampling. In just the Kings County Supreme Court, for the period reviewed, there were likely hundreds more cases containing the same foreclosure complaint template with the offensive bankruptcy disclaimer.

47. The sampling demonstrates that Gross and Polowy utilized the problematic foreclosure complaint template with an absolute indifference as to whether the homeowner filed for bankruptcy or not.

48. The sampling consists of just a small number of the filings that Gross and Polowy made in just one county, during a relatively short period of time. Accordingly, there should be no doubt that Gross and Polowy utilized this problematic

foreclosure complaint template hundreds and hundreds of times across the state, if not thousands. There are certainly a significant number of homeowners who previously filed for bankruptcy relief, and who were served with these complaints.

ARGUMENT

I. Gross Polowy Violated the Order of Discharge

49. By virtue of the bankruptcy discharge, the financial obligation on the subject mortgage note was discharged, although the mortgagee still retained a valid mortgage lien on the subject premises. The Debtor, in his bankruptcy petition, duly scheduled Bank of America, who apparently owned the subject mortgage at the time of filing, as well as their attorneys, Druckman Law Group, and Bank of America's predecessor in interest, Countrywide. The Court served these entities with the Notice of Commencement and the Discharge Order.
50. Accordingly, the Debtor's obligation to Bank of America was discharged.
51. Debtor acknowledges that the mortgagee retains certain *in rem* rights post-discharge. However, Debtor's *in personam* liability to Bank of America (or any subsequent assignee), was certainly discharged.
52. Even though Bank of New York apparently acquired the subject mortgage from Bank of America, Bank of New York and its attorneys were obligated to acknowledge that Debtor's financial liability on the mortgage note was discharged.

53. When Bank of New York and its attorneys filed a foreclosure action and served Debtor with the foreclosure summons and complaint, they violated the Discharge Order by seeking to collect on the mortgage note that had been discharged, when they knew or should have known of the discharge.

54. In the instant case, the Mortgagee did indeed know of the Debtor's bankruptcy filing and Discharge in December 2013, which was well over a year prior to the issuance of the foreclosure summons and complaint, which were dated March 12, 2015.

55. Nevertheless, Bank of New York, in its Deficiency Judgment Wherefore Clause, stated:

> WHEREFORE, PLAINTIFF DEMANDS… (h) That a deficiency judgment against all obligors on the note, for the amount that remains due after distribution of the sale proceeds, unless the debt was discharged in a bankruptcy, be granted if requested by Plaintiff.

56. This prayer for relief is a violation of the discharge injunction because the creditor is seeking to collect on discharged debt. Bankruptcy Code § 524 provides:

> (a) A discharge in a case under this title—
>
> (2) operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a personal liability of the debtor, whether or not discharge of such debt is waived

In re: Thomas Haemmerle, Case No.: 06-71530-ast, (Bankr. E.D.N.Y. April 16, 2015) in which the Honorable Alan S. Trust, sitting in the Central Islip Bankruptcy Court of our district, recently addressed the issue of a creditor violating a discharge injunction.

57. Bank of New York is seeking to collect on a deficiency judgment on the note, which is clearly an *in personam* obligation that was discharged. Thus, here, because Debtor's personal liability on the Note was discharged, any attempt by the mortgagee to collect on Debtor's discharged personal liability is a violation of Bankruptcy Code § 524(a)(2).

58. However, Bank of New York has a disclaimer of sorts attached to this prayer for relief: "unless the debt was discharged in a bankruptcy." (Hereinafter referred to as the "Bankruptcy Disclaimer").

59. For years, after creditors found themselves defending violation of stay and violation of discharge suits, they have used disclaimers on collection letters that may cross in the mail during which time the recipient may have sought bankruptcy relief. Mortgagees have also used such disclaimers on monthly mortgage bills, claiming that they provide important information. Some mortgagees have suggested that correspondence to a debtor about interest rate changes is technical and informational. *Haemmerle* at 15. However, it seems that some mortgagees, as is the case here, have now begun to commence actual foreclosure litigation, utilizing disclaimer language suggesting that the defendant-homeowner should ignore the requested prayer for relief in the event the defendant-homeowner previously filed for bankruptcy relief. This approach is clearly improper and a violation of a debtor's rights after receiving a discharge. In *Haemmerle*, Judge Trust found that the "informational statements" that the mortgagee in that case sent to the debtor did indeed constitute discharge injunction violations. *Haemmerle* at 15. However, in the instant case, we are not

addressing a mere informational statement, but a full-blown foreclosure law suit that has already been filed in state court.

60. In essence, Gross Polowy's conduct, of preparing and serving pleadings that seek to collect on a deficiency judgment, but including a Bankruptcy Disclaimer which essentially states that the defendant should ignore this relief if the debt was discharged in bankruptcy, improperly and unjustly shifts the burden to the debtor to defend the law suit by requiring the debtor to answer the pleadings, asserting that the debt was indeed discharged. This is what Debtor was forced to do in the instant case. This obligation, created by the Gross Polowy's ill-conceived choice of wording, puts a debtor on the defensive and requires the debtor to take affirmative action by seeking legal advice with regard to defending the prayer for relief. Forcing a debtor to take a defensive posture with a creditor on a discharged debt is totally contrary to the concept of a financial fresh start that bankruptcy is supposed to provide. Yet, this is what the Mortgagee has done.

61. Here, the Mortgagee knew over a year before it brought the foreclosure suit, that Debtor had filed bankruptcy and obtained a bankruptcy discharge. The mortgagee's file in this matter contained the bankruptcy filing information. Upon information and belief, the bankruptcy information was included in the information provided to Gross and Polowy. However, that law firm chose to ignore the bankruptcy information and instead use a prayer for relief that indicated that it was pursuing a deficiency judgment on behalf of their client.

62. Furthermore, the prayer for relief requesting a deficiency judgment, even couched by the Bankruptcy Disclosure, is far from innocuous. This is not an instance of a mortgagee sending a homeowner a monthly statement that contains pay-off amounts, cure amounts and escrow information, and which also contains a bankruptcy disclaimer to assure the recipient that the statement is merely informational. See *In re Patrick*, Case no. 12-30997, page 9 (Bankr. N.D.N.Y. Dec. 14, 2014) citing *In re Schatz*, 452 B.R. 544, 549–50 (Bankr. M.D. Pa. 2011). This is clearly not an instance of an appropriate post-discharge communication. Instead, what we have here is a full-blown mortgage foreclosure lawsuit which a reasonable person can only conclude will create tension, apprehension and anxiety upon the homeowner-defendant that maybe the bankruptcy process has not worked properly and that to prevent a deficiency judgment, legal defense counsel must be immediately retained.

63. From a procedural perspective, obtaining a deficiency judgment is a two-step process. First the mortgagee brings a foreclosure action; then it seeks a deficiency. Pursuant to New York Real Property Actions and Procedures Law (RPAPL) § 1371 (2), a mortgagee moves for a deficiency judgment after the sale of the mortgaged premises. However, it is abundantly clear that Bank of New York's conduct here, by seeking a deficiency judgment in its Deficiency Judgment Wherefore Clause, even if couched by the Bankruptcy Disclaimer, nevertheless amounts to the first step in an attempt to enforce the discharged mortgage debt as a personal liability.

64. Regardless of whether the Mortgagee desired to follow through with seeking a deficiency judgment, by including the Bankruptcy Disclaimer language in the complaint, it has essentially started the collection process.

II. This Court Has Authority to Impose Sanctions For Violations of the Order of Discharge

65. The discharge injunction is intended to further one of the primary purposes of the Bankruptcy Code: giving the debtor an opportunity to make a financial fresh start, unburdened by efforts to collect debts she no longer owes. *Haemmerle*, citing *Green v. Welsh, 956 F.2d 30,* at 33 *(2d Cir. 1992)*, 956 F.2d (citing *In re Jet Florida Systems, Inc*., 883 F.2d 970, 972 (11th Cir. 1989)); *In re Otten*, Case No. 10-74946, Adv. Proc. No. 12-8045 (AST), 2013 Bankr. LEXIS 1920, at *20 (Bankr. E.D.N.Y. May 3, 2013). See also *In re Szenes*, 515 B.R. 1, 6 (Bankr. E.D.N.Y. 2014); *In re Nicholas*, 457 B.R. 202, 224 (Bankr. E.D.N.Y. 2014).

66. It is respectfully submitted that Bankruptcy Code § 105 provides this Court with authority to impose sanctions for a violation of the Discharge Order. Although Bankruptcy Code § 524 does not include an explicit mechanism to enforce this injunction, § 105 of the Bankruptcy Code has been widely accepted as providing statutory authority to enforce the discharge injunction by holding a party who violates the injunction in contempt, and assessing appropriate punishment. *Haemmerle*, citing *In re Nassako*, 405 B.R. 515 (Bankr. S.D.N.Y. 2009) (citing *In re Thompson*, Case No. 06-32633 (SDG), 2007 Bankr. LEXIS 2830, at *6 (Bankr. N.D.N.Y. Aug. 21, 2007) (quoting § 105)); *Szenes*, 515 B.R. at 6; *In re Nicholas, 457 B.R. 202, 225 (Bankr. E.D.N.Y. 2014)* (enforcement of a debtor's discharge

is a core proceeding and "[b]ankruptcy courts retain jurisdiction to enforce and interpret their own orders.") (citations omitted).

67. A discharge injunction violation may be punished as a civil contempt of court, and requires a two part inquiry: "(1) did the party know of the lawful order of the court, and (2) did the defendant comply with it." *Haemmerle*, citing *Nicholas,* 457 B.R. at 225; *In re McKenzie-Gilyard*, 388 B.R. 474, 481 (Bankr. E.D.N.Y. 2007) (citation omitted); *In re DiGeronimo*, 354 B.R. 625, 642 (Bankr. E.D.N.Y. 2006) (holding that a violation of the discharge injunction is willful where "the creditor (1) knew that the discharge had issued, and (2) intended the actions which violated the discharge injunction."); see also 4 Collier on Bankruptcy P 524.02[2][c] ("A creditor's actions in violation of the discharge injunction are willful if the creditor knows the discharge has been entered and intends the actions which violated the discharge injunction.").

68. Here, the Debtor scheduled Bank of America as the creditor holding the mortgage to his home, and the Court provided Bank of America and its attorney with notice of the filing and discharge. The foreclosure suit was brought by Bank of New York, who apparently acquired the mortgage at some point from Bank of America. In any event, the Mortgagee had actual notice of the bankruptcy as its file contained information about the bankruptcy filing and discharge as of December 2013, over a year prior to the time that Gross and Polowy commenced the foreclosure action. During the course of litigation in the prior motion proceeding, the Mortgagee's servicer admitted that it had this information.

69. A creditor's knowledge of the discharge injunction may be actual or constructive. *Nassoko*, 405 B.R. at 522. In the instant case, Mortgagee had actual notice. Thus, the Mortgagee knew or should have known that it was violating the Order of Discharge. As such, the violation can be deemed willful.

70. What is most troubling is that Gross and Polowy, who drafted the complaint, violated their good faith duty to utilize the fact that Debtor previously filed for bankruptcy relief and obtained a discharge – facts which were in the file that their client provided to them. In all likelihood, counsel knew of the bankruptcy filing but chose to ignore that, instead using the pro-forma Wherefore Clause and not adapting it to the specific facts of the case. Counsel's use of a stock *pro-forma* relief provision seeking a deficiency judgment, qualified by a disclaimer provision, smacks of bad faith. Such conduct either reflects extreme laziness on counsel's part to avoid engaging in reasonable due diligence to determine whether it is appropriate to include a request for a deficiency, or an arrogant willful carelessness that they need not bother if they use a bankruptcy disclaimer. The mortgagee's seemingly ill-tailored relief provisions are clearly in violation of the order of discharge.

71. Gross and Polowy's use of the Deficiency Judgment Wherefore Clause in violation of the order of discharge was not an isolated occurrence. It appears that it was standard practice for Gross and Polowy to use a Deficiency Judgment Wherefore Clause as part of a general foreclosure complaint template in case after case. Gross and Polowy's use of the Deficiency Judgment Wherefore Clause is therefore part and parcel of an overall general and standard practice.

That firm served hundreds and hundreds of foreclosure complaints with the offensive language, if not thousands.

72. Even if Gross and Polowy, in a particular foreclosure case, was unaware of whether the homeowner had filed for bankruptcy, the firm could have taken reasonable steps to ascertain whether the homeowner previously filed for bankruptcy or not, and could have checked their client's file to see if it contained that information.

73. It does not make sense that Gross and Polowy would use a Deficiency Judgment Wherefore Clause which contains a bankruptcy disclaimer. Doing so is lazy and sloppy. It would be extremely easy for them to do a quick search of bankruptcy records through PACER and the ECF filing system, which they regularly utilize.

74. The way Gross and Polowy worded its Deficiency Judgment Wherefore Clause, by including the Bankruptcy Disclaimer, created confusion on the part of Debtor as to whether Debtor needed to defend the foreclosure case and engage in additional legal work to ensure that Debtor receives the benefits of his bankruptcy discharge on his *in personam* mortgage liability. By failing to clearly and conspicuously draft the Deficiency Judgment Wherefore Clause in a way that will permit Debtor to understand that the Mortgagee will recognize the bankruptcy discharge, Gross and Polowy has violated the Discharge Order. Gross and Polowy drafted the clause in a way almost designed to invite uncertainty, confusion and concern.

75. As indicated, even if Gross and Polowy did not have bankruptcy filing information in the file it received from their client, or if they were concerned that the

homeowner may have filed for bankruptcy in the interim, they could have easily run a PACER and ECF bankruptcy search to ascertain whether a party had sought bankruptcy relief. After all, the Mortgagee has the homeowner's full name, address, and Social Security number. As this Court undoubtedly knows, doing a PACER search takes no more than a minute; yet Gross and Polowy decided to utilize a totally-unnecessary prayer for relief in bad faith that creates a burden on a debtor-homeonwer to defend, and is a violation of the discharge injunction. This Court must take a position to send a strong message to foreclosing mortgagees and their counsel that such conduct and lazy shortcuts are not permissible – especially when done as an exceptionally large scale regular practice.

III. Gross and Polowy Also Violated New York State Law Designed to Prevent Sloppy and Shoddy Legal Work in Foreclosure Cases

76. It appears that Gross and Polowy's failure to engage in reasonable due diligence violated two New York state statutes designed to curb frivolous litigation, especially in foreclosure cases. In 2010, New York State Chief Judge, Jonathan A. Lippman imposed an administrative order directing all attorneys filing foreclosure actions to file a certificate of merit stating that the attorney personally reviewed all documents and records relating to the case, communicated with a representative of the mortgagee, confirmed the accuracy statements made in all filed papers after diligent inquiry, and certified that the pleadings and all other documents filed in the case are complete and accurate in all relevant respects. The Chief Judge found this necessary because of numerous and widespread

insufficiencies and improprieties with foreclosure filings that were occurring regularly at that time.

77. In one particular Nassau County foreclosure case, the judge was especially UPSET at the mortgagee's counsel because not only did the pleadings contained numerous errors, but counsel utilized a number of computer generated statements that were inapplicable. In that case, Judge Fairgrieve stated:

> Willful carelessness of this sort will not be accepted. Also, substituting reasoned and considered statements for computer generated ones displaces the verifying attorney's responsibility to make even a cursory investigation into the truthfulness of the statements to which he swears.
>
> These sentiments are echoed by Chief Judge Jonathan Lippman of the New York State Court of Appeals in regard to the verity of foreclosure papers. Chief Judge Lippman said, "We feel we have an obligation to make sure the attorneys do their due diligence and come to us with credible papers because the consequences are so great." [Andrew Keshner, New Court Rule Says Attorneys Must Verify Foreclosure Papers, N.Y.L.J., October 21, 2010.] Chief Judge Lippman goes on to state, "I think this makes clear to everybody the court system's absolute commitment that we are not going to allow anything to interfere with the integrity of the court process." [Id.] According to New Court Rule Says Attorneys Must Verify Foreclosure Papers, "Attorneys must now certify, under penalties of perjury,' that they have communicated with . . . [the plaintiff] and that they have personally reviewed all documents and records related to the case." [Id.] The importance of these statements concerning foreclosure papers is analogous to their importance concerning any other documents presented to the court. It is imperative that these words are heeded.

Federal Home Loan Mtge. Corp. v Raia, 2010 NY Slip Op 52003(U) [29 Misc 3d 1226(A)] Decided on November 23, 2010 District Court Of Nassau County, First District. In this case, the court found mortgagee's counsel, Steven J. Baum, P.C., "must" be sanctioned for filing incorrect documents with the court.

78. The Baum law firm, which at that time was filing more than half of all foreclosure cases in this state, became notorious upon being besieged by numerous allegations that it engaged in improper and shoddy foreclosure work. The firm, which was the subject of a great number of criticisms in judicial opinions, folded after paying a $2 million fine to resolve a probe of its foreclosure practices. Interestingly, the law firm representing the Mortgagee in the instant case, Gross Polowy, was created by two senior attorneys from the Baum firm. *Foreclosure and 'Home Retention': a New Firm by Ex-Baum Lawyers*, The Wall Street Journal Law Blog, February 10, 2012 http://blogs.wsj.com/law/2012/02/10/foreclosure-and-home-retention-a-new-firm-by-ex-baum-lawyers/). Perhaps they did not learn their lesson about sloppy and shoddy legal work.

79. In 2013, the New York State Legislature promulgated Judge Lippman's administrative order into Section 3012-b of New York State Civil Practice Law and Rules, effectively making it state law, effective August 30, 2013, for plaintiffs commencing residential foreclosure actions to serve and file a certificate of merit.

80. Counsel for the Mortagee, Laura M. Strauss of Gross Polowy, prepared, served and filed a Certificate of Merit dated April 16, 2015 (Certificate of Merit) in which counsel indicates that she reviewed the facts of the case and pertinent documents, and consulted with a representative of the Plaintiff, namely Kathleen Manly who is Assistant Vice President – Servicing. A copy of the Certificate of Merit is attached hereto as "**Exhibit F"**.

81. Counsel further states in the Certificate of Merit: “Upon this review and consultation, to the best of my knowledge, information, and belief, I certify that there is a reasonable basis for the commencement of this action, and that Plaintiff is the creditor entitled to enforce rights under these documents.”

82. However, it appears that counsel either failed to take reasonable steps to verify the information contained in the complaint, or chose to ignore the bankruptcy filing information in her file. Thus, counsel either violated her duty as required by CPLR 3012-b to engage in reasonable due diligence, or worse, chose to ignore bankruptcy filing information that she already had.

83. On its website, Gross and Polowy states:

> Gross Polowy, LLC is comprised of attorneys and support staff that have extensive experience in foreclosure, mortgage servicing and home retention/loss mitigation in New York. The firm possesses the knowledge, expertise and integrity to operate successfully in the ever-changing legal world. Gross Polowy provides a firm that is: Exceptionally knowledgeable in the areas of foreclosure, litigation, bankruptcy, eviction and REO processes. [http://grosspolowy.com/aboutus/]

84. It is submitted that Gross and Polowy is a large-scale foreclosure firm – one of the largest in the state – and has substantial experience in not only foreclosure cases but bankruptcy cases as well. Accordingly, they should know better than to have taken lazy and sloppy shortcuts with the foreclosure legal process which are in violation of the order of discharge in those cases where the homeowner previously obtained a bankruptcy discharge.

IV. Remedies Debtor is Seeking

85. The remedies the Debtor is seeking for this egregious discharge violation are as follows. Gross Polowy should reimburse Debtor for out of pocket expenses that he has incurred. This involves the attorney's fees Debtor has incurred to have your affirmant's law firm review the foreclosure complaint and bring this motion. Judge Trust, in the *Haemmerle* case, determined that attorney's fees were warranted by a mortgagee that violated the discharge injunction. He noted that courts have awarded attorneys' fees when a party (1) willfully disobeys a court order, and (2) is found to have acted in bad faith, vexatiously, wantonly or for oppressive reasons. *Szenes*, 515 B.R. at 7; Nicholas, 457 B.R. at 225; *Nassoko*, 405 B.R. at 520; *Dabrowski*, 257 B.R. at 416; *Watkins*, 240 B.R. at 678. An award of attorneys' fees may also be warranted where an offending party not only willfully violated the discharge injunction but also acted in bad faith or in a vexatious or oppressive manner. See *Haemmerle at 17*, citing *Watkins v. Guardian Loan Co. of Massapequa, Inc.* (*In re Watkins),* 240 B.R. 668, 678 (Bankr. E.D.N.Y. 1999); *DiGeronimo*, 354 B.R. at 642 (Bankr. E.D.N.Y. 2006); *Russell v. Chase Bank USA, NA* (*In re Russell*), 378 B.R. 735, 743-744 (Bankr. E.D.N.Y. 2007).

86. Here, Gross Polowy willfully disobeyed the order of discharge and acted in bad faith as it should not have imposed a duty on the Debtor to raise the defense of bankruptcy in the foreclosure proceeding. Gross Polowy's conduct was willful because it had actual notice of the bankruptcy filing and discharge by virtue of the information that their client provided.

87. In addition, as previously indicated herein, Gross Polowy intentionally used a prayer for relief in which a reasonable person can only conclude will create tension, apprehension and anxiety upon the homeowner-defendant that maybe the bankruptcy process has not worked properly and that to prevent a deficiency judgment, legal defense counsel must be immediately retained. In addition, Gross Polowy not only used the offensive Bankruptcy Disclosure in the instant case, but in many hundreds of cases. By so doing, Gross Polowy acted in extreme bad faith.

88. Punitive damages are also warranted. Judge Trust, in the *Haemmerle* case, determined that punitive sanctions in the sum of $69,500 were warranted. *Haemmerle at 19*, citing *Szenes*, 515 B.R. at 7; *In re Velo Holdings Inc.*, 500 B.R. 693, 700 (Bankr. S.D.N.Y. 2013); *Nicholas*, 457 B.R. at 227; *DiGeronimo*, 354 B.R. at 644. In the instant case, Gross Polowy, in seeking a deficiency judgment with bankruptcy disclaimer language which had the effect of imposing a duty on the Debtor to defend, demonstrated utter disregard and disrespect of the bankruptcy laws. See *Haemmerle at 19*, citing *Szenes*, 515 B.R. at 7-8; *Nicholas*, 457 B.R. at 227; *Watkins*, 240 B.R. at 680 (finding punitive damages for violation of a discharge injunction also appropriate where there was malicious and egregious behavior).

89. As Judge Trust pointed out in *Haemmerle,* the cases in this area have not established a formulaic approach to determine how much in punitive sanctions should be assessed; rather, courts are called upon to exercise their discretion to

determine what punitive sanction is appropriate and reasonable. *Haemmerle at 20.*

90. It is respectfully submitted that Debtor is entitled to a punitive sanctions award against Gross Polowy for its egregious conduct here which should be in an amount to send a clear message that such conduct is not acceptable and is in violation of the discharge injunction. Again, Gross Polowy's conduct is not an isolated occurrence, but instead, a large scale regular practice involving hundreds of foreclosure cases at one of New York's largest foreclosure mills.

91. As this application includes references to case law and citations, it is respectfully requested that the Court waive the filing of any memorandum of law.

92. No prior application seeking the same or similar relief has been made other than the prior motion brought against the Mortgagee as discussed herein.

WHEREFORE, the Debtors respectfully request that this Court issue an Order, against Gross Polowy, granting attorney's fees and civil sanctions, and for such other and further relief as this Court deems just and proper.

Dated: Melville, New York
March 6, 2017

/s/ Craig D. Robins, Esq.
Craig D. Robins, Esq. (CR5938)
LAW OFFICES OF CRAIG D. ROBINS
Attorneys for the Debtor
35 Pinelawn Road, Suite 218-E
Melville, New York 11747
(516) 496-0800

SETTLEMENT AGREEMENT

This Agreement (the "**Agreement**") is made and entered into as of this 6th day of December, 2019 (the "**Effective Date**"), by and among Shonda Ramirez ("**Debtor**"), Craig D. Robins, Esq. ("**Robins**"), Blackened Investments I, LLC ("**Blackened**"), and The Margolin & Weinreb Law Group, LLP ("**Margolin & Weinreb**", and all of the foregoing may be referred to as, collectively, the "**Parties**," and any one of them as a "**Party**").

RECITALS

WHEREAS, the Parties recite the following for purposes of this Agreement:

A. On or about April 26, 2007, Debtor executed a mortgage in the amount of $360,000 in favor of Home Funds Direct ("**Mortgage**"), securing a note of the same date.

B. In 2009, the Mortgage was modified pursuant to a Home Affordable Modification Agreement modifying the principal balance to $384,954.29.

C. In 2011, the Mortgage was modified again pursuant to a second modification agreement (the "**2011 Modification Agreement**") modifying the principal balance to approximately $225,674.50. The 2011 Modification Agreement changed the interest rate on the unpaid balance of the loan to a flat rate of TWO and ONE-HALF (2.50 %) PERCENT. The 2011 Modification Agreement also provided for a principal balance reduction of approximately $143,824.79.

D. On July 29, 2013, the Debtor commenced a Chapter 13 case (the "**Bankruptcy Case**") in the United States Bankruptcy Court for the Eastern District of New York (the "**Court**") as Case No. 13-73929-ast via the filing of a petition and related schedules. Robins represented Debtor with the Bankruptcy Case.

E. On or about March 9, 2015, the Mortgage was assigned to Blackened.

F. On May 8, 2018, Blackened filed a motion seeking relief from the automatic stay alleging post-petition mortgage arrears of approximately $4,863.81. The Court granted that motion by issuing an order on June 29, 2018. Margolin & Weinreb represented Blackened with that motion.

G. On May 16, 2018, the Chapter 13 Trustee served Blackened with a Notice of Final Cure Payment pursuant to Bankruptcy Rule 3002.1 stating that Blackened shall file a response within 21 days. Blackened did not file a response.

H. On or about May 24, 2018, Debtor paid Blackened the approximate amount of arrears that it has alleged were due in its motion for relief.

I. On July 9, 2018, the Court granted Debtor a discharge.

J. Shortly after receiving the discharge, Blackened and/or its servicer(s) alleged that Debtor owed mortgage arrears of approximately $20,000 to $30,000.

K. On April 30, 2019, Blackened commenced a foreclosure proceeding in United States District Court for the Eastern District of New York as Case No. 19—cv-02526(ENV)(LB) ("**Foreclosure Proceeding**"). Debtor appeared in that proceeding by Robins on or about June 18, 2019. During the following months, Debtor advised Blackened that it had violated Bankruptcy Rule 3002.1. Blackened withdrew this proceeding without prejudice on October 03, 2019 by filing a notice of discontinuance. Margolin & Weinreb represented Blackened in the Foreclosure Proceeding.

L. From the time Debtor appeared in the Foreclosure Proceeding, Debtor asserted that Blackened and its attorneys engaged in violations of Bankruptcy Rule 3002.1 as well as other federal statutes including RESPA and FDCPA, and also alleged that they engaged in wrongful foreclosure. Debtor indicated her position to reopen the Bankruptcy Case and pursue remedies in the Court pursuant to Bankruptcy Rule 3002.1 and other statutes, as well as litigate other issues in federal court. Blackened and Margolin & Weinreb indicated their position that they did not engage in any such violations, or if they did, they were minimal and inconsequential.

M. During a period of several months, the Parties engaged in negotiations to resolve their differences in an effort to avoid extensive litigation. This has led to a settlement by the Parties as set forth in this Agreement.

N. Pursuant to the terms of this Agreement, the Parties have reached and settled all issues arising from or related to the Bankruptcy Case, the Foreclosure Proceeding, RESPA, FDCPA, and any other consumer protection statutes or claims Debtor had against Blackened and Margolin & Weinreb.

O. In general terms, the settlement seeks to incorporate the following: an acknowledgement that the terms of the 2011 Modification Agreement apply to the Mortgage; that Blackened will adjust its records to deem Debtor current with her monthly payments through September 30, 2019; that Blackened will compensate Debtor for emotional distress; that Blackened will compensate Debtor for her attorney's fees; and that generally Debtor will be made whole which also means that she is only responsible for making mortgage payments from October 1, 2019, and that her real estate tax liability is only for those months beginning October 1, 2019.

P. The Parties have reached this Agreement without any admission of fault or wrongdoing, or the merits of any claims or defenses asserted with respect thereto.

Q. The Parties hereby indicate that their addresses are as follows:

Shonda Ramirez
152 Herbert Avenue
Elmont, NY 11003

Craig D. Robins, Esq.
Law Offices of Craig D. Robins
35 Pinelawn Road, Suite 218-E
Melville, NY 11747
Phone: 516-496-0800

Blackened Investments I, LLC
8002 Bromley Street
Houston, TX 77005

The Margolin & Weinreb Law Group, LLP
165 Eileen Way, Suite 101
Syosset, NY 11791
Phone: 516-945-6055

NOW, THEREFORE, in consideration of the mutual covenants and considerations herein set forth, it is hereby stipulated and agreed by and among the Parties, as follows:

1. Settlement Payment. Blackened shall pay Debtor and Robins the following amounts, which, in total, shall constitute the "**Settlement Payment**" pursuant to the terms hereof. The Settlement Payment is $35,813.55 and includes the following components.

    a. Blackened shall pay the sum of $5,000 to the Debtor to compensate Debtor for any emotional injury that she may have incurred;

    b. Blackened shall pay Robins the sum of $27,500 for Debtor's attorney's fees;

    c. Blackened shall pay Debtor the sum of $3,313.55 representing the pro-rata share of unpaid real estate taxes, as well as the full amount of any late charges and penalties, as follows.

        i. The second half of the 2019 Town/County tax is $1,684.77, which was due on July 1, 2019, and covers the period July 1, 2019 through December 31, 2019. Blackened shall pay Debtor a pro-rata amount equal to three months (July, August and September) of this six month period, which is $842.39. In addition, Blackened shall pay Debtor the current late charge penalties, which, through December 2019, is approximately $110.00 penalty plus $94.00 interest plus $200.00 fees, for a total of $406.00.

        ii. The Second Half of the 2019/2020 School Tax is $3,430.32, which was due on October 1, 2019, and covers the period July 1, 2019 through December 31, 2019. Blackened shall pay Debtor a pro-rata amount equal to three months (July, August and September) of this six

month period, which is $1,715.16. In addition, Blackened shall pay Debtor the current late charge penalties, which, through December 2019, is approximately $80.00 penalty plus $70.00 interest plus $200.00 fees, for a total of $350.00.

2. Within 10 days of the execution of this Agreement, Blackened shall deliver the Settlement Payment by issuing a check payable as follows: "Craig D. Robins, as attorney" and Blackened shall deliver the check to the following address:

Craig D. Robins, Esq.
Law Offices of Craig D. Robins
35 Pinelawn Road, Suite 218-E
Melville, New York 11747

If the Settlement Payment is not delivered within ten days, or if it does not clear, then this Settlement Agreement shall become null and void.

3. Credit to Debtor of Monthly Mortgage Payments and Other Charges Through September 30, 2019. Blackened agrees to credit Debtor with all monthly mortgage payments and other charges due through September 30, 2019, whether Debtor paid them or not. Debtor's sole obligation to Blackened as of September 30, 2019 shall be the obligation to pay the Unpaid Principal Balance (as defined herein) pursuant to the terms of the 2011 Modification Agreement. Debtor shall have no liability to Blackened for any other sum, including monies Blackened previously claimed were due for real estate taxes, insurance payments, late charges, attorney's fees, or any other miscellaneous charge or expense.

4. Amount of Unpaid Principal Balance. The parties agree that the amount of the unpaid principal balance remaining on the mortgage as of September 30, 2019, which includes application of the September 1, 2019 monthly payment, is $168,566 (the "**Unpaid Principal Balance**"). The next monthly mortgage payment due is the October 2019 payment due October 1, 2019.

5. Resumption of Monthly Mortgage Payments and Amount. Debtor will resume making monthly mortgage payments to Blackened, by sending payments to its servicer, FCI Lender Services, commencing with the October 1, 2019 mortgage payment. The parties agree that each monthly mortgage payment, as set forth in the attached **Amortization Schedule**, is **$984.41**. Debtor will make any outstanding monthly mortgage payments due at the time this Agreement is fully executed (the monthly payments due October 1, 2019 and November 1, 2019), at the time she makes her December 1, 2019 mortgage payment. There shall be no late penalty for the October 1, 2019, November 1, 2019 and December 1, 2019 mortgage payments. Debtor shall send the mortgage payments to FCI Lender Services, whose address and contact information is as follows:

FCI Lender Services
8180 East Kaiser Blvd.
Anaheim Hills, CA 92808
Phone: (800) 931-2424 x 243

Fax: (714) 282-5775
Email contact: vdavis@trustfci.com

If Blackened's servicer, FCI Lender Services, or any subsequent servicer, offers its mortgagors/customers the ability to make monthly mortgage payments by phone or through automatic monthly debits or other means, Debtor shall be permitted to make monthly payments by the same methods. Debtor shall be entitled to obtain, upon request, a full payment history of this account, containing entries beginning September 30, 2019, every six months, at no charge. The payment history shall include the current pay-off amount. Such requests shall be fulfilled within 15 days.

6. Ratification of 2011 Modification Agreement. The parties hereby ratify the 2011 Modification Agreement and all of its terms. **A copy of the 2011 Modification Agreement is annexed hereto.**

7. Future Payments of Real Estate Taxes and Liability Insurance. Although the 2011 Modification Agreement requires Debtor to make monthly escrow payments to the mortgagee for real estate taxes and liability insurance, effective upon the date of this Settlement Agreement, Debtor shall instead directly pay all real estate taxes, on or prior to their due dates, and shall further maintain her liability insurance policy and directly pay all insurance premiums on or prior to their due dates. Accordingly, Blackened (or its servicer) shall have no obligation to maintain any escrow account related to this mortgage for the purpose of paying real estate taxes or liability insurance premiums. Debtor shall pay the outstanding real estate taxes as indicated above by December 31, 2019.

8. Amortization Schedule. **An amortization schedule showing the amount of principal and interest applied to each monthly payment, and the current monthly pay-off amount for each month, from the period of June 2011 through the remaining term of the mortgage ending May 2037, is annexed hereto.**

9. Advising Credit Reporting Bureaus. Blackened and Margolin & Weinreb agree to ensure that each of the three main credit reporting bureaus (Equifax, Experian and TransUnion) indicate on Debtor's credit report that Debtor's Mortgage is current and that it has been paid on time since July 2013. In addition, Blackened and Margolin & Weinreb agree to ensure that the credit reporting bureaus remove all references to the Foreclosure Proceeding, advising them that this suit was brought in error and was discontinued. Blackened and Margolin & Weinreb further agree to engage in such written communications with the credit reporting bureaus within 15 days of the date that this Agreement is fully executed, and further agree to provide carbon copies of all such correspondence to Robins, both sent and received. Blackened and Margolin & Weinreb agree to engage in any necessary additional communications or other work to achieve the above objectives, and agree to do so in an expeditious manner.

10. Debtor's and Robins's (the "**Releasors**") Release and Waiver of Claims against Blackened, and Margolin & Weinreb (the "**Releasees**"). Debtor and Robins, for good and valuable consideration, including the terms of this Agreement, and each of their past, present and future representatives, successors, heirs, executors, administrators, assigns and attorneys (the "**Releasors**"), hereby absolutely and irrevocably waive, release, discharge and acquit

Blackened and Margolin & Weinreb, as well as, to the extent applicable, its past, present and future partners, officers, directors, employees, agents, administrators, representatives, parents, subsidiaries, affiliates, attorneys, insurers, accountants, advisors and their respective heirs, successors and assigns (the "**Releasees**"), from any and all claims, demands, costs, contracts, liabilities, objections, actions and causes of action of any nature, whether in law or in equity, whether known or unknown, whether suspected or unsuspected, whether asserted or unasserted, which the Releasors ever had, now have, or may claim to have against the Releasees on account of or arising from or relating to the Bankruptcy Case or the Foreclosure Action or any other possible claim related to the Mortgage prior to the date of this Agreement.

11. Costs and Fees. Other than as indicated herein, each Party shall be responsible for its own attorneys' and other fees incurred to date in connection with this Agreement.

12. No Admission of Liability. The Parties acknowledge that this Agreement, its terms, or the negotiations connected with it will not be construed as an admission by any party of the truth or merits of any claims or defenses asserted in or related to or arising from the Bankruptcy Case, or the Foreclosure Proceeding, or of any liability, fault, or wrongdoing of any kind whatsoever, but rather reflects the desire of the Parties to resolve their differences amicably and without further expense.

13. Choice of Law. This Agreement shall be construed under the laws of the State of New York, without regard to the principles of conflicts of laws of such state. The Parties further agree that venue for any litigation brought to enforce this Agreement shall lie exclusively with the United States Bankruptcy Court for the Eastern District of New York or the United States District Court for the Eastern District of New York.

14. Representation by Counsel. Each Party hereto acknowledges that it has had the opportunity to consult with legal counsel of its choice prior to execution of this Agreement, has in fact done so, and has been specifically advised by counsel of the consequences of this Agreement and its respective rights and obligations hereunder. Each Party further acknowledges that the terms of this Agreement are the result of negotiations between all of the Parties and that this Agreement shall not be construed in favor of, or against any Party by reason of the extent to which a Party or its counsel participating in its drafting or by reason of the extent to which this Agreement may be inconsistent with prior drafts thereof.

15. Entire Agreement. This Agreement with the Stipulation constitutes the entire understanding of the Parties with respect to the subject matter hereof, and supersedes any prior agreements or understandings between the Parties oral or written, with respect to the subject matter hereof.

16. Good Faith Settlement. The Parties represent, warrant and acknowledge that this Agreement has been negotiated at arm's length and in good faith and that this Agreement constitutes a good faith settlement of all claims between them and acknowledge that it is entered into freely and voluntarily.

17. Effect of Waiver. No waiver of any of the provisions of this Agreement shall be deemed to constitute a waiver of any of the other provisions hereof whether or not similar, nor shall such waiver constitute a continuing waiver.

18. Counterparts and Signatures. This Agreement may be executed in counterparts, and so executed shall constitute but one and the same Agreement binding on all Parties. Photostatic, facsimile or .pdf format signatures of the original signatures of this Agreement, and photostatic, facsimile or .pdf format copies of this Agreement fully executed, shall be deemed originals for all purposes, and the parties hereto and/or beneficiaries hereof waive the "best evidence" rule or any similar law or rule in any proceeding in which this Agreement shall be presented as evidence or for enforcement.

19. Use of Headings. The use in this Agreement of paragraph headings is for convenience only and is not intended to limit or enlarge the rights of any Party.

20. Representations and Warranties. Each of the parties hereto represents and warrants to each other party hereto that: (a) such party has the power and authority as an entity, or the legal capacity as an individual, to enter into this Agreement and, to the extent applicable, perform its obligations hereunder, and, in the case of any party that is an entity, such party is duly organized and existing under the laws of its jurisdiction of organization; (b) no party has relied upon any representation or warranty not set forth herein; (c) such party has duly executed and delivered this Agreement; (d) in the case of any party that is an entity, the execution and delivery of this Agreement by such party and, to the extent applicable, the performance by such party of its obligations hereunder, have been duly authorized by all requisite action on the part of such party and its security holders (if any); (e) the execution and delivery of this Agreement by such party and, to the extent applicable, the performance by such party of its obligations hereunder, do not conflict with applicable law, or any contract by which such party or its property is bound or affected, or, in the case of any party that is an entity, the organizational documents of such entity; and (f) this Agreement is a legal and valid obligation of such party, enforceable against such party in accordance with its terms, except as such enforcement may be limited by bankruptcy, reorganization, or similar laws of general application or by general principals of equity.

21. Assignments, Transfers, and Conveyances. Each of the Parties represents and warrants that it has not assigned, transferred or conveyed, or purported to assign, transfer, or convey, voluntarily, involuntarily, or by operation of law, any claim, cause of action, or other matter released pursuant to this Agreement, or any part or portion thereof, to any person or entity.

22. Enforceability. If any phrase, clause or provision of this Agreement is declared to be illegal, invalid, unenforceable, unreasonable, onerous or unduly restrictive by a court of competent jurisdiction, this Agreement shall be deemed void *ab initio* and the parties shall have the remedy of rescission.

23. Modification, Amendment, Etc. Each and every modification and amendment of this Agreement shall be in writing and signed by all of the parties hereto, and each and every waiver

of, or consent to any departure from, any covenant, representation, warranty or other provision of this Agreement shall be in writing and signed by each party affected thereby.

24. Time of the Essence to Complete Agreement. This agreement shall become void unless it is not fully executed by Blackened and Margolin & Weinreb, and delivered to Robins by December 13, 2019.

IN WITNESS WHEREOF, the parties hereto have affixed, or caused to be affixed, their respective signatures, effective on the day and year first above written.

THE MARGOLIN & WEINREB LAW GROUP, LLP

By:_____
Name: Alan Weinreb
Title: Partner

STATE OF NEW YORK)
) ss.
COUNTY OF NASSAU)

On the 13 day of December 2019, before me personally came **ALAN WEINREB** to me known, who being by me duly sworn, did depose and say that he is the individual described in and who also executed the foregoing instrument in his capacity as an authorized person on behalf of the entity identified above which bears his signature.

TIFFANY LAJUNE HENRY
Notary Public, State of New York
No. 02HE6307370
Qualified in Nassau County
Commission Expires 07/07/2021

Notary Public

Blackened Investments I, LLC

By: _____
Name: Donald Black
Title: Member

STATE OF TX)
) ss.
COUNTY OF Harris)

On the 9th day of December 2019, before me personally came **Donald Black** to me known, or upon producing proof of identification in the form of TX Driver's License, who being by me duly sworn, did depose and say that he is the individual described in and who also executed the foregoing instrument in his capacity as a member, an authorized person on behalf of **Blackened Investments I, LLC.**

VAN T PHAM
Notary ID #12308210
My Commission Expires
June 26, 2023

_____
Notary Public

CRAIG D. ROBINS, ESQ.

STATE OF NEW YORK)
) ss.
COUNTY OF SUFFOLK)

On the 9th day of December 2019, before me personally came **CRAIG D. ROBINS, ESQ.** to me known, who being by me duly sworn, did depose and say that he is the individual described in and who also executed the foregoing instrument.

Notary Public

MARC W. DANIELS
Notary Public, State of New York
No. 01DA6148719
Qualified in Suffolk County
Commission Expires June 26, 20 22

SHONDA RAMIREZ

STATE OF NEW YORK)
) ss.
COUNTY OF SUFFOLK)

On the 9th day of December 2019, before me personally came **SHONDA RAMIREZ** to me known, who being by me duly sworn, did depose and say that she is the individual described in and who also executed the foregoing instrument.

Notary Public

CRAIG DENNISON ROBINS
STATE OF NEW YORK
NOTARY PUBLIC
Qualified in Nassau County
02RO6338782
MY COMMISSION EXPIRES 03/21/2020

UNITED STATES DISTRICT COURT

DISTRICT OF NEVADA

* * *

LESLIE J. SHAW, Plaintiff, v. CITIMORTGAGE, INC.; *et al.*, Defendants.	)	3:13-CV-0445-LRH-VPC ORDER

This is a breach of contract action arising from an alleged residential loan modification agreement between plaintiff Leslie J. Shaw ("Shaw") and defendant CitiMortgage, Inc. ("CMI"). Shaw alleges that in mid-2011, the parties executed a loan modification agreement on his residential home loan, but CMI breached the agreement prompting Shaw to stop making payments on his modified loan. Shaw then fell into default and CMI initiated non-judicial foreclosure proceedings in early 2013.

On July 26, 2013, Shaw filed a complaint against CMI and defendant Northwest Trustee Services, Inc. ("NTS"), the trustee identified on the recorded notice of default. ECF No. 1, Exhibit A, p. 8-19. On April 3, 2014, Shaw filed an amended complaint adding defendant Bank of New York Mellon ("BNY"), as trustee for SASCO Fund 2003-37A, as a defendant to this action. ECF No. 52. Subsequently, on August 25, 2014, Shaw filed a second amended complaint against defendants alleging eight causes of action: (1) declaratory relief against defendant BNY; (2) declaratory relief against defendant CMI; (3) breach of contract; (4) breach of the implied covenants of good faith and fair dealing; (5) fraudulent misrepresentation and concealment;

(6) negligent misrepresentation; (7) interference with prospective economic advantage; and (8) violation of the Real Estate Settlement Procedures Act ("RESPA"). ECF No. 109.

On January 14, 2015, the court granted defendant NTS' motion to dismiss (ECF No. 110) and dismissed NTS as a defendant in this action. ECF No. 124. Three weeks later, on February 5, 2015, the court granted defendants BNY and CMI's motion to dismiss (ECF No. 113). ECF No. 128. In that order, the court dismissed BNY as a defendant and dismissed Shaw's fifth cause of action for fraudulent misrepresentation and sixth cause of action for negligent misrepresentation. *Id*.

A bench trial was held on Shaw's remaining claims[1] against sole-remaining defendant CMI from May 3 through May 5, 2016. *See* ECF Nos. 203-05. The court, having heard the testimony of all witnesses at trial[2] and having considered all exhibits accepted into evidence, renders the following findings of fact and conclusions of law:[3]

I. Findings of Fact

1. Plaintiff Shaw is a resident of the State of Nevada. Shaw is also an attorney duly licensed to practice law in the States of Nevada and California. Shaw practices primarily in the areas of family and divorce law and during the relevant time period had a practice at Lake Tahoe that moved to Reno, Nevada.

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[1] Shaw's remaining claims are his second cause of action for declaratory relief, third cause of action for breach of contract, fourth cause of action for breach of the implied covenants of good faith and fair dealing, seventh cause of action for interference with prospective economic advantage, and eighth cause of action for violation of RESPA.

[2] At trial the court heard the live testimony of plaintiff Leslie Shaw; Attorney Colt Dodrill, counsel of record for defendant CMI; Jill Hackman, business operations analyst and corporate representative of CMI; Dan Leck, Shaw's real estate expert; and Michael Brunson, CMI's real estate expert. The court also heard the testimony by deposition of Travis Nurse, CMI's designated Rule 30(b)(6) witness; Christopher Gabbert, a CMI employee in the Executive Response Unit; Attorney Dana Ross, Assistant General Counsel for CMI; Katherine Barkley, junior lien holder; and Janice Shaw, Shaw's ex-wife and junior lien holder.

[3] If any finding of fact herein is considered to be a conclusion of law, or any conclusion of law is considered to be a finding of fact, it is the court's intention that it be so considered.

2. In 2001, Shaw purchased a vacant lot located in Zephyr Cove, Nevada, and built a single-family residence commonly known as 251 McFaul Court ("the McFaul Court property"), the underlying residential property at issue in this action.

3. On October 8, 2003, Shaw executed a promissory note for a residential home loan on the McFaul Court property in favor of non-party Lehman Brothers Bank, FSB ("Lehman Brothers"), a federal savings bank, in the amount of $875,000.00 with an adjustable interest rate starting at 5.125%. The residential loan was secured by a first deed of trust recorded against the McFaul Court property on October 14, 2003, in the official records of Douglas County, Nevada (Doc. No. 0593479). Def. Trial Ex. 501-B, CMI000001-22.

4. Immediately following the execution of the residential home loan, non-party Aurora Loan Services ("Aurora"), a servicing branch of Lehman Brothers, began servicing Shaw's residential loan and accepted all mortgage payments on behalf of non-party Lehman Brothers. In June 2005, Aurora ceased servicing the loan and transferred the servicing rights to CMI.

5. At some point prior to the relevant time period, Lehman Brothers sold Shaw's residential home loan as part of an investment mortgage package to an unknown party.

6. Defendant CMI, a foreign corporation duly qualified to conduct business in the State of Nevada, is a mortgage servicing company. CMI is owned by non-party CitiBank and is part of the Citi Group corporate organization. Since June 2005, CMI has been servicing Shaw's residential home loan and has collected all payments on behalf of the various owners of the loan. On June 20, 2012, CMI became the beneficiary under the first deed of trust pursuant to an assignment of deed of trust recorded in the official records of Douglas County, Nevada (Doc. No. 0804389). Def. Trial Ex. 504-B, CMI000038-39.

7. Each mortgage account serviced by CMI is assigned an electronic account file. The electronic account file, identified by a specific numerical identifier (the mortgage account number), is accessible to CMI employees and contains information about each particular

account including payment information, loan terms, account notes, and other relevant account information. As part of its servicing of Shaw's residential home loan, CMI maintained such an electronic account file for Shaw's loan. It is in this electronic account that CMI booked the terms of Shaw's residential loan and all payments made under that agreement.

8. In August 2006, Shaw and his then wife, non-party Janice Shaw, separated. As part of their eventual divorce - as evidenced by the divorce decree issued in July 2007 - Shaw was awarded the McFaul Court property as his sole and separate property.

9. On or about January 19, 2007, Shaw obtained a loan from non-party Katherine Barkley in the amount of $225,000.00 at an annual interest rate of 10%. This loan was secured by a second deed of trust recorded against the McFaul Court property on January 23, 2007, in the official records of Douglas County, Nevada (Doc. No. 0693296). Def. Trial Ex. 502-B, CMI000023-27.

10. On September 20, 2007, a third deed of trust was recorded in the amount of $77,123.50 against the McFaul Court property in favor of non-party Janice Shaw, Shaw's ex-wife, in the official records of Douglas County, Nevada (Doc. No. 0709512). Def. Trial Ex. 503-B, CMI000028-37.

11. In 2010, Shaw began experiencing financial difficulties. On or about the fall of 2010, while still current on his monthly mortgage payments, Shaw contacted CMI to request a modification of his residential mortgage loan. At that time, Shaw's monthly mortgage obligation was approximately $4,300.00.

12. During the relevant time period, CMI had a company policy that it would not consider any application for the modification of an existing loan unless a borrower was at least three (3) months in arrears on the borrower's monthly mortgage obligations. This policy was communicated to Shaw during one of the telephonic conversations in the fall of 2010.

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13. Beginning October 2010, and continuing through December 2010, Shaw withheld his monthly mortgage payments from CMI. Def. Trial Ex. 510-B, CMI000067. Shaw then contacted CMI and received a loan modification application. Shaw completed and submitted the application to CMI in early December 2010.

14. CMI reported Shaw's mortgage account as delinquent to the various credit reporting agencies for the months that Shaw withheld payment on his account: October, November, and December 2010.

15. At the time he submitted his loan modification application Shaw had never, in memory, been denied an application for credit and was current on all credit obligations except for his mortgage account.

16. On December 24, 2010, Shaw received an e-mail from CMI. Pl. Trial Ex. 1, P00001. The e-mail advised Shaw that his "mortgage assistance request [had] been approved" and he could expect a "mortgage solution package within the next 5-7 business days." *Id*.

17. On December 28, 2010, four days after receiving CMI's approval e-mail, Shaw received a letter from CMI denying his request for a loan modification. Pl. Trial Ex. 2, P00002-5. The letter specifically stated that CMI could not "approve a mortgage modification under the government's Home Affordable Modification Program ("HAMP")" and that Shaw's "mortgage terms [would] remain unchanged." *Id*. at P00002. At the time Shaw received this letter from CMI, he had not applied for a specific HAMP loan modification. Rather, Shaw had only applied for a general loan modification with defendant CMI.[4]

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[4] During the relevant time period, CMI had a policy that when a borrower submitted a completed loan modification application, Loss Mitigation would review the application for all available modification options - from company modification options to government supported modification programs like HAMP. However, it was not CMI's policy to advise or disclose to applicants that an application would be reviewed by Loss Mitigation for all possible modification options including government programs. Nor was it CMI's policy to advise or disclose to applicants that they may receive several responses from CMI concerning the outcome of an application and that such responses could differ in whether an application was approved or denied.

In accordance with CMI's policies, Loss Mitigation reviewed Shaw's application and determined, through an underwriter, that Shaw was eligible for a modification of his existing residential loan but was

18. Commencing on or about December 28, 2010, and continuing through February 2011, Shaw began near daily telephonic efforts with CMI to resolve the inconsistent and contradictory written communications of December 24 and December 28, 2010. Despite repeated phone calls with CMI employees in various departments, including Loss Mitigation, Shaw never received an explanation as to why he received two separate communications from CMI about his loan modification application, or why he had been denied a modification after already receiving notification that his application had been approved.[5] Further, Shaw did not receive an answer from CMI as to which of the two communications constituted CMI's final determination of his loan modification application.

19. Shaw did not make either of his monthly mortgage payments for January or February 2011. Def. Trial Ex. 510-B, CMI000067. Subsequently, CMI reported Shaw's mortgage account as delinquent to the various credit reporting agencies for those months.

20. Between December 28, 2010, and early February 2011, Shaw did not receive any written communication from CMI concerning his loan modification application.

21. On February 15, 2011, Shaw received another e-mail from CMI. Pl. Trial Ex. 3, P00006. This e-mail again advised Shaw that his "mortgage assistance request [had] been approved" and that he could expect a "mortgage solution package within the next 5-7 business days." *Id*.

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ineligible for a HAMP modification. But Shaw was never advised that his application would be considered for all available modification options, that he would receive multiple responses from CMI about his application, that those responses could be contradictory (as they were in this case), and which of those responses would constitute CMI's final determination of his application.

[5] At trial, it was explained for the first time that Shaw had received a separate response on his loan modification application relating specifically to the government's HAMP program because any denial of a modification under HAMP must be directly communicated to the buyer and contain the reasons for the denial along with information related to other loan modification programs and credit counseling. This simple explanation was never provided to Shaw throughout the history of this action.

22. On or about February 16, 2011, after receiving CMI's second approval e-mail, Shaw received another letter from CMI again denying his request for a loan modification. Pl. Trial Ex. 4, P00007-10. The letter specifically stated that CMI could not "approve a mortgage modification under the government's Home Affordable Modification Program ("HAMP")" and that Shaw's "mortgage terms [would] remain unchanged." *Id*. at P00007.

23. Commencing February 16, 2011, Shaw again contacted CMI to resolve the inconsistent and contradictory written communications concerning his loan modification application. Despite repeated calls with CMI employees, Shaw never received an explanation why he had received new communications regarding his application,[6] or why he had once again been denied mortgage assistance after receiving notification that his loan modification application had been approved. Further, Shaw did not receive an answer from CMI as to which of the four communications constituted CMI's final determination of his loan modification application.

24. On or about February 23, 2011, Shaw received a mortgage solution package from CMI. Def. Trial Ex. 505-A, CMI000051-56. The mortgage solution package advised Shaw that he had been "approved to enter into a trial period plan" modifying his residential loan for a period of ninety (90) days. *Id*. at CMI000051. The package further advised Shaw that in order to qualify for a permanent modification, Shaw must comply with two requirements. First, Shaw was required to timely make three modified monthly mortgage payments of

[6] At trial, it was explained that Shaw had received two separate sets of written communications, first in December 2010 and then again in February 2011, because of the amount of principal remaining on his residential loan. In December 2010, an underwriter for CMI approved Shaw for a modification of his existing loan obligations. Based on that decision, the first set of communications was sent to Shaw in December 2010.

However, because Shaw's remaining principal obligation was substantial (over $800,000), the original underwriter did not have final authority on Shaw's application and a manager-level underwriter had to separately review Shaw's application and make a final determination on whether to approve or deny the application. Upon review, this manager-level underwriter approved Shaw's application and another set of communications was sent to Shaw in February 2011. Once again, this simple explanation was never provided to Shaw throughout the history of this action.

$3,079.30 starting March 2011. *Id*. Second, Shaw was required to submit various documents to CMI. *Id*. If Shaw complied with both requirements, CMI advised Shaw that his residential home loan would be "permanently modified" and it would send him "a modification agreement detailing the terms of the modified loan." *Id*. at CMI000052.

25. Shaw timely made all three required trial payments of $3,079.30 under the trial period plan for the months of March, April, and May 2011. Def. Trial Ex. 510-B, CMI000067.

26. CMI reported Shaw delinquent on his mortgage account to the various credit reporting agencies for the months of March, April, and May 2011, despite granting Shaw a trial modification plan and having received all three modified payments in a timely manner. By this time, Shaw had been reported delinquent on his mortgage account for eight months.

27. During the time period after submitting his loan modification application through the time of the trial modification plan, Shaw received various collection calls from CMI seeking payment on his delinquent account. Approximately April 2011, Shaw registered for CMI's no-call list, thereby precluding CMI from initiating telephonic contact with Shaw. Since that time, Shaw has received no telephonic attempts to collect on his mortgage account.

28. On May 11, 2011, having submitted all trial plan payments, Shaw received an e-mail from CMI advising him that his "mortgage assistance documents [had] been sent" the previous day, May 10, 2011. Pl. Trial Ex. 5, P00011. The e-mail further directed Shaw to "review and sign the documents as instructed." *Id*.

29. On May 18, 2011, Shaw received a letter from CMI authored by CMI employee Kim Vukovich ("Vukovich"). Pl. Trial Ex. 6, P00014-20. The letter advised Shaw that he was "eligible for a Citi Affordable Modification" and directed him to complete and return the enclosed modification agreement (also prepared by Vukovich) no later than May 20, 2011. *Id*. at P00014. The enclosed proposed modification agreement, titled "Citi Affordable Modification Agreement" ("May 2011 Modification Agreement"), outlined

the various terms of the proposed loan modification. *Id*. at P00016-20. Those terms included, in relevant part to this action, that: (1) permanent modified payments in the amount of $3,079.30[7] would commence starting June 1, 2011; (2) the new principal balance under the modified loan would be set at $910,110.34 and include all past due amounts, including the difference between the original monthly payment amount (approximately $4,300) and the payment amount made under the three months of the trial modification plan ($3,079.30); (3) $85,777.89 of the new principal balance was deferred from interest charges during the life of the modification and would be due as a balloon payment; (4) the effective date of the properly executed agreement would be May 1, 2011; and (5) the maturity date under the modified loan would be November 1, 2033. *Id.*

30. Also on May 18, 2011, Shaw promptly executed, by notarized signature, the May 2011 Modification Agreement and submitted the signed agreement to CMI via an enclosed Next Day Air envelope. Pl. Trial Ex. 6, P00013; Def. Trial Ex. 506-A, CMI000061.

31. On May 19, 2011, CMI received the executed May 2011 Modification Agreement. Pl. Trial Ex. 7, P00021.

32. On May 23, 2011, CMI entered and booked the terms of the May 2011 Modification Agreement into Shaw's electronic mortgage account. Def. Trial Ex. 510-B, CMI000066. At the time CMI booked the terms of the modification, CMI misentered the length of the loan, extending the loan from three hundred and sixty (360) months to four hundred and eighty (480) months. *Id*. This administrative booking error extended the loan maturity date and subsequent due date of the $85,777.89 balloon payment from November 1, 2033, to November 1, 2045.

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[7] The proposed modification agreement contained a staggered payment and interest rate schedule that increased the monthly payment on Shaw's modified loan over the course of several years. *See* Pl. Trial Ex. 6, P000018. However, for purposes of this order and the relevant time period, Shaw's modified payment was $3,079.30. *Id*.

33. Shaw timely made his modified mortgage payments of $3,079.30 for the months of June and July 2011. Def. Trial Ex. 510-B, CMI000066.

34. On June 30, 2011, Larry Bauman, Vice-President for CMI, executed, by notarized signature, the May 2011 Modification Agreement. Def. Trial Ex. 506-A, CMI000061; Pl. Trial Ex. 18, P00055-56.

35. From May 20, 2011, through mid-July 2011, Shaw did not receive any communication from CMI concerning the May 2011 Modification Agreement and was not informed that the agreement had been executed by CMI.

36. Prior to July 2011, Shaw maintained, in good standing, a Diners Club Charge Card credit account and had sufficient credit to qualify as a cosigner on his daughter's student loans obtained through non-party Wells Fargo Bank. At that time, Shaw was also at the tail end of a thirty-six (36) month lease agreement with non-party Audi Financial Services on a 2008 Audi A-4 automobile.

37. Approximately early-July 2011, Loss Mitigation reviewed Shaw's mortgage account and unilaterally determined that there was an issue with the modified terms of his residential loan booked pursuant to the May 2011 Modification Agreement documents. Loss Mitigation then, without consultation or communication with Shaw, unbooked the May 2011 Modification Agreement from Shaw's electronic mortgage account. Def. Trial Ex. 510-B, CMI000065-66. This action automatically unbooked Shaw's timely made modified mortgage payments under both the trial and permanent modification periods, and placed his account in default. *Id.* As Shaw's account then showed that no payment had been made on his account for the months of June and July 2011, CMI reported Shaw's account as delinquent to the various credit reporting agencies for those months.

38. On July 15, 2011, non-party BMO Financial Group sent Shaw a letter advising him that his Diners Club Charge Card account, a credit account with Citicorp Credit Services, Inc., was going to be closed effective July 20, 2011. Pl. Trial Ex. 50, P00022.

39. On July 16, 2011, non-party U.S. Bank, National Association sent Shaw a letter advising him that his credit application for an auto loan to purchase his leased 2008 Audi A-4 automobile had been denied. Pl. Trial Ex. 51, P00023.

40. On July 18, 2011, CMI sent Shaw a letter advising him that his mortgage account was in default and that monthly mortgage payments had not been made as required under his residential home loan. Pl. Trial Ex. 10, P00035-36. In that letter, CMI further demanded Shaw pay, in full, the past due amount of $31,684.34 by August 18, 2011, or the McFaul Court property could be sold in accordance with the terms of the first deed of trust. *Id*. at P00035.

41. On July 19, 2011, CMI sent Shaw a letter authored by CMI employee Juan Mayorga ("Mayorga").[8] Pl. Trial Ex. 9, P00025-33. This letter again advised Shaw that he was "eligible for a Citi Affordable Modification" and directed him to complete and return the new "corrected" modification agreement (separately prepared by Mayorga) no later than August 2, 2011. *Id*. at P00025. The enclosed "corrected" modification agreement, again titled "Citi Affordable Modification Agreement" ("July 2011 Modification Agreement"), outlined the various terms and provisions of the new agreement. *Id*. at P00027-33. The majority of the terms in the July 2011 Modification Agreement were similar, or even identical, to the terms and provisions of the May 2011 Modification Agreement, including that: (1) permanent modified payments of $3,079.30 would commence starting June 1, 2011;[9] (2) the modified principal balance was set at $910,110.34; (3) $85,777.89 of the principal balance was deferred from interest charges and would be due as a balloon

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[8] No mention was made during the course of trial as to why Mayorga had been assigned to Shaw's account to draft the "corrected" modification agreement or what happened to Vukovich during that two month period.

[9] This June 1, 2011 date was still established as the first due date for modified payments even though the July 2011 Modification Agreement was not drafted until some time in July 2011, and sent to Shaw on July 19, 2011.

payment; (4) the effective date of the properly executed agreement would be May 1, 2011; and (5) the maturity date under the modified residential loan would be November 1, 2033. *Id*. However, the July 2011 Modification Agreement also included specific language establishing the due date of the deferred principal balloon payment that was not in the May 2011 Modification Agreement. *Compare* Pl. Trial Ex. 6 at P00018 (no date) *with* Pl. Trial Ex. 9 at P00028 (establishing the maturity date of the modified loan (November 1, 2033) as the due date). Further, the "corrected" agreement contained several additional provisions that were not in the May 2011 Modification Agreement, including Section 5(G). *Id*. at P00032. Section 5(G) required, in pertinent part, that under the July 2011 Modification Agreement Shaw would be required to execute any and all other documents requested by CMI or forfeit all his rights under the modified agreement. *Id*. ("If I elect not to sign any such corrected documentation, the terms of the original Loan Documents shall continue in full force and effect, such terms will not be modified by this Agreement, and I will not be eligible for a modification . . . .").

42. On July 20, 2011, Shaw received an e-mail from CMI advising him that "mortgage assistance documents" had been sent on July 19, 2011. Pl. Trial Ex. 8, P00024. The communication further directed Shaw to "review and sign the documents as instructed." *Id*. On the same day, Shaw received CMI's communications dated July 18 and July 19, 2011. Shaw immediately contacted CMI, including a conversation with Mayorga, but was never provided an explanation why his mortgage account was placed in default, or why a new modification agreement had been sent only two months after he executed and submitted the May 2011 Modification Agreement. Instead, Shaw was directed to review and sign the July 2011 Modification Agreement.[10]

[10] At trial, it was established that the May 2011 Modification Agreement was missing language in the balloon payment provision setting a specific due date for the balloon payment, although the agreement contained the correct loan maturity date of November 1, 2033. Thus, when CMI received the executed

43. On July 21, 2011, Shaw sent a letter to Mayorga objecting to CMI's handling of his mortgage account, including CMI's unilateral decision to unbook the May 2011 Modification Agreement and place his mortgage account in default, as well as the additional material terms in the July 2011 Modification Agreement not present in the May 2011 Modification Agreement. Pl. Trial Ex. 13, P00040.

44. Shaw did not execute the July 2011 Modification Agreement.

45. On July 22, 2011, Shaw received a letter from CMI dated July 20, 2011, advising him that CMI had reviewed his loan modification application and could not approve a modification at that time. Pl. Trial Ex. 11, P00037-38. CMI sent the letter to Shaw even though it had already executed the May 2011 Modification Agreement and sent the separate July 2011 Modification Agreement.

46. Also on July 22, 2011, Shaw received an e-mail from CMI advising Shaw that his "mortgage assistance documents [had] been received by [CMI.]" Pl. Trial Ex. 12, P00039. However, Shaw had not submitted any mortgage assistance documents to CMI and had refused to execute the July 2011 Modification Agreement.

47. Commencing late July 2011, Shaw again contacted CMI to resolve the inconsistent and contradictory communications received during the previous weeks including why he had received a loan modification denial letter after having just received the July 2011 Modification Agreement. Once again, Shaw did not receive any explanation from CMI for these contradictory communications.

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agreement and booked the modification terms into Shaw's electronic mortgage account, CMI mistakenly entered a 480 month term for the balloon payment, thereby extending Shaw's loan past the maturity date. When Loss Mitigation audited Shaw's mortgage account in July 2011, it determined that a "corrected" modification agreement should be sent to Shaw containing a specific due date for the balloon payment, that of the maturity date of November 1, 2033. This "corrected" agreement was sent to Shaw in order to correct CMI's own mistake. However, no explanation was ever provided at trial as to why the July 2011 Modification Agreement, if all it was supposed to do was correct the balloon payment language error, contained additional material terms like Section 5(G), which placed additional duties and obligations on Shaw.

48. Approximately July 2011, in response to Shaw's near daily communications with CMI, CMI deemed Shaw's mortgage account an Escalated Case and turned his account over to the Executive Response Unit, a CMI department dedicated to addressing customer account issues. Shaw's account was placed with Chris Gabbert ("Gabbert"), a Homeowner Support Specialist in the Executive Response Unit. Shaw contacted Gabbert to outline and discuss his ongoing mortgage and modification issues. At that time, Gabbert advised Shaw that the July 2011 Modification Agreement was the only modification agreement that CMI would accept, directed him to execute the agreement, and informed him that there was not a prior modification of his residential loan under the May 2011 Modification Agreement.

49. As a result of CMI's repeated inconsistent communications and complete lack of any explanation for CMI's conduct in handling his mortgage account and loan modification, Shaw experienced increasing confusion, frustration, stress, and a general feeling of worthlessness over not being able to resolve his issues with CMI. This frustration and stress caused Shaw to suffer occasional sleeplessness during this time. Further, Shaw spent significant amounts of time and energy, sometimes as much as eight (8) hours in a single day, contacting CMI and dealing with various CMI employees that were unable to address his concerns or help with his mortgage and modification issues.

50. Due to Shaw's ongoing frustration in dealing with CMI, Shaw sought the identity of the owner/beneficiary of his loan in the hopes of resolving his problems directly with the loan's owner.

51. Between July 25 and July 28, 2011, Shaw contacted Gabbert several times. In those telephonic conversations, Shaw requested information about the current owner of his loan. Gabbert advised Shaw that the current owner of his loan was Lehman Brothers through Structured Asset Security Corporation ("SASCO") Mortgage Pass-Through Certificates.

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52. On July 31, 2011, Shaw again e-mailed Gabbert. Pl. Trial Ex. 15, P00044-45. In that e-mail, Shaw specifically requested information related to the owner of his loan, as Shaw had determined on his own that Lehman Brothers had previously gone bankrupt and the SASCO Mortgage Pass-Through Certificates that included his residential loan had been transferred to a new, unknown owner. *Id*.

53. Shaw requested contact information for the current owner of his loan in order to seek a modification directly from the owner and to make sure that he was receiving credit from the owner for payments made on the mortgage.

54. Shaw timely made a modified mortgage payment in the amount of $3,079.30 for the month of August 2011. Def. Trial Ex. 510-B, CMI000065. CMI did not book Shaw's payment into his electronic mortgage account.

55. Approximately August 2011, Shaw applied for and was denied credit with non-party Audi Financial Services to purchase his Audi automobile which he had been leasing from Audi for approximately four (4) years.

56. On August 2, 2011, CMI sent Shaw another letter again advising Shaw that his mortgage account was in default and demanded Shaw pay, in full, the past due amount of $31,697.84 by September 2, 2011, or the McFaul Court property could be sold in accordance with the terms of the first deed of trust. Pl. Trial Ex. 16, P00046-47.

57. On August 9, 2011, CMI sent Shaw a letter from the Document Processing Modification Unit that included a copy of the completed and executed May 2011 Modification Agreement signed by CMI Vice-President Bauman. Pl. Trial Ex. 18, P00049-56. The letter advised Shaw that the copy of the agreement executed by both parties was solely for his records and that "no further action [was] necessary." *Id*.

58. Upon receiving his copy of the executed May 2011 Modification Agreement, Shaw immediately contacted Gabbert who initiated the involvement of Dana Ross ("Ross"), Assistant General Counsel of CMI, to resolve Shaw's mortgage account and loan

modification.

59. On August 12, 2011, after reviewing Shaw's account and the May 2011 Modification Agreement, Ross advised Shaw that he would be receiving a letter outlining CMI's resolution of Shaw's mortgage account and loan modification. Pl. Trial Ex. 22, P00061.

60. On August 15, CMI rebooked the terms of the May 2011 Modification Agreement into Shaw's electronic mortgage account. Def. Trial Ex. 510-B, CMI000064. As of that date, Shaw's account reflected all of the modification terms outlined in the May 2011 Modification Agreement, including principal amount, deferred principal amount, and modified payment amounts. *See* Pl. Trial Ex. 19, P00057-58. CMI also rebooked all payments Shaw made under the trial period plan and the May 2011 Modification Agreement to date. These actions brought Shaw's mortgage account current and removed his account from default.

61. On August 23, 2011, Ross sent Shaw an e-mail advising him that CMI had resolved the issues on his account and directed him to access a document on his online mortgage account constituting CMI's resolution. Pl. Trial Ex. 20, P00059. The aforementioned document was a letter signed by Gabbert explaining the actions CMI took on Shaw's mortgage account in July 2011, and outlining CMI's resolution of his account and modification. Pl. Trial Ex. 21, P00060. The resolution document advised Shaw that although the May 2011 Modification Agreement did not have clear balloon payment language (as no due date was specifically mentioned in that provision), the agreement correctly identified the appropriate maturity date for the loan (November 1, 2033), and thus, "there [was] nothing legally deficient with the [May 2011 Modification Agreement.]" *Id*. Further, the resolution document advised Shaw that CMI had already rebooked the May 2011 Modification Agreement and that his account was permanently modified under that agreement going forward. *Id*.

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62. Shaw believed that he had a binding loan modification with CMI and that all his account issues had been resolved. Thereafter, Shaw timely made all modified monthly payments of $3,079.30 pursuant to the May 2011 Modification Agreement through December 2011. Def. Trial Ex. 510-B, CMI000063-64.

63. Beginning in September and continuing through December 2011, Shaw received sporadic written collection notices from CMI that consisted of formal collection notices and informal door hangers left in plain view at the McFaul Court property, demanding payment on past due amounts. Whenever he received a collection notice, Shaw contacted the telephone number on that notice. However, Shaw was repeatedly told by various CMI employees that because Shaw's account had been transferred to the Executive Response Unit, only his dedicated Homeowner Support Specialist was allowed to deal with, discuss, and handle his account issues. Shaw would then contact and advise Gabbert that he was still receiving collection notices from CMI despite the rebooking of the May 2011 Modification Agreement and the inclusion of all past due amounts into his new principal balance.

64. Sometime in the fall of 2011, Shaw applied for and was denied credit as a cosigner on his daughter's student loans through non-party Wells Fargo Bank for the 2011-12 school year.

65. Throughout the fall of 2011, Shaw repeatedly sought the identity and contact information for the owner of his residential home loan from CMI. Shaw's efforts consisted of various telephonic and written requests to Gabbert. In response to these requests, Gabbert advised Shaw of different owners at different times. Lehman Brothers through SASCO Mortgage Pass-Through Certificates was identified, non-party Aurora Loan Services was identified, and even CMI itself was identified as the owner.

66. On December 5, 2011, Shaw attempted to e-mail Gabbert requesting specific information about his loan - including copies of the original note, deed of trust, and any assignment of rights - as well as contact information for the current owner of his loan as Shaw had

previously received such inconsistent information about the owner from CMI. *See* Def. Trial Ex. 512-A. At that time, Shaw was informed that Gabbert was no longer employed with CMI. Shaw then forwarded the email directly to Ross, CMI's Assistant General Counsel. Def. Trial Ex. 512-A.

67. On December 8, 2011, CMI sent Shaw a letter advising him that his account had been transferred to a new Homeowner Support Specialist in the Executive Response Unit, Jennifer Butler ("Butler"). Pl. Trial Ex. 23, P00062-63. Shaw contacted Butler to outline his account history and discuss CMI's ongoing collection efforts despite his resolved loan modification. Butler informed Shaw that Shaw did not have any loan modification with CMI because he had not yet signed the July 2011 Modification Agreement. Shaw provided Butler all prior communications allegedly resolving his modification, but was then informed that CMI's Loss Mitigation and underwriting departments had confirmed that Shaw did not have a loan modification with CMI at that time, and would not have any modification with CMI unless and until he executed and submitted the July 2011 Modification Agreement.

68. Upon now being informed that he did not have a binding loan modification with CMI under the May 2011 Modification Agreement, Shaw did not make his modified mortgage payment of $3079.30 for the month of January 2012. Def. Trial Ex. 510-B, CMI000063. Since January 2012, Shaw has not made any payments on his mortgage account. *See* Def. Trial Ex. 510-B, CMI000062-63; Def. Trial Ex. 511-B.

69. On January 3, 2012, Shaw again e-mailed Ross, CMI's Assistant General Counsel, requesting information related to his loan and informing Ross that he was withholding all mortgage payments until CMI officially and finally resolved his account under the May 2011 Modification Agreement. Pl. Trial Ex. 24, P00064-65. Ross responded and informed Shaw that she had reached out to CMI Senior Management for the information Shaw had requested. *Id*.

70. On January 9, 2012, CMI sent Shaw a letter in response to his recent request advising him that non-party Aurora was the owner of his mortgage. Pl. Trial Ex. 25, P00066. Shaw then contacted Aurora and was informed by Aurora that it was not the owner of his mortgage and had no involvement in either his mortgage account or his loan modification since transferring the servicing rights to CMI. *See* Pl. Trial Ex. 26, P00067-69.

71. On January 20, 2012, Shaw sent Ross a formal letter outlining the information obtained from Aurora that it was not the owner of his residential home loan and requested correct ownership information, as well as all documents related to his mortgage account. Pl. Trial Ex. 26, P00067-69.

72. Approximately February 2012, Shaw's mortgage account was placed in default.

73. On February 13, 2012, CMI sent Shaw another letter again identifying the owner of his loan as non-party Aurora. Pl. Trial Ex. 31, P00099.

74. On February 23, 2012, Shaw e-mailed Butler after receiving another collection notice requesting she contact him to resolve his loan modification issues. Pl. Trial Ex. 26, P00070.

75. On March 12, 2012, Shaw received an e-mail from Butler outlining CMI's final position concerning his loan modification. Pl. Trial Ex. 27, P00068. The e-mail informed Shaw that he did not have a loan modification with CMI under the May 2011 Modification Agreement and would not have any modification of his residential loan unless and until Shaw executed the July 2011 Modification Agreement. *Id*. Butler then sent Shaw another copy of the July 2011 Modification Agreement. Pl. Trial Ex. 29, P00074-85.

76. On March 16, 2012, Shaw e-mailed Butler requesting confirmation that it was CMI's final position that the May 2011 Modification Agreement executed by both parties was not in force. Pl. Trial Ex. 30, P00086. Butler responded and confirmed that CMI was not recognizing the May 2011 Modification Agreement and was not changing its position that Shaw had to sign the July 2011 Modification Agreement. *Id*. at P00088. Further, Butler

advised Shaw that because he refused to sign the July 2011 Modification Agreement, his Escalated Case file with the Executive Response Unit was closed and she would no longer communicate with Shaw about his mortgage account. *Id.* at P00088; P00093. At that point, Shaw's Escalated Case with the Executive Response unit was closed and he received no further communication from Butler.

77. Two months later, on May 30, 2012, CMI sent Shaw a letter advising him that his mortgage account had again been deemed an Escalated Case and had been transferred to a new Homeowner Support Specialist in the Executive Response Unit, Robert Orcutt ("Orcutt"). Pl. Trial Ex. 33, P00101-02. Shaw contacted Orcutt and outlined the history of his mortgage account and CMI's inconsistent positions on his loan modification. Orcutt advised Shaw that he would review Shaw's mortgage account and contact him to resolve his account issues.

78. On June 13, 2012, Orcutt sent Shaw an e-mail outlining a proposed reinstatement of Shaw's mortgage account. Pl. Trial Ex. 35, P00104-06. The reinstatement offer provided that if Shaw paid a past due amount of $18,534.34 by June 30, 2012, CMI would reinstate Shaw's mortgage account and remove his account from default. *Id*. at P00105. However, the reinstatement offer made no mention of any loan modification or the terms of Shaw's loan going forward after reinstatement. Shaw contacted Orcutt and asked whether CMI would recognize the May 2011 Modification Agreement if he made the reinstatement payment but was not given any assurance that CMI would rebook the modification agreement or not require him to execute the July 2011 Modification Agreement documents at some time in the future. Shaw refused the reinstatement offer and did not make any reinstatement payment.

79. On June 20, 2012, Shaw e-mailed Orcutt and requested contact information for the representative or trustee of the SASCO 2003-37A Mortgage Pass-Through Certificates, the bundled mortgage investment that included Shaw's residential home loan. Pl. Trial

Ex. 36, P00107. In response, Orcutt provided Shaw with the e-mail contact of non-party Deborah Lenhart, a representative of the bondholders of the SASCO Mortgage Pass-Through Certificates 2003-37A.

80. On June 21, 2012, Shaw sent an e-mail to Deborah Lenhart at the contact information provided by Orcutt, but the e-mail was returned as undeliverable. Pl. Trial Ex. 37, P00110-111.

81. On June 22, 2012, Shaw again contacted Orcutt to request correct contact information for Lenhart, or another representative, as the information Orcutt provided was incorrect. Pl. Trial Ex. 37, P00112-114. Orcutt informed Shaw that he did not have any other contact information for Lenhart. Pl. Trial Ex. 37, P00115.

82. On June 26, 2012, Shaw received an e-mail from CMI stating that his online account had been suspended and that he would no longer be able to receive online statements or access his online account. Pl. Trial Ex. 37, P00117.

83. In August 2012, Shaw moved out of the McFaul Court property.

84. At the end of 2012, CMI began foreclosure proceedings on the McFaul Court property. In response, Shaw placed the McFaul Court property up for sale as a short sale with non-party Pinnacle Realty.

85. On January 3, 2013, dismissed defendant NTS recorded a Notice of Default and Election to Sell Under Deed of Trust in the official records of Douglas County, Nevada (Doc. No. 0815587). Def. Trial Ex. 505-B, CMI000042-47.

86. On January 29, 2013, Shaw sent a letter to CMI objecting to the pending foreclosure of the McFaul Court property and again requesting information and documents pertaining to his residential loan. Pl. Trial Ex. 38, P00120-22.

87. On February 5, 2013, Shaw received an e-mail from attorney Joseph E. Bleeker on behalf of both CMI and dismissed defendant NTS. Pl. Trial Ex. 39, P00123-24. The e-mail informed Shaw that attorney Bleeker was in receipt of Shaw's January 29, 2013 letter and

was treating that letter as a "Qualified Written Request" pursuant to RESPA. *Id*. Attorney Bleeker then advised Shaw that CMI would respond to his letter within sixty days as required under RESPA. *Id*.

88. On February 8, 2013, Shaw received and accepted an offer on the McFaul Court property from non-parties Jeff and Cathy Knapp ("the Knapps"). Pl. Trial Ex. 40, P00125-135. The offer was a contingent short sale offer with a purchase price of $857,000.00 ("the Knapp Offer").

89. At the time of the Knapp Offer, Shaw owed approximately $900,000.00 to CMI on the residential loan and approximately $250,000.00 on the two junior liens for a total liability on the McFaul Court Property of approximately $1,150,000.

90. On February 14, 2013, Shaw forwarded to CMI, through his real estate agent, the accepted Knapp Offer. Pl. Trial Ex. 44, P00202.

91. On February 25, 2013, Shaw received a letter from CMI advising him that pursuant to the terms of the May 2011 Modification Agreement, Shaw's modified payments would be increasing from $3079.30 to $3,539.22 starting June 1, 2013. Pl. Trial Ex. 42, P00138. Shaw received this letter despite CMI repeatedly informing Shaw as early as December 2011, that he did not have a loan modification with CMI under the May 2011 Modification Agreement.

92. On March 6, 2013, Shaw received a package from Kristin Dennis, a Default Research Specialist at CMI, in response to Shaw's January 29, 2013 "Qualified Written Request." Pl. Trial Ex. 43, P00139-87. The package included copies of Shaw's account history with CMI from February 2006 through March 2013 (*Id*. at P00140-49); CMI's transaction codes for its electronic mortgage accounts (*Id*. at P00150-51); Shaw's adjustable rate note dated October 8, 2013 (*Id*. at P00152-60); the recorded first deed of trust (*Id*. at P00161-82); and the June 20, 2012 assignment of deed of trust to CMI (*Id*. at P00183-87). The letter further advised Shaw that CMI had determined that Shaw had been eligible for a

modification of his residential loan, but that his application was closed for lack of documentation because he did not sign and return the July 2011 Modification Agreement. *Id*. at P00139.

93. On or about March 19, 2013, Maria Mejia ("Mejia"), an employee in CMI's Homeowner Assistance Department, was assigned as the short sale advisor to review the Knapp Offer. Def. Trial Ex. 26.

94. On March 26, 2013, Mejia contacted Shaw's real estate agent and advised Shaw, through his real estate agent, that in order for CMI to review the Knapp Offer, Shaw had to submit several documents including: (1) a hardship letter; (2) a signed purchase agreement (as the original offer had expired in late February 2013); (3) Shaw's tax returns for the tax years 2011 and 2012; (4) all payoffs for the junior liens on the property within the last sixty days, if any; or, (5) if the junior liens still needed to be paid off, then approval letters of the short sale by each junior lien holder and releases of their junior liens; (6) the 2011 real estate tax bill for the McFaul Court property; and (7) a hazard insurance policy on the property. Def. Trial Ex. 525-A.

95. In mid-March 2013, Shaw and the Knapps signed an agreement to extend the Knapp Offer for an additional thirty (30) days.

96. On April 3, 2013, an appraisal of the McFaul Court property was conducted at the request of CMI as part of the evaluation of the Knapp Offer. Pl. Trial Ex. 49, P00283. At that time, the McFaul Court property was appraised at a value of $1,082,000.00. *Id*.

97. In mid-April 2013, after no response to the Knapp Offer by CMI, Shaw and the Knapps executed a second thirty (30) days extension on the Knapp Offer.

98. On May 6, 2013, dismissed defendant NTS recorded a Notice of Trustee's Sale on the McFaul Court property in the official records of Douglas County, Nevada (Doc. No. 0823028) setting the trustee's sale for June 5, 2013. Def. Trial Ex. 507-B, CMI000049-50.

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99. On May 16, 2013, Shaw received an e-mail from Mejia informing him that CMI had not received all required documentation for CMI to review and consider the Knapp Offer. Shaw resubmitted most of the documentation but did not provide, at any point during the relevant time period, payoff information on the junior liens or a release of liens from the junior lien holders.

100. On May 23, 2013, CMI denied the short sale of the McFaul Court property under the Knapp Offer for lack of documentation related to the junior lien holders. However, by that point, the Knapp Offer had already expired under the terms of the second extension.

101. On June 5, 2013, dismissed defendant NTS sent Shaw a letter advising him that the trustee's sale set for June 5, 2013, was postponed until August 7, 2013. Pl. Trial Ex. 45 P00204.

102. In July 2013, Shaw and the Knapps revived the Knapp Offer to purchase the McFaul Court property as a short sale for the purchase price of $857,000.00. Shaw submitted the revived Knapp Offer to CMI. Along with the revived Knapp Offer, Shaw submitted all documents originally requested by CMI for consideration of the short sale except for releases from the junior lien holders.

103. On July 26, 2013, Shaw filed his initial complaint against CMI initiating the present action. ECF No. 1, Exhibit 1, p.8-19.

104. In mid-August 2013, after no response to the revived Knapp Offer by CMI, Shaw and the Knapps executed a thirty (30) day extension on the offer.

105. In mid-September 2013, again after no response to the revived Knapp Offer by CMI, Shaw and the Knapps executed a second thirty (30) day extension on the offer.

106. In October 2013, Shaw applied for and was denied credit as a cosigner for his son on a thirty-six (36) month lease of a Kia automobile.

107. In mid-October 2013, after still no response to the revived Knapp Offer by CMI, Shaw and the Knapps executed a third and final thirty (30) day extension on the offer.

108. In mid-November 2013, the revived Knapp Offer expired under the terms of the last extension. At that point, Shaw ended his listing agreement with non-party Pinnacle Realty and the McFaul Court property was no longer listed for sale.

109. On December 11, 2013, and in response to developments in the litigation, dismissed defendant NTS recorded a rescission of the notice of default in the official records of Douglas County, Nevada (Doc. No. 0835262). Def. Trial Ex. 508-B.

110. During the infancy of the litigation, defendant CMI was represented by Attorney Colt Dodrill ("Attorney Dodrill"). While the litigation was proceeding, Shaw contacted and met with Attorney Dodrill several times. In December 2013, after a court hearing, Attorney Dodrill and Shaw had a discussion about the possible short sale of the McFaul Court property. As part of that conversation, Attorney Dodrill advised Shaw that if he was to re-list the property for sale and accept any short sale offers, those offers should be submitted directly to Attorney Dodrill as counsel of record for CMI, rather than to CMI's Homeowner's Assistance department.

111. After the discussion with Attorney Dodrill, Shaw listed the McFaul Court property as a short sale with non-party Chase International Realty, at a listing price of $1,082,000.00, the appraised value of the property in April 2013.

112. On April 3, 2014, Shaw filed an amended complaint in this litigation. ECF No. 52.

113. On April 8, 2014, Shaw received a short sale offer on the McFaul Court property from non-parties Darin and Lisette Smith ("the Smiths") to purchase the property for $785,000.00. Pl. Trial Ex. 48A.

114. On April 11, 2014, Shaw submitted a counter-offer to the Smiths for the same purchase price which they accepted ("the first Smith Offer"). Pl. Trial Ex. 48A. The terms of the accepted counter-offer included that: (1) CMI had until April 30, 2014, to approve the short sale; (2) Katherine Barkley and Janice Shaw, the second and third junior lien holders, would be paid in full on their junior liens from the sale proceeds of the McFaul

Court property; (3) Shaw would receive $75,000.00 from the sale proceeds of the property; and (4) CMI would receive the remaining sale proceeds as full and final satisfaction of Shaw's residential loan and the first deed of trust. *Id.*

115. On April 14, 2014, Shaw forwarded the first Smith Offer to Attorney Dodrill and demanded a response on the offer by April 28, 2014. Pl. Trial Ex. 48A.

116. On April 30, 2014, the first Smith Offer lapsed pursuant to its terms without any action by CMI on the short sale offer.

117. On June 2, 2014, CMI denied the first Smith Offer. However, by that point, the offer had already expired under its terms more than a month earlier.

118. On July 11, 2014, Shaw received another short sale offer from the Smiths to purchase the McFaul Court property for $825,000.00 ("the second Smith Offer"). Pl. Trial Ex. 48B. The terms of the second Smith Offer included: (1) approval of the short sale by CMI within 5 business days of acceptance by Shaw; (2) Katherine Barkley and Janice Shaw, the second and third junior lien holders, would be paid in full on their junior liens from the sale proceeds; (3) Shaw would receive $75,000.00 from the sale proceeds; and (4) CMI would receive the remaining proceeds as full and final satisfaction of Shaw's residential loan and the first deed of trust. *Id.* Shaw accepted and forwarded the second Smith Offer to Attorney Andrew Bao ("Attorney Bao"), CMI's new counsel of record in the litigation. Pl. Trial Ex. 48B. Attorney Bao advised Shaw that the second Smith Offer had been submitted to CMI and that if any further information was required to consider the offer he would contact Shaw. *Id.*

119. On July 19, 2014, the second Smith Offer lapsed without any action by CMI.

120. During Shaw's attempts to sell the property in 2013 and 2014, junior lien holder Katherine Barkley did not have any conversations with Shaw regarding the various short sale offers on the McFaul Court property, had not agreed to any short sale offers on the property, and had not agreed to release her junior lien.

121. Similarly, junior lien holder Janice Shaw did not have any conversations with Shaw regarding the various short sale offers on the McFaul Court property, had not agreed to any short sale offer on the property, and had not agreed to release her junior lien.[11]

122. On August 25, 2014, Shaw filed his second amended complaint in this action. ECF No. 109. The second amended complaint is the operative complaint in this litigation.

123. By the time trial began in May 2016, Shaw's mortgage account with CMI showed a total amount due of $1,162,304.95. Pl. Trial Ex. 57. This amount was calculated as the combination of the remaining principal balance of $891,467.07; $221,350.69 in accrued interest; $43,110.45 in advanced escrow charges;[12] $186.90 in fees; and $7963.83 in past-due fees and late charges. *Id.*

124. Throughout the history of this action, Shaw sought contact information from CMI for the current owner of his residential loan. However, prior to trial in June of 2016, CMI never provided contact information for, or identified the actual current owner of Shaw's residential loan.

125. Throughout the history of this action Shaw suffered a loss of personal and business reputation as a direct consequence of CMI's conduct, collection activities, and eventual initiation of foreclosure proceedings on the McFaul Court property.

II. Conclusions of Law

In his second amended complaint, Shaw has alleged five causes of action against CMI that are currently before the court: declaratory relief, breach of contract, breach of the implied covenants of good faith and fair dealing, interference with prospective economic advantage, and violation of

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[11] Due to their status as junior lien holders on the McFaul Court property and beneficiaries under Shaw's obligations in their favor, the court will order that copies of this order be served upon them by Shaw's counsel.

[12] Since January 2012, CMI has advanced and paid all taxes, Homeowner's Insurance premiums, and other escrow expenses on the McFaul Court property in order to protect its security interest under the first deed of trust. Def. Trial Ex. 513-B.

the Real Estate Settlement Procedures Act. ECF No. 109. Shaw has the burden of proof on all his claims and must prove each claim by a preponderance of the evidence. *See, e.g., Cal. State Bd. of Equilization v. Renovisor's Inc.*, 282 F.3d 1233 (9th Cir. 2002) (stating the basic premise that civil claims must be proven by a preponderance of the evidence). Along with contract and tort damages, Shaw also seeks punitive damages for CMI's conduct in this action. *See* ECF No. 109. In order to be eligible for an award of punitive damages, Shaw must prove by clear and convincing evidence that CMI engaged in oppression, fraud, or malice. *See* NRS §42.005(1). The court addresses each of Shaw's remaining causes of action below.

A. Declaratory Relief

Pursuant to Section 2201 of the Declaratory Judgment Act, "any court of the United States . . . may declare the rights and other legal relations of any interested party seeking such declaration." 28 U.S.C. §2201. Further "[a]ny such declaration shall have the force and effect of a final judgment or decree and shall be reviewable as such." *Id*. In his claim for declaratory relief, Shaw seeks a declaration from the court that the May 2011 Modification Agreement was a fully executed, valid, and binding loan modification agreement between the parties and that such agreement was, pursuant to its terms, effective May 1, 2011. *See* ECF No. 109. Shaw also seeks an order from the court declaring the parties' obligations and financial relationship under that agreement. *Id*.

The existence of a contract is a question of law. *May v. Anderson*, 119 P.3d 1254, 1257 (Nev. 2005); *Kabil Developments Corp. v. Mignot*, 566 P.2d 505, 577 (Or. 1977). "Formation of a valid contract requires that there be a meeting of the minds as evidenced by a manifestation of mutual intent to contract." *Ridenour v. Bank of Am., N.A.*, 23 F. Supp. 3d 1201, 1208 (D. Idaho 2014). This manifestation can take the form of an offer by one party and acceptance by the other. *Id*.; *see also Erection Co. v. W&W Steel, LLC*, 2011 U.S. Dist LEXIS 121581, at *19 (D. Or. 2011) (citing *Ken Hood Construction Co. v. Pacific Coast Construction, Inc.*, 120 P.3d 6 (Or. 2005) ("Manifestation of mutual assent ordinarily occurs through an offer or proposal by one party

followed by acceptance of the other party."); *Integrated Storage Consulting Servs. v. NetApp, Inc.*, 2013 U.S. Dist. LEXIS 107705, at *19 (N.D. Cal. 2013) ("The formation of a contract is properly shown through evidence of an offer and acceptance of definite terms."). The party asserting the existence of a contract has the burden to establish the contract's existence and its terms. *Erection Co*., 2011 U.S. Dist. LEXIS 121581, at *20.

Here, the undisputed evidence presented at trial establishes that defendant CMI offered to modify Shaw's residential home loan in May 2011. CMI sent Shaw a letter written by CMI employee Kim Vukovich along with a copy of the May 2011 Modification Agreement. CMI's letter specifically advised Shaw that he was eligible for a loan modification as outlined by the terms of the enclosed agreement. The letter further advised Shaw that if he accepted the terms of that agreement, he should execute and submit the agreement to CMI. Shaw properly executed, by notarized signature, the May 2011 Modification Agreement and submitted the agreement to CMI on May 18, 2011, pursuant to CMI's instructions. CMI then accepted the executed May 2011 Modification Agreement by booking the terms of the modification into Shaw's electronic mortgage account on May 23, 2011. After that date, Shaw's mortgage account showed that his residential loan had been modified pursuant to the terms of the May 2011 Modification Agreement.

Additionally, on June 30, 2011, after having already booked the May 2011 Modification Agreement into Shaw's mortgage account and having accepted Shaw's first timely made modified payment under the agreement, CMI Vice-President Larry Bauman separately executed, by notarized signature, the May 2011 Modification Agreement on behalf of CMI. CMI then sent a copy of the completed May 2011 Modification Agreement, executed by both parties, to Shaw on August 9, 2011. Moreover, CMI, through its Assistant General Counsel, Dana Ross, and Homeowner Support Specialist Chris Gabbert, recognized both the validity and the legality of the May 2011 Modification Agreement in a separate letter to Shaw sent on August 23, 2011. Finally, it is undisputed that CMI accepted Shaw's timely made modified monthly payments of $3079.30 from June through December 2011.

The court finds that this record of activity is sufficient to establish an offer of a modification by CMI and acceptance of that offer by Shaw. Such conduct establishes the formation of a contract as a matter of law. *See Erection Co.*, 2011 U.S. Dist. LEXIS 121581, at *19. Further, this record of activity unequivocally established "a manifestation of mutual intent" between the parties to modify Shaw's residential home loan. *Ridenour*, 23 F. Supp. 3d at 1208. Therefore, the court finds that the undisputed evidence in this action establishes that the parties executed a valid and binding loan modification agreement known as the May 2011 Modification Agreement that defines the financial relationship, duties, and obligations between Shaw and CMI, the terms of which are outlined in the agreement. *See* Pl. Trial Ex. 6, P00016-20. The court makes this finding concerning the formation and validity of the May 2011 Modification Agreement *nunc pro tunc*.

As the court has found that the May 2011 Modification Agreement is a valid contract between the parties, the court finds that due to the long history of this action it is necessary to define the obligations and financial relationship of the parties under the May 2011 Modification Agreement and going forward from this order. In that regard, the court makes these additional findings. First, the modification of Shaw's residential loan pursuant to the May 2011 Modification Agreement became effective May 1, 2011. *See* Pl. Trial Ex. 6, P00017, Section 4. Second, pursuant to the contract, Shaw's modified monthly payments for the first two years of the agreement were set at $3,079.30, with the first payment having been due on June 1, 2011. *Id*. at P00018, Section 4(C). It is undisputed that Shaw timely made modified monthly payments under the May 2011 Modification Agreement from June through December 2011, for a total of seven (7) modified payments. As addressed in depth below when analyzing Shaw's breach of contract claim, the court finds that Shaw's breach of the May 2011 Modification Agreement - by withholding his modified monthly mortgage payments beginning in January 2012 - was reasonable and excused because of CMI's anticipatory repudiation of the May 2011 Modification Agreement in December 2011. *See Infra* Section II(B)(ii). Accordingly, the court considers the time period from January 2012, through the date of this order tolled and excluded under the agreement. The court finds that this tolling of

the modification agreement is equitable based on CMI's continued refusal to recognize the existence of the May 2011 Modification Agreement until the filing of the pretrial order in late 2015, four-and-a-half years after the May 2011 Modification Agreement was executed by both parties. Therefore, going forward from this order, Shaw's modified monthly payment under the May 2011 Modification Agreement remains $3,079.30 for the next seventeen (17) months, after which the monthly payment will increase pursuant to the staggered payment plan outlined in the agreement with the date the staggered payments begin commencing from the date of this order and excluding the tolled period. *See* Pl. Trial Ex. 6, P00018, Section 4(C). Similarly, the maturity date of Shaw's modified loan is extended from November 1, 2033, until approximately August 1, 2038, to account for the time tolled in this action.

Third, as specified in the May 2011 Modification Agreement, Shaw's principal balance on the loan was set at $910,110.34, $85,777.89 of which was deferred from interest charges and is due as a balloon payment at the end of Shaw's loan. *See* Pl. Trial Ex. 6, P00017-18, Section 4(B) & 4(C). Since that time, Shaw made seven modified payments of $3,079.30 under the agreement and reduced the principal balance on his residential loan. According to Shaw's April 2016 mortgage statement admitted at trial, his current remaining principal balance under his loan is $891,467.07. Pl. Trial Ex. 57. Thus, going forward, the court finds that the remaining principal balance on Shaw's loan is $891,467.07, and that Shaw's mortgage account with CMI should reflect this amount.

Fourth, the court recognizes that beginning in January 2012, CMI advanced $43,100.45 in escrow funds to Shaw's mortgage account in order to protect its security interest in the McFaul Court property during the parties' dispute and this litigation. *See* Pl. Trial Ex. 57; Def. Trial Ex. 513-B. These advanced escrow funds included quarterly property tax payments on the McFaul Court property, monthly Homeowner's Insurance premiums, and other escrow expenses for which Shaw was responsible under the terms of his original residential loan, first deed of trust, and the May 2011 Modification Agreement. CMI made all escrow payments on Shaw's account since

January 2012, even though Shaw's escrow account had insufficient funds to make these payments. Though it was in CMI's interest to advance these funds in order to protect its security interest in the McFaul Court property, Shaw directly benefited from CMI's conduct as no property tax liens were recorded on the McFaul Court property during the parties' dispute and his Homeowner's Insurance policy did not lapse. Accordingly, the court finds that in the interest of equity between the parties, Shaw is liable for, and CMI is entitled to recover from Shaw, the $43,100.45 in advanced escrow charges. Therefore, going forward from this order, Shaw's mortgage account should reflect that he continues to owe $43,100.45 to CMI in advanced escrow charges.

Finally, the court finds that any other fees charged by CMI against Shaw's mortgage account since January 2012, are invalid and improper. As the court has found the time between January 2012 and this order is tolled and excluded from the May 2011 Modification Agreement, all interest charges, late payment fees, and any other fees or past due amounts charged against Shaw under either his original residential loan or the May 2011 Modification Agreement are excluded. The court's finding specifically extends to and includes the $221,350.89 in accrued interest, $189.90 in fees, and $7,963.83 in past-due fees and late charges reflected on Shaw's April 2016 mortgage statement, as well as any and all other expenses and fees that have accumulated since January 2012, except for the aforementioned advanced escrow charges. *See* Pl. Trial Ex. 57. Accordingly, the court shall issue judgment on Shaw's claim for declaratory relief as outlined above.

B. Breach of Contract

To prevail on a breach of contract claim, a plaintiff must prove: (1) the existence of a valid contract; (2) a breach of that contract by the defendant; and (3) damages resulting from defendant's breach. *Saini v. Int'l Game Tech.*, 434 F. Supp. 2d 913, 919-20 (D. Nev. 2006); *Brown v. Kinross Gold U.S.A., Inc.*, 531 F. Supp. 2d 1234, 1240 (D. Nev. 2008). A breach of contract can occur in one of two ways. *See Nev. Power Co. v. Calpine Corp.*, 2006 U.S. Dist. LEXIS 36135, at *22 (D. Nev. 2006). The first is an actual breach of the specific terms and obligations of the contract.

Brown, 531 F. Supp. 2d at 1240. The second is an anticipatory breach, or repudiation, of the contract. *Nev. Power Co.*, 2006 U.S. Dist. LEXIS 36135, at *23.

In this action, Shaw has alleged both an actual breach of contract claim and an anticipatory breach of contract claim against CMI. *See* ECF No. 109; ECF No. 168. As each type of breach permits different relief and requires proof of separate and distinct elements, the court shall evaluate CMI's conduct for each type of breach separately.

i. Actual Breach

As addressed above, the court has found that the May 2011 Modification Agreement constitutes a valid and binding contract. *Supra* Section II(A). Thus, the remaining issues for the court to determine are (1) whether CMI breached the terms of the May 2011 Modification Agreement, and (2) if there was a breach of that agreement, the damages Shaw incurred as a result of that breach, if any. *See Saini*, 434 F. Supp. 2d at 920.

Under the terms of the May 2011 Modification Agreement, CMI had a duty to correctly book and apply all of Shaw's timely made modified payments throughout the life of the modified loan. Further, CMI had a duty to keep correct records of Shaw's mortgage account so that his account was not improperly placed in default. However, in direct contravention of its obligations and duties under the May 2011 Modification Agreement, CMI unbooked the modified loan terms from Shaw's electronic mortgage account, unbooked Shaw's timely made mortgage payments for the months of June and July 2011; placed Shaw's account into default at a time that he was current on all his mortgage obligations under the express terms of the May 2011 Modification Agreement; and refused to book Shaw's timely made mortgage payment for the month of August 2011. Further, CMI sent Shaw collection notices demanding payment on over $30,000.00 in past due amounts in both July and August 2011, even though pursuant to the terms of the May 2011 Modification Agreement, all amounts that were previously past due (including the unpaid monthly payments from October 2010, through February 2011, as well as the difference between Shaw's prior monthly payments and the modified payments under the trial modification period) were specifically

included in the new principal balance of $910,110.34, and thus, there was no past due balance on Shaw's mortgage account at the time.

The court finds that CMI's undisputed conduct was a direct breach of the May 2011 Modification Agreement. Further, the court finds that CMI's unilateral actions were made without justification. As recognized by CMI, there was nothing legally deficient with the May 2011 Modification Agreement. Pl. Trial Ex. 21, P00060. Thus, CMI was not justified in unbooking both the modification's terms and Shaw's monthly payments from his electronic mortgage account simply because the May 2011 Modification Agreement lacked a payment date for the balloon payment.

As the court has found that CMI breached the May 2011 Modification Agreement, the court now turns to the issue of damages. Damages for a breach of contract claim are limited to those specifically outlined in the contract, if any, and those expectation damages sufficient to put the non-breaching party in the position it would have been in had the breach not occurred. *See, e.g., Keife v. Metro. Life Ins. Co.*, 931 F. Supp. 2d 1100, 1108-09 (D. Nev. 2013); *Midwest Precision Services, Inc. v. PTM Indus. Corp.*, 887 F.2d 1128, 1136-37 (1st Cir. 1989). Here, the May 2011 Modification Agreement does not set forth any damages for a breach of that agreement by CMI. *See* Pl. Trial Ex. 6, P00016-20. As such, Shaw's damages claim is limited to being placed in the same position under the May 2011 Modification Agreement as if the agreement had not been breached by CMI, which is a modification of his residential loan under the terms of that agreement. Shaw has already achieved this position as addressed above in the court's analysis of Shaw's declaratory relief claim. *See Supra* Section II(A). Further, it is undisputed that after CMI breached the May 2011 Modification Agreement it resolved and cured its breach of that agreement on August 15, 2011, when it rebooked the modification terms and Shaw's payments into his electronic mortgage account. *See* Def. Trial Ex. 510-B, CMI000064. At the same time, CMI removed Shaw's account from default and corrected the delinquent payment reports it had made to the various credit reporting agencies during its breach. Finally, CMI waived all late fees and other charges that it had

charged to Shaw's account during its breach. Thus, Shaw was already placed in the same position under the May 2011 Modification Agreement in late August 2011, as if CMI's breach had not occurred. And, Shaw has failed to prove any other consequential damages resulting from CMI's one-month breach of the May 2011 Modification Agreement. Accordingly, the court finds that Shaw is not entitled to contract damages for CMI's breach.

ii. Anticipatory Breach

An anticipatory breach is a breach of a contract that occurs when one party to the contract, without justification and prior to a breach by the other party, makes a statement or engages in conduct indicating that it will not or cannot substantially perform its duties under the contract. *Nev. Power Co.*, 2006 U.S. Dist. LEXIS 36135, at *28. An anticipatory breach, or repudiation, of a contract may be express or implied. *Id.* An express repudiation occurs when one party demonstrates "a definite unequivocal and absolute intent not to perform a substantial portion of the contract." *Kahle v, Kostiner,* 455 P.2d 42, 44 (Nev. 1969); *see also Stratosphere Litigation, LLC v. Grand Casinos*, 298 F.3d 1137, 1147 (9th Cir. 2002) (holding that an "[a]nticipatory repudiation occurs when a party through conduct or language makes a clear, positive and unequivocal declaration of an intent not to perform."). An implied repudiation occurs when one party acts in such a manner as to make its future performance under the contract impossible. *Covington Bros. v. Valley Plastering, Inc.*, 566 P.2d 814, 817 (Nev. 1977). If one party anticipatorily breaches the contract, a repudiation of the contract has occurred and the non-breaching party is excused from performing its obligations under the contract. *Kahle*, 455 P.2d at 44; *see also Cleverley v. Ballantyne*, 2013 U.S. Dist. LEXIS 177416, at *13 (D. Nev. 2013) (stating that an anticipatory repudiation of a contract excuses the necessity for the non-breaching party to tender performance).

The court has reviewed the evidence presented at trial and finds that CMI expressly repudiated the May 2011 Modification Agreement. The evidence in this action establishes that CMI made repeated, unambiguous, and unequivocal statements to Shaw that the May 2011 Modification Agreement was not a binding modification agreement between the parties, that Shaw did not have

any modification agreement with CMI, and that CMI would not recognize any modification agreement until Shaw executed the July 2011 Modification Agreement. CMI began making these statements to Shaw in July 2011, when Chris Gabbert, Shaw's Homeowner Support Specialist, told Shaw that CMI would only grant him a modification of his loan if he signed the July 2011 Modification Agreement. And CMI continued making similar statements about the need for Shaw to execute the July 2011 Modification Agreement even after CMI had rebooked the May 2011 Modification Agreement in August 2011. For example, Shaw's next Homeowner Support Specialist, Jennifer Butler, unequivocally advised Shaw in December 2011, and repeatedly through early 2012, that he would not have any modification of his residential loan unless he signed the July 2011 Modification Agreement and that this decision was confirmed by CMI's Loss Mitigation and underwriting departments. Although Gabbert's statement concerning the validity of the May 2011 Modification Agreement was prior to CMI curing its breach in August 2011, Butler's statements regarding the validity of the May 2011 Modification Agreement occurred in December 2011, over four months after CMI rebooked that agreement. And still no explanation was ever provided to Shaw for CMI's change in position between August 23, 2011, and early December 2011.

Based on this conduct, especially all conduct that occurred after CMI's "resolution" of Shaw's mortgage account in August 2011, the court finds that CMI expressly repudiated the May 2011 Modification Agreement. CMI's conduct constituted "a definite unequivocal and absolute intent not to perform" under the contract. *Kahle*, 455 P.2d at 44. In fact, this court cannot imagine a more unequivocal and absolute intent to not perform under the May 2011 Modification Agreement than stating that the agreement executed by the parties simply did not exist, and would not be honored. Moreover, as addressed above in Shaw's actual breach of contract claim, the court finds that CMI was not justified in its conduct simply because the May 2011 Modification Agreement did not contain a specific due date for the balloon payment. *See Supra* Section II(B)(i). Therefore, the court finds that because CMI repudiated the May 2011 Modification Agreement, Shaw was excused from his performance under that agreement beginning in January 2012. Further, the court

finds that Shaw was reasonable in withholding his payments after being told by Butler in December 2011, that the May 2011 Modification Agreement was not in force and that there would be no modification unless and until he executed the July 2011 Modification Agreement based on CMI's prior conduct in both breaching and repudiating the contract in July 2011, and its history of inconsistent and contradictory statements. Thus, because Shaw's non-performance under the May 2011 Modification Agreement was excused, all interest, late fees, and past due charges accrued on Shaw's loan since January 2012, are not recoverable by CMI and the court finds that these charges shall be excluded from Shaw's mortgage account.[13]

C. Breach of the Implied Covenants of Good Faith and Fair Dealing

Under Nevada law, "[e]very contract imposes upon each party a duty of good faith and fair dealing in its performance and execution." *A.C. Shaw Constr. v. Washoe Cty.*, 784 P.2d 9, 9 (Nev. 1989) (quoting Restatement (Second) of Contracts §205); *see also Nelson v. Heer*, 163 P.3d 420, 427 (Nev. 2007) ("It is well established that all contracts impose upon the parties an implied covenant of good faith and fair dealing, which prohibits arbitrary or unfair actions by one party that work to the disadvantage of the other."). "The implied covenants of good faith and fair dealing impose a burden that requires each party to a contract to 'refrain from doing anything to injure the right of the other to receive the benefits of the agreement.'" *Integrated Storage Consulting Servs.*, 2013 U.S. Dist. LEXIS 107705, at *23 (quoting *San Jose Prod. Credit Ass'n v. Old Republic Life Ins. Co.*, 723 F.2d 700, 703 (9th Cir. 1984).

To establish a claim for breach of the implied covenants of good faith and fair dealing, a plaintiff must prove: (1) the existence of a contract between the parties; (2) that defendant breached its duty of good faith and fair dealing by acting in a manner unfaithful to the purpose of the contract; and (3) the plaintiff's justified expectations under the contract were denied. *See Perry v.*

[13] The court has previously addressed the impact of CMI's anticipatory breach and how it affects the parties going forward from the court's order in the court's analysis of Shaw's declaratory relief claim. *See Supra* Section II(A).

Jordan, 900 P.2d 335, 338 (Nev. 1995) (citing *Hilton Hotels Corp. v. Butch Lewis Prod. Inc.*, 808 P.2d 919, 922-23 (Nev. 1991). Generally, the remedy for a breach of the implied covenants of good faith and fair dealing is limited to contractual remedies. *Mundy v. Household Fin. Corp.*, 885 F.2d 542, 544 (9th Cir. 1989); *see also Nev. Power Co.*, 2006 U.S. Dist. LEXIS 36135, at *26 ("As a contract concept, breach of duty leads to the imposition of contract damages determined by the nature of the breach and contract principles."). However, in limited circumstances, a breach of the implied covenants can give rise to tort liability. *See, e.g., State v. Sutton*, 103 P.3d 8, 19 (Nev. 2004) (holding that in special circumstances, a breach of the implied covenants of good faith and fair dealing can give rise to tort liability).

In his second amended complaint, Shaw has alleged a breach of the implied covenants of good faith and fair dealing arising from CMI's repeated refusal to accept the May 2011 Modification Agreement and continued demands for both payment on past due amounts and the execution of the July 2011 Modification Agreement. ECF No. 109. As part of this claim, Shaw has requested both contract and tort damages. *Id*. Because Shaw is requesting both contract and tort damages, the court shall evaluate Shaw's breach of the implied covenants claims separately for both a contractual and tortious breach.

i. Contractual Breach of Implied Covenants

A contractual breach of the implied covenants of good faith and fair dealing occurs "[w]here the terms of a contract are literally complied with but one party to the contract deliberately countervenes the intention and spirit of the contract." *Hilton Hotels Corp*., 808 P.2d at 923-24. "Establishing such a breach of the implied covenant depends upon the 'nature and purposes of the underlying contract and the legitimate expectations of the parties arising from the contract.'" *Integrated Storage Consulting Servs.*, 2013 U.S. Dist. LEXIS 107705, at *23 (quoting *Mundy*, 885 F.2d at 544) As such, a breach of the implied covenants of good faith and fair dealing is "limited to assuring compliance with the express terms of the contract, and cannot be extended to create obligations not contemplated by the contract." *McKnight v. Torres*, 563 F.3d 890, 893 (9th Cir.

2009)

At trial, Shaw testified that under the terms of the May 2011 Modification Agreement he expected to receive a modification of his loan as outlined by the express terms of that agreement and that his mortgage account would no longer be in default as a result of the modification. However, after the parties executed the May 2011 Modification Agreement, CMI engaged in a pattern of conduct specifically designed to thwart the purpose of the contract and Shaw's reasonable expectations[14] of a modification of his residential home loan.

Initially, the court notes that some of CMI's conduct which Shaw contends establishes a breach of the implied covenants cannot support his claim as a matter of law. It is well established that a claim alleging breach of the implied covenants of good faith and fair dealing cannot be based on the same conduct establishing a separately pled breach of contract claim. *Daly v. United Healthcare Ins. Co.*, 2010 U.S. Dist. LEXIS 116048, at *4 (N.D. Cal. 2010); *see also Guz v. Betchel Nat. Inc.*, 8 P.3d 1089 (Cal. 2010) (holding that when both a breach of contract and breach of implied covenants claim are based on the same conduct, the implied covenants claim is superfluous). Thus, CMI's conduct that was a direct actual breach of the May 2011 Modification Agreement in July 2011, cannot support Shaw's implied covenants claim. As such, the court cannot, and shall not, consider CMI's conduct in unbooking the May 2011 Modification Agreement and all payments made under that agreement from Shaw's electronic mortgage account in determining whether CMI breached the implied covenants.

Nonetheless, the court finds that Shaw has proven by a preponderance of the evidence that CMI breached the implied covenants of good faith and fair dealing. First, it is undisputed that within two weeks after CMI executed the May 2011 Modification Agreement, CMI sent Shaw an entirely new modification agreement, the July 2011 Modification Agreement. This new agreement was identified by CMI employee Juan Mayorga as a "corrected" agreement that had to be signed by

[14] The court has reviewed the May 2011 Modification Agreement and finds that Shaw's expectations under that agreement were reasonable and justified.

Shaw before CMI would modify Shaw's residential loan even though it contained new material terms. No explanation was ever provided to Shaw for why the new modification agreement had been sent. Even Mayorga, the CMI employee who sent the July 2011 Modification Agreement, was unable to inform Shaw as to why the new agreement had been drafted. Shaw was given similar unresponsive answers from Chris Gabbert, who also directed Shaw to sign the new agreement if he wanted a loan modification. The court finds that within the context of the confusing signals to Shaw, CMI's conduct of executing a loan modification agreement and then insisting upon a new agreement with materially different terms without explanation to Shaw "deliberately contravenes the intention and spirit" of the properly executed and valid May 2011 Modification Agreement. *Hilton Hotels Corp.*, 808 P.2d at 923-24. CMI's conduct was completely unfaithful to the purpose of the May 2011 Modification Agreement which was to provide Shaw with a modification of his residential home loan.[15]

Further, CMI engaged in a similar pattern of conduct after resolving Shaw's account in August 2011. For example, Shaw timely made all modified monthly payments of $3,079.30 under the May 2011 Modification Agreement through December 2011. Def. Trial Ex. 510-B, CMI000063-64. However, during that same time, Shaw received written collection notices from CMI demanding payment on non-existent past due amounts. Further, after his account was transferred to Jennifer Butler in December 2011, CMI reversed its position on the May 2011 Modification Agreement and once again claimed that Shaw did not have any modification with CMI because he had not yet signed the July 2011 Modification Agreement. Moreover, even after being informed that CMI had previously determined that there was nothing legally deficient in the May 2011 Modification Agreement, CMI's Loss Mitigation and underwriting departments

[15] The court recognizes that this aforementioned conduct occurred prior to Shaw receiving his copy of the fully executed May 2011 Modification Agreement and the involvement of CMI's Assistant General Counsel, Dana Ross. Once Ross got involved with Shaw's mortgage issues, CMI resolved Shaw's account by determining that the May 2011 Modification Agreement was a valid agreement which constituted a modification of Shaw's residential home loan. However, CMI's conduct prior to this resolution in August 2011 is still relevant to Shaw's claim as it constitutes a breach of the implied covenants until that resolution.

confirmed that Shaw did not have a loan modification with CMI in December 2011, and would not have a recognized loan modification with CMI unless and until he signed the July 2011 Modification Agreement. The court finds that this post August 2011 conduct likewise "deliberately contravenes the intention and spirit" of the May 2011 Modification Agreement. *Hilton Hotel Corp.*, 808 P.2d at 923-24. Based on all of CMI's conduct in this action, the court finds that CMI breached the implied covenants of good faith and fair dealing.

As the court has found that CMI breached the implied covenants of good faith and fair dealing, the court now turns to the issue of damages. Damages under a contractual breach of the implied covenants are limited to regular contract damages. *Munly*, 885 F.2d at 544. As addressed above in the court's analysis of Shaw's actual breach of contract claim, Shaw is not entitled to contract-based damages. *See Supra* Section II(B)(i). Shaw has already been placed in the position that he would have been under the May 2011 Modification Agreement absent CMI's breach of the implied covenants. *Id*. Further, Shaw has not proven any other contract damages that could be awarded under this claim. Therefore, the court finds that Shaw is not entitled to any damages for CMI's contractual breach of the implied covenants.

ii. Tortious Breach of Implied Covenants

Generally, a breach of the implied covenants is a contract-based claim. *Hilton Hotels Corp.*, 808 P.2d at 923. However, a breach of the implied covenants can give rise to tort liability when there is a special relationship between the contracting parties. *Id*. (stating that a tort action for an implied covenants claim requires a special element of reliance or fiduciary duty); *see also Sutton*, 103 P.3d at 19 (Tort liability for breach of the implied covenants of good faith and fair dealing is appropriate where "the party in the superior or entrusted position has engaged in grievous and perfidious misconduct."); *Max Baer Prods., Ltd. v. Riverwood Partners, LLC*, 2010 U.S. Dist. LEXIS 100325, at *14 (D. Nev. 2010) ("Although every contract contains an implied covenant of good faith and fair dealing, an action in tort for breach of the covenant arises only 'in rare and exceptional cases' when there is a special relationship between the victim and tortfeasor."). A

special relationship is "characterized by elements of public interest, adhesion, and fiduciary responsibility." *Id*. Under a tortious breach, "a successful plaintiff is entitled to compensation for all of the natural and probable consequences of the wrong, including injury to the feelings from humiliation, indignity and disgrace to the person." *Sutton*, 103 P.3d at 19.

Here, the court finds that there is a special relationship between the parties sufficient to support tort liability in this action. First, the parties are in drastically different and unequal bargaining positions. *Max Baer Prods., Ltd.*, 2010 U.S. Dist. LEXIS 100325, at *9 (holding that courts allow tort liability where one party holds "vastly superior bargaining power"). CMI, as the servicer of Shaw's residential loan, held all of the bargaining power as it controlled the decision of whether to offer Shaw a loan modification, as well as the terms of that agreement. In contrast, Shaw had limited bargaining power as a financially strapped borrower seeking a modification to a loan agreement that he agreed to years earlier and for which CMI held a protected security interest. Although it was in CMI's interest to grant Shaw a modification so that Shaw would continue making payments, CMI was under no obligation to offer Shaw the May 2011 Modification Agreement or any modification agreement at all. Further, the loan modification agreement is an adhesion contract as CMI completely dictated the terms of the modification with no input by Shaw and offered that agreement to Shaw with his only option to agree to or refuse the agreement. The parties' relationship necessarily shares "a special element of reliance" sufficient for the court to find a special relationship between the parties for tort liability. *Id*. at *15. In such relationships, courts have routinely recognized that "there is a need to 'protect the weak from the insults of the stronger' that is not adequately met by ordinary contract damages." *Id*.

Further, the same conduct that supports a claim for contractual breach of the implied covenants also supports a claim for tortious breach of the implied covenants. *See Supra* Section II(C)(i). The court now turns to the issue of compensable damages under this claim. In his

complaint, Shaw seeks general tort damages pursuant to NRS §41.334.[16] *See* ECF No. 109. NRS §41.334 allows for a party to receive compensation for "loss of reputation, shame, mortification and hurt feelings." Further, under a tortious breach of the implied covenants claim, "a successful plaintiff is entitled to compensation for all of the natural and probable consequences of the wrong, including injury to the feelings from humiliation, indignity and disgrace to the person." *Sutton*, 103 P.3d at 19.

The court has reviewed all the testimony and documents admitted at trial and finds that Shaw has proven by a preponderance of the evidence that he suffered a loss of reputation, shame, mortification, indignity and disgrace as a direct result of CMI's tortious breach of the implied covenants. Shaw testified that he suffered both a loss in personal and business reputation as a proximate result of CMI's improper collection efforts after executing the May 2011 Modification Agreement. For example, Shaw testified that door hanger collection notices were placed on the door of the McFaul Court property in plain sight and were visible to his neighbors and guests to the property. Further, Shaw testified that he received various e-mails, letters, and comments from former clients and former spouses of former clients. In those various communications, Shaw was chastised and his professional skills as an attorney were questioned as he, himself, was suffering financial difficulties and facing potential foreclosure upon his personal residence. Further, Shaw's prior business partner in his legal practice used Shaw's lack of creditworthiness, as a result of CMI's pending foreclosure, in a separate legal dispute regarding the partnership's assets (which included another property) which eventually led to Shaw leaving the business and starting a new practice in Reno, Nevada. Additionally, Shaw testified that he suffered from increasing feelings of frustration, worthlessness, shame and sleeplessness in not being able to resolve or even confront his financial difficulties because of the dispute with CMI. The court finds that Shaw has proven by a

[16] At trial, Shaw specifically stated that he was not seeking any damages for lost income, lost rent on the McFaul Court property, or emotional distress within the context of a emotional distress claim. Thus, Shaw's damages are limited to those under NRS §41.334.

preponderance of the evidence that he suffered a loss of reputation, shame, indignity and disgrace, and other general damages as a proximate cause of CMI's conduct.

As the court has determined that Shaw has proven that he suffered general damages as a result of CMI's conduct, the next significant issue for the court is to quantify Shaw's general damages. A second issue is to determine the time frame for Shaw's damages arising from CMI's tortious conduct. At trial, Shaw presented no evidence related to any monetary figure for his general damages. In fact, the only number offered for Shaw's general damages was presented by Shaw's counsel in closing. In Shaw's closing, Shaw's counsel asked the court to award Shaw damages in the amount of $2,700 per day from the date of the execution of the May 2011 Modification Agreement by both parties through the date of trial for compensation in an amount of approximately $5,000,000.00. However, there is no testimony or evidence to support that number and the $2,700 per day figure has no relation to anything specific in this action.

The court has reviewed the documents and evidence admitted at trial and finds that an appropriate award of compensatory damages to Shaw is $500 per day during the critical time periods from May 23, 2011, through December 31, 2011, subject to tolling from August 23, 2011, to December 7, 2011, during which the May 2011 Modification Agreement was being recognized by CMI; $250 per day during the period commencing in January 2012 (when Shaw discontinued further house payments) through August 2012 (when Shaw vacated the home); and a reduced amount of $100 per day from August 2012 through the close of trial on May 5, 2016.

The court reaches the $500 per day figure based upon the reasonable amount of time spent by Shaw in the many contacts, conversations, and other uneventful communications he had with CMI concerning the properly executed and "not legally deficient" May 2011 Modification Agreement. These uneventful contacts resulted in great stress and frustration to Shaw as well as adverse effects upon Shaw's standing in the community, business reputation and credit worthiness. In support of the damages amount, the court takes judicial notice that the hourly billing rate for an experienced attorney of similar skills as Shaw in this district would have been a minimum of $300

per hour and there is no question that Shaw spent at least one to two hours a day, and on some days much longer, either directly responding to or communicating with CMI and its representatives, or attempting to understand CMI's inconsistent and contradictory positions concerning his mortgage account and loan modification. The court also takes into consideration that any homeowner whose home represented his or her most significant asset and also greatest debt, in this case over $900,000.00, would undergo such frustration, feelings of worthlessness and shame which should be reasonably and fairly compensable at a daily rate of $500.00 per day during this critical time period. Calculating Shaw's damages during this period at a rate of $500 per day, the court finds that Shaw is entitled to compensation in the amount of $57,000.00 ($500 per day for 114 days).

With regard to the period commencing January 2012, when Shaw stopped making his monthly payments, through August 2012, when he voluntarily vacated the McFaul Court property, the court finds that Shaw's decision to terminate payments for lack of reasonable treatment by CMI and to ultimately vacate the house eight months later and move to Reno, Nevada, is reflective in part of the continuation of Shaw's frustration, bitterness and shame imposed upon him by CMI prior to January 2012. Thus the court finds that Shaw is entitled to receive compensation for the harm he suffered during this time period. However, the court finds that Shaw's damages during this period should be adjusted to $250 per day. Calculating Shaw's damages for this period, the court finds that Shaw is entitled to compensation in the amount of $60,750.00 ($250 per day for 243 days).

Finally, with regard to the period commencing in August 2012 through the close of trial on May 5, 2016, the court finds that the tortious conduct inflicted upon Shaw prior to this time continued to cause him to suffer similarly compensable harm at an average rate of $100 per day. The reduction in this amount of compensation is reflective of the fact that Shaw was no longer paying his monthly mortgage payment and was no longer living in the McFaul Court property, although he continued to suffer from the compensable harm previously imposed upon him by CMI as previously set forth. Calculating Shaw's damages for this period, the court finds that Shaw is

entitled to compensation in the amount of $122,100.00 ($100.00 per day for 1,221 days).

D. RESPA

The Real Estate Settlement Procedures Act, found at 12 U.S.C. §2601 *et seq.*, places certain duties and restrictions on mortgage lenders, services, and other entities that deal with residential mortgages. Pertinent to this action is Section 2605 of RESPA which requires a loan servicer, like CMI, to respond to inquires from a borrower. *See* 12 U.S.C. §2605(e). Pursuant to Section 2605(e), if a loan servicer receives a "qualified written request from the borrower" for information relating to the servicing of the borrower's loan, "the servicer shall provide a written response" appropriately responding to the borrower's request and providing any requested documentation. 12 U.S.C. §2605(e)(1)(A) & (2)(C). Similarly, pursuant to Section 2605(k), a loan servicer shall provide "the identity, address, and other relevant contact information about the owner or assignee of the loan" when requested by the borrower. 12 U.S.C. §2605(k)(1)(D). For purposes of triggering a servicer's duty under RESPA, a Qualified Written Request must (1) be a written communication, and (2) include "the name and account of the borrower," and "a statement of the reasons for the belief of the borrower, to the extent applicable, that the account is in error or provides sufficient detail to the servicer regarding other information sought by the borrower." 12 U.S.C. §2605(e)(1)(B)(i)-(ii).

If a servicer receives a Qualified Written Request from a borrower, then the servicer has sixty (60) days to conduct an investigation into the borrower's account, make any appropriate corrections to that account, and respond to the borrower's request "with production of the requested information or an explanation of why the information is unavailable." *Pettie v. Saxon Mortg. Servs.*, 2009 U.S. Dist. LEXIS 4149, at *7 (W.D. Wash. 2009); *see also* 12 U.S.C. §2605(e)(2). Further, the servicer shall provide the contact information for an employee who can provide assistance to the borrower. 12 U.S.C. §2605(e)(2). During the servicer's sixty day investigation and response period, a servicer is precluded from providing "information regarding any overdue payment, owed by such borrower and relating to such period or qualified written request, to any consumer reporting agency." 12 U.S.C. §2605(e)(3). If a servicer fails to comply with its duties

under RESPA, the servicer may be liable for (1) any actual damages the borrower suffered as a result of the servicer's failure to comply with its duties, and/or (2) statutory damages not to exceed $2,000.00. 12 U.S.C. §2605(f).

In his second amended complaint, Shaw has alleged that he sent several Qualified Written Requests to CMI requesting contact information for the owner of his loan and copies of various loan documents, but that CMI failed to respond to his requests in violation of RESPA. ECF No. 109. The initial step for the court under Shaw's RESPA claim is to determine whether Shaw submitted Qualified Written Requests to CMI. At trial, Shaw testified that he requested information from CMI about his mortgage and the owner of his loan immediately after CMI unbooked the May 2011 Modification Agreement and placed his account into default and continued to request this information throughout this litigation. In particular, Shaw alleged that he made the following Qualified Written Requests to CMI: (1) a July 31, 2011 e-mail request to Chris Gabbert; (2) a December 5, 2011 e-mail request to Dana Ross; (3) a January 3, 2012 e-mail request to Ross; (4) a January 20, 2012 formal letter to Ross; (5) a June 20, 2012 e-mail request to Robert Orcutt; (6) a January 29, 2013 formal letter to CMI; and (7) multiple written requests to Gabbert, Jennifer Butler, and Orcutt beginning in the fall of 2011 and continuing until Shaw initiated this litigation. The court shall address each alleged Qualified Written Request below.

To constitute a Qualified Written Request under RESPA, a letter must include the name and account of the borrower as well as a statement of reasons for believing the account is in error. *Pettie*, 2009 U.S. Dist. LEXIS 4149, at *5. Initially, the court notes that Shaw's generally identified written requests to Gabbert, Butler, and Orcutt beginning in the fall of 2011 are not sufficient to constitute Qualified Written Requests. First, Shaw failed to provide any evidence of the dates of these various communications or what information was requested or included in these communications sufficient for the court to determine whether these communications met the requirements of RESPA. Therefore, the court finds that Shaw has not met his burden to prove these communications were Qualified Written Requests under RESPA.

As to the remaining alleged Qualified Written Requests, the court finds that Shaw did proffer copies of these communications at trial. These admitted exhibits contain sufficient information for the court to determine whether these communications meet the requirements for Qualified Written Requests under RESPA. First, the court has reviewed the July 31, 2011 e-mail request to Gabbert and finds that it does not constitute a Qualified Written Request. Although the e-mail (and all of Shaw's communications) appropriately identified Shaw and his mortgage account, the e-mail does not contain a statement for why Shaw believes that his mortgage account is in error. *See* Pl. Trial Ex. 15. Rather, the e-mail only complains of CMI's failure to previously identify the current owner of his residential loan. These statements are insufficient to trigger CMI's RESPA duties because they do not mention or discuss his default or mortgage account. *See Pettie*, 2009 U.S. Dist. LEXIS 4149, at *6 (finding that RESPA "clearly requires that a disputing party give specific 'reasons' for claiming that an account it in error."); *Banayan v. OneWest Bank F.S.B.*, 2012 U.S. Dist. LEXIS 35301, at *15 (S.D. Cal. 2012) (finding that a qualified written request must seek information "relating to the servicing of a loan."). Thus, because this e-mail did not provide any statement of reasons for Shaw's dispute with CMI regarding his mortgage account, the July 31, 2011 e-mail does not constitute a Qualified Written Request. *Pettie*, 2009 U.S. Dist. LEXIS 4149, at *7. Similarly, the court finds that Shaw's June 20, 2012 e-mail to Orcutt likewise did not constitute a Qualified Written Request. That e-mail only complains of Orcutt's failure to provide information about CMI's reinstatement offer and references several telephonic conversations. *See* Pl. Trial Ex. 36. But, like Shaw's July 31, 2011 e-mail, the June 20, 2012 e-mail does not provide any statement of the reasons for Shaw's dispute with CMI or the ongoing problems with his mortgage account. Thus, as with the July 31, 2011 e-mail to Gabbert, the court finds that Shaw's June 20, 2012 e-mail to Orcutt does not constitute a Qualified Written Request.

As for Shaw's remaining alleged Qualified Written Requests - the December 5, 2011 e-mail; January 3, 2012 e-mail; January 20, 2012 letter to Dana Ross; and the January 29, 2013 formal letter to CMI - the court finds that these document did constitute Qualified Written Requests

sufficient to trigger CMI's investigation and response duties under RESPA. In his December 5, 2011 e-mail to Ross, Shaw specifically laid out in detail the parties' dispute over his mortgage account and also requested various documents from CMI including contact information for the current owner of his loan, a copy of the original mortgage note and deed of trust, and copies of any assignment of the mortgage note and deed of trust, if any. *See* Def. Trial Ex. 512-A. Similarly, the January 3, 2012 e-mail to Ross references CMI's lack of response to the December 5, 2011 e-mail, and again details the parties' dispute including CMI's ongoing collection attempts, and requests relevant loan documents and owner information. Pl. Trial Ex. 24. Likewise, the formal letter Shaw sent to Ross on January 20, 2012, contained similar information about the parties' dispute and requested loan documents and contract information for the owner of his loan. Pl. Trial Ex. 26, P00067-69. Finally, the January 29, 2013 e-mail contained similar dispute information and demanded documentation from CMI. Such communications constitute Qualified Written Requests under RESPA. *Pettie*, 2009 U.S. Dist. LEXIS 4149, at *6; *Banayan v. OneWest Bank F.S.B.*, 2012 U.S. Dist. LEXIS 35301, at *15 (finding that a letter which contained "an extremely detailed account of various communications between the two parties" constitutes a qualified written request).

Now that the court has found that four of Shaw's written communications were Qualified Written Requests sufficient to trigger CMI's investigation and response duties under RESPA, the court must determine whether CMI's response to those requests, if any, was in accordance with its duties under RESPA. Initially, the court finds that CMI did not even respond to or acknowledge Shaw's December 5, 2011 Qualified Written Request. This lack of acknowledgment of the request is, itself, a violation of RESPA. *See* 12 U.S.C. §2605(e)(1)(A) (stating that a loan servicer "shall provide a written response acknowledging receipt of the correspondence . . . ."). CMI's failure to acknowledge receipt of Shaw's Qualified Written Request, as evidenced by the January 3, 2012 e-mail to Ross which references CMI's lack of response, was a direct violation of its duties under RESPA.

The court finds that CMI likewise violated its duties under RESPA as it relates to the January 3, 2012 Qualified Written Request. Although Dana Ross properly acknowledged this request in a January 5, 2012 e-mail to Shaw, CMI did not appropriately respond to the request after the investigation period. The evidence establishes that CMI's only response to Shaw's January 3, 2012 Qualified Written Request was a January 9, 2012 letter advising Shaw that non-party Aurora was the current owner of his residential loan and provided contact information for Aurora. Pl. Trial Ex. 25, P00066. However, at no point within sixty (60) days after receiving Shaw's request did CMI provide any of the loan documents that had been requested. CMI's failure to provide these documents to Shaw is a direct violation of RESPA. *Pettie*, 2009 U.S. Dist. LEXIS 4149, at *7.

After receiving CMI's January 9, 2012 letter identifying Aurora as the current owner of his loan, Shaw contacted Aurora at the contact information provided by CMI. Aurora advised Shaw that it was not the owner of his loan at which point Shaw again contacted CMI as outlined in his January 20, 2012 Qualified Written Request. *See* Pl. Trial Ex. 26, P00067-69. Similar to Shaw's December 3, 2011 request, CMI did not acknowledge receipt of Shaw's January 20, 2012 request. As addressed above, this failure by CMI is a violation of its duties under RESPA. 12 U.S.C. §2605(e)(1)(A). Further, the only response to Shaw's request was a February 13, 2012 letter from CMI again identifying non-party Aurora as the owner of Shaw's residential loan. Pl. Trial Ex. 31, P00099. However, by that point Shaw had already informed CMI that Aurora was not the owner of his residential loan. Thus, the information CMI provided, stating that Aurora was the current owner of his loan, was false information. CMI's failure to provide Shaw correct contact information for the owner of his loan is an express violation of RESPA. *See* 12 U.S.C. §2605(k)(1)(D) (stating that a loan servicer shall provide "the identity, address, and other relevant contact information about the owner of assignee of the loan" when requested by the borrower). Further, once again, at no point did CMI provide Shaw with any of the loan documents that he had been requesting since December 5, 2011. As addressed above, this is also a violation of RESPA. *Pettie*, 2009 U.S. Dist. LEXIS 4149, at *7.

Shaw's last Qualified Written Request was his January 29, 2013 Qualified Written Request. Attorney Joseph Bleeker, CMI's counsel of record at that time, acknowledged Shaw's request within the twenty day time period and stated that CMI would be responding to Shaw's request within the requisite sixty (60) days time period. *See* Pl. Trial Ex. 39, P00123-124. Further, in contrast to CMI's prior responses, or lack of responses to Shaw's requests, CMI sent Shaw a package on March 6, 2013, from Kristin Dennis, a Default Research Specialist at CMI. Pl. Trial Ex. 43, P00139-187. The court has reviewed CMI's response and finds that it properly and appropriately complied with its duties under RESPA. The package included copies of all of the documents that Shaw requested, provided a detailed explanation for CMI's actions on Shaw's mortgage account, and explained the reasons for any lacking information. As such, the court finds that CMI did not violate RESPA as it relates to Shaw's January 29, 2013 Qualified Written Request. *See, e.g., Pettie*, 2009 U.S. Dist. LEXIS 4149, at *7.

Based on the evidence presented at trial, the court has found that CMI violated RESPA on three separate occasions when dealing with Shaw's various Qualified Written Requests. A plaintiff who establishes that a servicer violated RESPA is entitled to recover "any actual damages" that the plaintiff suffered as a result of the defendant's violation and statutory damages. 12 U.S.C. §2605(f)(1)(A) & (1)(B). RESPA's "actual damages" are limited to pecuniary damages. *Zeich v. Select Portfolio Servicing, Inc.*, 2015 U.S. Dist. LEXIS 151519, at *5 (D. Or. 2015). Here, Shaw has not proven any actual damages as a result of CMI's violations of RESPA. In contrast to Shaw's claim for tortious breach of the implied covenants, under RESPA a plaintiff "cannot recover for worry, concern, or frustration." *Id.* Thus, the court finds that Shaw is not entitled to any actual damages. Instead, Shaw's damages award for CMI's violations is limited to statutory damages. Under RESPA, statutory damages may not exceed $2,000.00. 12 U.S.C. §2605(f)(1)(B). Here, the court finds that such a statutory maximum is warranted based on the repeated pattern of CMI's failure to appropriately respond to Shaw's Qualified Written Requests and the fact that Shaw was never once provided correct contact information for the owner of his residential loan. Accordingly,

the court shall enter judgment in the amount of $6,000.00 favor of Shaw and against CMI on Shaw's claims for violation of RESPA.

E. Intentional Interference

In Nevada, a claim for intentional interference with prospective economic advantage requires a plaintiff establish: "(1) a prospective contractual relationship between the plaintiff and a third party; (2) knowledge by the defendant of the prospective relationship; (3) intent to harm the plaintiff by preventing the relationship; (4) the absence of privilege or justification by the defendant; and (5) actual harm to the plaintiff as a result of the defendants' conduct." *Fagin v. Doby George, LLC*, 2011 U.S. Dist. LEXIS 86389, at *15 (D. Nev. 2011) (citing *Wichinsky v. Mosa*, 847 P.2d 727, 729-30 (Nev. 1993)); *see also Barket v. Clarke*, 2012 U.S. Dist. LEXIS 88097 (D. Nev. 2012).

The court has reviewed the evidence submitted at trial in this matter and finds that Shaw has failed to prove his claim for intentional interference with prospective economic advantage by a preponderance of the evidence. Shaw's claim for intentional interference with prospective economic advantage relates solely to CMI's alleged failure to approve a short sale of the McFaul Court property in a timely manner, which stigmatized the property for potential buyers and caused a devaluation of the property. Although it is undisputed that Shaw had entered into four (4) separate short sale contracts on the McFaul Court property with two different parties, the Knapps and the Smiths, and that CMI had knowledge of these short sale agreements because Shaw had forwarded all four accepted short sale offers to CMI, the court finds that Shaw has not proven that CMI intended to harm Shaw by either denying the short sale offers or not responding to the short sale offers in a timely manner. At trial, Shaw only established that CMI did not respond to any of the four short sale offers in a timely manner thereby causing all four offers to expire under their terms. However, Shaw failed to provide any evidence that CMI's delay was specifically intended to cause the proposed buyers to walk away from the McFaul Court property or to cause harm to Shaw.

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Further, the court finds that Shaw has not proven that CMI, as the servicer of his loan who had final approval on all short sales of the property, was not justified in its conduct. Initially, the court notes that CMI was justified in any delay in its responses to the two Knapp Offers because Shaw did not provide all necessary documents to CMI for it to properly evaluate and respond to these offers. It is undisputed that after receiving the first Knapp Offer, CMI requested various documentation from Shaw including: (1) a hardship letter; (2) a signed purchase agreement (as the original offer had expired in late February 2013); (3) Shaw's tax returns for the tax years 2011 and 2012; (4) all payoffs for the junior liens on the property within the last sixty days, if any; or, (5) if the junior liens still needed to be paid off, then approval letters of the short sale by each junior lien holder and releases of their junior liens; (6) the 2011 real estate tax bill for the McFaul Court property; and (7) a hazard insurance policy on the property. Def. Trial Ex. 525-A. Shaw submitted, and re-submitted, all requested documents except for signed releases from the junior lien holders. Shaw testified at trial that he had prepared appropriate junior lien holder releases including a consent to judgment in favor of non-party Katherine Barkley and a stipulated monetary judgment in favor of non-party Janice Shaw so that CMI could evaluate the Knapp Offers. However, both Katherine Barkley and Janice Shaw testified that they did not have any conversations with Shaw regarding the various short sale offers on the McFaul Court property, had not agreed to any short sale offers on the property, and had not agreed to release their junior liens or signed any paperwork releasing their junior liens. Further, Shaw did not provide the "judgment" documents to CMI and CMI never received any release documents signed by the junior lien holders. Accordingly, the court finds that CMI did not have any duty to approve, or even respond to, the Knapp Offers in a timely manner as Shaw failed to provide all required documents.

As to the first and second Smith Offers, the court finds that Shaw was not required to provide any releases from the junior lien holders for CMI to consider these short sale offers because under both offers, the junior lien holders were being paid in full. However, the court finds that because CMI had final authority to approve the short sales, Shaw has not established that under the

short sales he had reasonable expectations of any economic advantage under these offers. Generally, a loan servicer like CitiMortgage has no duty to approve a short sale. *See Blanford v. Suntrust Mortgage, Inc.*, 2012 U.S. Dist. LEXIS 141666, at *11 (D. Nev. 2012). Further, as the servicer of Shaw's loan, all short sale offers had to be approved by CMI, thus, even though Shaw accepted the short sale offers, he did not have any true prospective economic benefit from these offers. For example, if CMI declined both Smith Offers, then Shaw would not have received any economic benefit as a matter of law because the McFaul Court property could not be sold at an amount less than Shaw's remaining indebtedness without CMI's permission. The court cannot now say that simply because CMI took no action on the offers, rather than deny them outright, that Shaw would have received an economic benefit. As CMI had no duty to respond,[17] a lack of response which caused the offers to lapse would constitute the same action as a denial and thus, not be actionable for an intentional interference with prospective economic advantage. As CMI has no duty to approve, act on, or even acknowledge any short sale offers Shaw received on the McFaul Court property, the court finds that Shaw has failed to prove he had a prospective economic advantage under the contracts as the determination of whether to allow the property to be sold at short sale was solely within CMI's control. Further, the testimony at trial establishes that the two Smith Offers were not reasonable short sale offers, such that the court cannot find that CMI's lack of response on these offers was designed to intentionally cause harm to Shaw or was not justified. At trial, Attorney Dodrill testified that CMI would not have approved either Smith Offer as both

[17] At trial, Shaw argued that CMI created a duty to respond to the Smith Offers in a timely manner by specifically requesting that Shaw re-list the McFaul Court property for sale and forward all accepted short sale offers directly to Attorney Colt Dodrill, CMI's counsel of record at that point. However, the court has reviewed the evidence submitted at trial and finds that it does not support Shaw's argument or interpretation of the December conversation that Shaw had with Attorney Dodrill. Attorney Dodrill testified that he told Shaw that if he accepted any short sale offers on the McFaul Court property that such offers should be submitted directly to him as counsel of record for CMI, but did not tell Shaw to put the property back up for sale or that he would be able to handle any short sale offers. Instead, Attorney Dodrill testified that Shaw needed to submit any offers to him directly because by that point in time, Shaw had initiated litigation against CMI and was not allowed to directly contact CMI as an adverse party. Thus, the court finds that based on this testimony, CMI did not create a specific duty to respond to the Smith Offers.

offers proposed to pay off both junior lien holders in full and give Shaw $75,000 while CMI lost roughly $500,000 in the sale of the McFaul Court property. Attorney Dodrill further testified that CMI had never approved a short sale in such a situation and that no short sale offer which allowed for the borrower to receive money would be approved. Therefore, the court finds that CMI was justified in not responding to these short sale offers as such offers were not reasonable offers for the purchase of the property. Accordingly, based on all of the evidence presented at trial, the court finds that Shaw has not established by a preponderance of the evidence that CMI engaged in conduct that intentionally interfered with any prospective economic advantage. The court shall enter judgment in favor of CMI and against Shaw on this claim.

F. Punitive Damages

In his second amended complaint, Shaw seeks punitive damages for CMI's conduct outlined in this action. ECF No. 109. Punitive damages are not available in contract-based claims. *See* NRS §42.005(1) (stating that punitive damages are available in any action "for the breach of an obligation not arising from contract"). Thus, the only claim for which punitive damages could be awarded in this action is Shaw's claim for tortious breach of the implied covenants of good faith and fair dealing.

Under Nevada law, in order to recover punitive damages, a plaintiff must show the defendant acted with oppression, fraud or malice. *Pioneer Chlor Alkali Co. v. National Union Fire Ins. Co.*, 863 F.Supp. 1237, 1250 (D. Nev. 1994). Oppression is a conscious disregard for the rights of others constituting cruel and unjust hardship. *Id.* at 1251 (citing *Ainsworth v. Combined Ins. Co. of America*, 763 P.2d 673, 675 (Nev. 1988)). "Conscious disregard" is defined as "the knowledge of the probable harmful consequences of a wrongful act and a willful and deliberate failure to act to avoid those consequences." NRS §42.001(1). Malice is conduct which is intended to injure a person or despicable conduct which is engaged in with a conscious disregard of the rights and safety of others. *See* NRS §42.005(1). In order to establish that a defendant's conduct constitutes conscious disregard, the conduct must at a minimum "exceed mere recklessness or gross

negligence." *Pioneer Chlor Alkali Co.*, 863 F.Supp. at 1251; *see also Countrywide Home Loans, Inc. v. Thitchener*, 192 P.3d 243, 255 (Nev. 2008) (holding that conscious disregard requires a "culpable state of mind" and therefore "denotes conduct that, at a minimum, must exceed mere recklessness or gross negligence.").

Based upon the substantial factual history in this action, and recognizing that CMI is a large home loan servicing company, the court finds by clear and convincing evidence that CMI's business practices and its specific conduct toward Shaw constituted oppression and a conscious disregard for Shaw's rights warranting punitive damages. Given the fact that Shaw's debt of over $900,000 was for his home, that a home is most Americans greatest asset and also greatest liability and is such an integral part of any homeowner's personal well being, the court finds that a homeowner is particularly vulnerable as a result of a tortious breach of the implied covenant of good faith and fair dealing oppressively committed by a large corporate servicing company such as CMI.

Here, there was a willful and unconscionable failure to avoid needless and harmful consequences in refusing to honor or recognize the May 2011 Modification Agreement (executed by CMI's Vice-President in May 2011). CMI's conduct in recognizing then continuously disavowing that agreement - despite a resolving document from CMI's Assistant General Counsel - was made with a conscious disregard for the harm that it was causing Shaw. Further, there was a willful and deliberate failure by CMI to avoid these consequences. Accordingly, the court finds that this is an appropriate case for punitive damages.

The court has already cited many of the factors that support the court's finding within the findings of fact and tortious breach of the implied covenants section of this order and those factors find equal weight here. But, the court now highlights several factors which particularly stand out in support of punitive damages and which have not been more specifically addressed. These include CMI's lack of policies, procedures, practices and management oversight in handling mortgage account issues such as Shaw's. The lack of company policies and management oversight in this

action allowed CMI, through its Loss Mitigation, underwriting, and Executive Response Unit departments, to take the offensive position that CMI was entitled to require Shaw to abandon the fully executed May 2011 Modification Agreement in favor of the proposed July 2011 Modification Agreement despite upper management and assistant general counsel taking inconsistent and contrary positions. In essence, CMI chose to ignore its own agreement (and its own corporate counsel) because the company was aware that a financially strapped homeowner who was in default on a home loan during the post-recession economic downturn was in no position to hold CMI to the agreement it had unilaterally chosen to ignore. Given the obvious effects such a position would have upon any borrower/homeowner and the lack of any bargaining position to challenge CMI's position, it is clear that there would be dramatic and harmful consequences to a borrower which would cause feelings of utter frustration, worthlessness, and shame - shame and fear over losing a home - at the very time that the borrower was likely experiencing an insurmountable burden of debt. A non-attorney borrower would likely have caved in to CMI while an attorney like Shaw chose instead to rely upon his contract, though not without obvious compensable injury.

Beyond the above, the court also finds that there was a serious lack of practices, policies and procedures to deal with and explain the company's positions and actions to the borrower/homeowner. Here, despite repeated requests for information as to why Shaw received contradictory and inconsistent communications, CMI never provided any meaningful explanations. Moreover, CMI's responses to Shaw's requests for identification of his loan holder, including both those that qualified under RESPA and those that did not qualify, show a lack of policy and procedure to identify to a borrower/homeowner the creditor (whom CMI was representing) who owned the loan and how the creditor might be contacted. These are just a few examples of CMI's lack of centralized management policy and speak to the very core of CMI's conscious disregard of Shaw's rights. Significantly, even after going through a full trial, there has been no identification by CMI of the owner of Shaw's loan.

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CMI's failures in this action are exacerbated by the frustration and unexplained revolving door of CMI personnel with whom Shaw was required to deal. Just during the time period from May 2011 through July 2012 when CMI effectively stopped communication with Shaw concerning his mortgage account, Shaw had dealt with two different individuals who had drafted separate modification agreements (Kim Vukovich and Juan Mayorga), three separate Homeowner Support Specialists (Chris Gabbert, Jennifer Butler, and Robert Orcutt), and CMI's Assistant General Counsel, Dana Ross, not to mention the myriad of unnamed employees Shaw contacted in 2011 through 2012. And there was commonly no meaningful explanation of why a new person, new department, or some other representative was being identified as the person with whom Shaw was now required to deal. Moreover, the evidence established that Shaw informed each new CMI representative of the history of his mortgage account and rather than investigate the matter further - an investigation readily available through Shaw's electronic mortgage account and the documents in Shaw's and CMI's possession - these representatives continued to push forward with CMI's untenable position that there was no valid and binding loan modification under the May 2011 Modification Agreement. CMI willfully ignored the harm it was causing to Shaw despite clear warning signs from Shaw that its conduct was improper.

Another failure, previously mentioned, was CMI's inexcusably delayed recognition of the May 2011 Modification Agreement. An agreement executed by its Vice-President but then rejected by some employee in the Loss Mitigation department only to be honored by CMI's own assistant general counsel and then rejected again by an employee in the Executive Response Unit without any meaningful explanation to the borrower/homeowner and without any regard for the financial burden, frustration and stress such inconsistency placed on the borrower/homeowner is strong evidence of oppression. After three plus years of litigation and a three-day bench trial, an explanation for CMI's behavior is still unknown.

Also significant to the court in finding that punitive damages are warranted in this action is the effect of CMI's actions and lack of actions concerning Shaw's credit status. While it is clear

that he was in default on his original loan, it is also clear that he cured the default through the execution of the May 2011 Modification Agreement which subsumed all past due amounts into a new principal balance, made all payments under that agreement in a timely fashion through December 2011, and yet Shaw received negative and unreliable credit reporting by CMI throughout much of this period and afterward. Although the evidence could not show the reasons for the revocation of Shaw's credit card, and the denial for Shaw's credit applications for his daughter's student loans, the rejection of the credit application for the purchase of his son's automobile, and the rejection of Shaw's own automobile purchase, it is a reasonable conclusion that CMI's negative reporting during the periods of time when the default had been cleared contributed to Shaw's credit problems, particularly when his only negative credit issues were related to his mortgage, and would have been a factor in the shame, embarrassment, stress and frustration suffered by Shaw over the relevant time period. Taking all of these factors together, they demonstrate that CMI acted with conscious disregard of Shaw's rights and support an award of punitive damages.

In Nevada, an award of punitive damages is limited to "[t]hree times the amount of compensatory damages awarded to the plaintiff if the amount of compensatory damages is $100,000 or more." NRS §42.005(a). Here, the compensatory damages under Shaw's tortious breach of the implied covenants claim is $239,850.00 and the court finds that an appropriate amount of punitive damages for the conduct outlined above is the statutory limit. Thus, trebling this amount, the court shall enter judgment in the amount of $719,550.00 in favor of Shaw and against CMI for punitive damages.

G. Attorney's Fees

Although not presently before the court, the court notes for the benefit of the parties that it would consider a motion for attorney's fees filed by Shaw pursuant to NRS §18.010 and 12 U.S.C. §2605(f)(3), as Shaw is the prevailing party in this action under his declaratory relief, tortious breach of the implied covenants, and RESPA claims. Therefore, the court shall grant Shaw leave to

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file a motion for attorney's fees, if any, within twenty (20) days of entry of this order. Such motion shall comply with Local Court Rule 54-14.

IT IS THEREFORE ORDERED that the clerk of court shall enter judgment in favor of plaintiff Leslie Shaw and against defendant CitiMortgage, Inc. on Shaw's claim for declaratory relief and breach of contract in accordance with this order.

IT IS FURTHER ORDERED that the clerk of court shall enter judgment in the amount of $239,850.00 in favor of plaintiff Leslie Shaw and against defendant CitiMortgage, Inc. on plaintiff's claim for breach of the implied covenants of good faith and fair dealing.

IT IS FURTHER ORDERED that the clerk of court shall enter judgment in the amount of $6,000.00 in favor of plaintiff Leslie Shaw and against defendant CitiMortgage, Inc. on plaintiff's claims for violation of the Real Estate Settlement Procedures Act.

IT IS FURTHER ORDERED that the clerk of court shall enter judgment in favor of defendant CitiMortgage, Inc. and against plaintiff Leslie Shaw on plaintiff's claim for intentional interference with prospective economic advantage.

IT IS FURTHER ORDERED that the clerk of court shall enter judgment in the amount of $719,550.00 in favor of plaintiff Leslie Shaw and against defendant CitiMortgage, Inc. for punitive damages.

IT IS FURTHER ORDERED that plaintiff shall serve a copy of this order upon junior lien holders Katherine Barkley and Janice Shaw within (10) days of entry of this order.

IT IS FURTHER ORDERED that plaintiff shall have twenty (20) days from entry of this order to file a motion for attorney's fees in accordance with this order, if any.

IT IS SO ORDERED.

DATED this 17th day of August, 2016.

LARRY R. HICKS
UNITED STATES DISTRICT JUDGE