4. DISCHARGE, PLAN CONFIRMATION, CONVERSION AND DISMISSAL

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by

Barry H. Sternberg, Esq.
Law Offices of Barry H. Sternberg
4245 Union Road, Suite 101
Cheektowaga, New York 14225
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By

Jenette A. Barrow-Bosshart, Esq.
And
Scott L. Hazan, Esq.
Otterbourg, Steindler, Houston & Rosen, P.C.
230 Park Ave.
New York, NY 10169

I. EFFECT OF DISCHARGE

Dischargeable Debts

One of the primary purposes of filing a bankruptcy petition is to obtain a "fresh start" by virtue of the discharge of debts. The discharge order signifies that the debtor is given final relief from the burdensome obligations that gave rise to the bankruptcy. Code §524 provides for one of the fundamental benefits of a filing under the Code and is applicable regardless of which Chapter of the Code the case is pending under. Code §524(a)(1) voids any judgment to the extent the judgment is a determination of personal liability. Likewise, all other claims for payment are dischargeable unless specifically made non-dischargeable under §523(a), §727, §944, §1141, §1228 and §1328 of the Code. It is important to note that only those debts incurred prior to the filing date of the petition are discharged. The debtor remains responsible for the payment of any post-petition obligations. Before filing the petition, counsel should verify that the debtor is not expected to incur significant obligations in the near future, such as continuing uninsured medical bills which would not be dischargeable.

The practical effect of the discharge order is that creditors are enjoined under Code §524(a)(2) from any future attempt to collect on a discharged debt. A creditor who willfully violates the discharge injunction can be subject to the assessment of costs and punitive damages. 11 U.S.C. 362(k)(1). The 2005 Bankruptcy Abuse Prevention and Consumer Protection Act (hereinafter "2005 Act") amended §524 to provide that the willful failure of a creditor to credit payments received under a confirmed reorganization plan shall constitute a violation of the discharge injunction to the extent that the failure to properly credit payments results in a material injury to the debtor. See 11 U.S.C. 524(i).

The 2005 Act carved out an exception to the discharge injunction under §524(j), which allows creditors possessing a security interest in real property that is the debtor's principle residence from being enjoined from acts seeking to obtaining periodic payments in the ordinary course of business in lieu of in rem proceedings to enforce the lien. See Generally 11 U.S.C. 524(j).

Reaffirmation Agreements

The debtor may choose to reaffirm a debt that would otherwise be dischargeable to keep collateral or for some other valid reason. Many debtors, for instance, wish to maintain a relationship with their credit union, thus would be willing to reaffirm an unsecured debt in exchange for continued membership privileges. Reaffirmation agreements are valid only if made prior to the discharge. Once entered into, a reaffirmation agreement can be rescinded at any time prior to the discharge, or within two months from the date the agreement is filed with the court, whichever is later. 11 U.S.C. 524(c)(4). Once the time limitation for rescission has expired, however, the debtor can no longer claim the reaffirmed debt to be discharged under the bankruptcy filing. However, Code §524(f) makes it clear that a debtor may continue to make voluntary payments.

The 2005 Act has significantly overhauled the requirements for reaffirmation agreements in an effort to curb perceived abuses of the reaffirmation process. See Generally 11 U.S.C. 524(k). The 2005 Act includes official reaffirmation agreement forms with more comprehensive disclosure requirements, and requires a statement by the debtor in support of the agreement, acknowledging that the reaffirmation will not impose an undue hardship on the debtor or debtor's dependents. An undue hardship is presumed where the debtor's net monthly income is less than the scheduled payments under the reaffirmation agreement. Where there exists a

presumption of an undue hardship the court must approve the agreement, although this subsection does not apply to a reaffirmation with a credit union.

Chapter 13 Super Discharge Eliminated

The so-called Chapter 13 "super discharge" was eliminated under the 2005 Act, thus removing a common reason for many bankruptcy practitioners to previously recommend Chapter 13 over Chapter 7 to many of their clients. The super discharge had allowed debtors to take advantage of the more limited exceptions to discharge in Chapter 13 found under §1328. Prior to the 2005 Act, where the debtor had lower income and minimal non-exempt assets, it was often advantageous for the debtor to offer a minimal repayment to unsecured creditors under the plan in exchange for discharging debts that may otherwise have been non-dischargeable in Chapter 7. Debtors no longer have this option. Code §1328 now makes the provisions for dealing with exceptions to discharge almost identical under both Chapter 7 and Chapter 13. It is ironic that the 2005 Act, which intends on steering more debtors into Chapter 13 plans, has also eliminated one of the primary advantages for debtors choosing to file a Chapter 13 case.

Treatment of Unfiled Secured Claims After Chapter 13 Discharge

Proposing to pay a secured creditor through the plan to allow the debtor to retain collateral does not necessarily guarantee that the claim will, in fact, be paid through the plan. Unless, either the secured creditor or the debtor files a proof of claim with the court, the Chapter 13 Trustee cannot distribute payments to the secured creditor under the plan.

The debtor usually will not care whether an unsecured creditor files a proof of claim. Many unsecured creditors simply do not bother to file their claims in minimal repayment plans. This results in a benefit to the debtor, who may end up paying less over the plan duration than

originally proposed.[1] The unsecured creditor who fails to file a timely claim, furthermore, loses the ability to collect on the claim once the Chapter 13 debtor receives a discharge. See 11 U.S.C. 524(a)(2).

The *secured* creditor failing to file a claim, on the other hand, does not lose out completely. Secured creditors may still retain their lien post-discharge on their collateral, regardless of whether a proof of claim had not been filed. The discharge order may bar the creditor from collecting on the balance of the underlying note, but does not prevent the secured creditor from exercising the right to recover the collateral if an outstanding balance remains unpaid after the plan is completed. Note that §501(c) gives the debtor the option of filing a proof of claim on behalf of the creditor to ensure that a large balance does not remain unpaid on a secured debt after the discharge.

Revocation of Discharge

It is possible for the discharge order to be revoked after being entered. In Chapter 7 cases, §727(d) provides that a discharge can be revoked on motion of a creditor, trustee or the United States Trustee within one year of the discharge being granted, or before the case is closed, whichever is later. A discharge can be revoked if the discharge was obtained through fraud, and the requesting party was unaware of the fraud prior to the granting of the discharge; or after the discharge the debtor acquires property of the estate that is not reported or turned over to the trustee; or if the debtor refuses to obey any lawful order of the court or refuses to testify other than on self-incrimination grounds unless given immunity. The 2005 Act provided an additional

[1] Some jurisdictions will not let the debtor benefit in this way, and will increase the percentage amount on claims to the other unsecured creditor who have filed claims to make up the difference in the amount the debtor had originally proposed to pay.

ground for revocation of a Chapter 7 discharge for failure to comply with an audit authorized under §586(f), or failure to satisfactorily explain a material misstatement

In Chapter 13 cases, a discharge can be revoked on request of a party in interest within one year after the discharge is granted if, after a notice and hearing, it can be shown that the discharge was obtained by the debtor through fraud, and the requesting party was unaware of the fraud prior to the granting of the discharge. 11 U.S.C. 1328(e).

Note that the grounds for revocation of a Chapter 13 discharge are narrower than grounds for revocation under Chapter 7. However, the parties authorized to request a revocation of a discharge are broader in Chapter 13. Any party in interest can request a revocation in Chapter 13, while a Chapter 7 request for revocation can only be made by a creditor, trustee or the United States Trustee.

Chapter 13 Hardship Discharge

Occasionally, a Chapter 13 debtor may be eligible to receive a hardship discharge before the scheduled completion of all payments under the plan. The debtor must meet three criteria. The debtor must show that the failure to complete plan payments is due to circumstances that the debtor cannot justly be held accountable; and the debtor has already made payments to unsecured creditors through the plan that at least equal the amount unsecured creditors would have hypothetically received if the debtor's non-exempt assets were liquidated in a Chapter 7 case; and modification of the plan is not practicable. See 11 U.S.C. 1328(b).

II. OBJECTIONS TO DISCHARGE AND DISCHARGEABILITY

Public policy considerations operate to prevent the discharge of certain types of debts in bankruptcy. Likewise, policy considerations may compel the denial of a debtor's entire

discharge under certain circumstances. Code §523(a) codifies the dischargeability of specific types of debts under Chapters 7, 11, 12 and 13 of the Bankruptcy Code, while §727(a) enumerates several grounds on which an objection can be brought seeking to deny the debtor an entire discharge of all debts in a Chapter 7 proceeding. A denial of a discharge under §727(a) could be particularly vexing for a debtor, who suffers the liquidation of assets without any corresponding benefit of receiving a discharge of debts.

A. <u>Exceptions to Discharge Under 523(a)</u>

Initially, it is important to note that the most types of debts covered under §523(a) are excepted from discharge without the creditor having to take specific action in the bankruptcy proceeding. Under §523(c)(1), however, creditors seeking to have debts excepted from discharge under §523(a)(2) *(false pretenses, active fraud or fraudulent statements other than concerning the debtor's or an insider's financial condition), (4) (embezzlement, larceny or fiduciary misstatements) or (6) (willful and malicious injury)* must act within 60 days after the first date set for the §341 meeting of creditors by filing an adversary proceeding seeking to determine dischargeability of the debt. See Bankruptcy Rule 4007. The federal courts retain exclusive jurisdiction to determine the dischargeability of debts alleged to fall under these categories. Unless the creditor acts within the time limitations imposed, the debts will be discharged upon the conclusion of the case, and there can be no further review of the dischargeability of those debts in a subsequent state court review. However, a bankruptcy case once closed can be reopened for "cause" to consider the dischargeability of a debt. See Bankruptcy Rule 4007.

Conversely, other types of discharge exceptions under §523(a) do not limit the creditor to a determination of dischargeability within the bankruptcy proceeding. A determination of non-dischargeability may often arise in the context of a subsequent state court proceeding absent any ruling by the bankruptcy court. A typical example may include a determination concerning dischargeability of marital obligations (now termed a domestic support obligation under the 2005 Act) in a state court enforcement proceeding.

In a federal court determination of dischargeability, the burden of proof rests with the creditor seeking to have a debt exempted from discharge. The legal standard the creditor must meet is a preponderance of the evidence. *Grogan v. Garner*, 498 U.S. 279, 111 S.Ct. 654. In determining whether a particular debt falls within one of the exceptions to discharge the court should strictly construe the statute against the objecting creditor, and liberally in favor of the debtor. See *Equitable Bank v. Miller (In re Miller)*, 39 F.3rd 301 (11th Cir. 1994); *In re Tully*, 18 F.2d 106 (1st Cir. 1987). If the creditor brings an adversary proceeding under §523(a)(2) and is unsuccessful, the court may grant costs and reasonable attorney fees to the debtor if the court finds that the position of the creditor was not substantially justified, unless there are special circumstances that would make such an award against the creditor unjust. 11 U.S.C. §523(d).

Either the creditor or the debtor may file an adversary proceeding to determine dischargeability in the bankruptcy court. The types of debts that may be excepted from discharge under §523(a) are summarized below:

Tax or Customs Duty

Code §523(a)(1)(A) excepts any taxes that are entitled to a priority in distribution under §507(a)(2) or §507(a)(8). This generally includes taxes that become due in the ordinary course of the debtor's business, such as employment, certain property taxes, excise, withholding and

customs duties. It would also include the debtor's personal income taxes if it is for a return, if required, that was last due, including extensions, three years before the date of the filing of the petition; and was assessed within 240 days before the date of the filing of the petition, exclusive of (I) any time during which an offer in compromise with respect to that tax was pending or in effect during that 240-day period, plus 30 days; and (II) any time during which a stay of proceedings against collections was in effect in a prior case under this title during that 240-day period, plus 90 days. See 11 U.S.C. 507 (a)(8).

Code §523(a)(1)(B) prohibits the discharge of the debtor's income taxes, even if otherwise dischargeable under §507(a)(8), if the debtor never filed the return, or the return was not filed at least two years prior to the filing of the bankruptcy petition.

A further limitation on the discharge of income taxes is provided under §523(a)(1)(C), where the debtor makes a fraudulent return or willfully attempts in any manner to evade or defeat the tax. Note that in determining whether the debtor's personal income taxes are dischargeable it will necessary to read all three subsections of §523(a)(1) together with §507(a)(8).

Debts Obtained by False Pretenses or Fraudulent Statements

Code §523(a)(2) provides three provisions on which to base an objection on fraud or misrepresentation. The first, and perhaps the most commonly encountered objection to discharge, is found under §523(a)(2)(A), and excepts debts from discharge to the extent obtained by false pretense, a false representation, or actual fraud. It should be noted that debts obtained by a false *written* statement are specifically excluded under this subsection, and are covered separately under §523(a)(2)(B).

There has been much debate on the correct legal theory courts should utilize in finding misrepresentation or fraud under §523(a)(2)(A), especially where the case involves a credit card

transaction. A majority of bankruptcy courts believe that the Supreme Court decision of *Fields v. Mans*, 116 S.Ct. 437 (1995) implicitly requires an application of the five elements of common law fraud to determine dischargeability. Although the *Mans* case did not specifically involve a credit card transaction, most, but not all courts, feel compelled by precedent to apply common law fraud analysis to credit card cases.

The bankruptcy courts, however, have had difficulty in adapting common law fraud theory to credit card transactions. Typically, credit card transactions involve tendering payment to a third party merchant, and not directly to the card issuing lender, thus the required common law element of a direct representation to the lender of an intent to repay is missing. While the Second Circuit has not directly ruled on the issue, the weight of authority favors the so-called "implied representation theory," where a legal fiction is imposed to find that each time a debtor uses a credit card the debtor makes an implied, if not actual, representation of an ability and intent to repay the debt.

The second sub-provision, §523(a)(2)(B), as mentioned above, specifically pertains to misrepresentations made in writing. The writing must be a materially false written statement respecting the debtor's or an insider's financial condition, on which the creditor reasonably relied, and on which the debtor published with an intent to deceive.

The third sub-provision, §523(a)(2)(C), sets up what is commonly referred to as a "presumption period," where certain types of debts over a set amount incurred within a short time period prior to the filing are presumed to be non-dischargeable. The 2005 Act bolstered this section for the benefit of creditors by both reducing the amount of debt, and lengthening the time period triggering the presumption of non-dischargeability. Code §523(a)(2)(C)(i)(I) provides that consumer debts owed to a single creditor for luxury goods or services aggregating more than

$600, and incurred within 90 days of filing the petition are presumed to be non-dischargeable.[2] Luxury goods and services do not include goods or services reasonably necessary for the support of the debtor or debtor's dependents. See 11 U.S.C. 523(a)(2)(C)(i)(I).

§523(a)(2)(C)(i)(II) now provides that cash advances under an open ended credit plan aggregating more than $875 obtained within 70 days of the filing are presumed to be non-dischargeable.[3] The legislative intent of §523(a)(2)(C) was to alleviate concern that debtors may go on a shopping spree before filing. The effectiveness of the provision, however, may be somewhat debatable. As a practical matter, a debtor inclined to abuse the spirit of the Code in this manner could simply delay filing for three months. It should also be noted that the presumptions can be rebutted by the debtor. Thus, a showing by the debtor of changed circumstances, or some other reason aside from false pretenses, could still allow the court to find the debt dischargeable.

Unscheduled Debts

If the debtor fails to schedule certain creditors on the petition, under certain circumstances the debt owed to those creditors may not be dischargeable. Code §523(a)(3)(A) provides that an unscheduled debt, other than under §523(a)(2), (4) or (6), will not be discharged if the debtor is aware of the creditor, and yet does not schedule the debt in time for the creditor to file a timely proof of claim. This provision will not apply, however, where the creditor otherwise had notice or actual knowledge of the bankruptcy in time to make a timely filing of a proof of claim. The essence of the provision is to protect the creditor's ability to receive a

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[2] The presumption limits were formerly set at $1,225 for luxury goods and services within 60 days of filing the petition under the prior code provisions.

[3] The presumption limits were formerly set at $1,225 for cash advances within 60 days of filing the petition under the prior code provisions.

distribution under the bankruptcy. The weight of authority holds that where the creditor's right to receive a distribution is not affected by the debtor's inadvertent failure to schedule the debt, such as in a no-asset case, or where the deadline for the filing of proofs of claims has not been set, then the debt will still be dischargeable.

Unscheduled creditors, who may have otherwise lost the opportunity to have a debt declared non-dischargeable under §523(a)(2), (4) or (6) resulting from lack of timely notice, may have grounds for the denial of dischargeability without considering the merits of the creditor's claim after the case is closed. Most jurisdictions would probably allow the case to be re-opened to allow the creditor to file an adversary proceeding to determine dischargeability, rather than penalize the debtor for an inadvertent omission on the schedules.

Code §523(a)(3)(A) places the burden on the creditor to take affirmative measures to file a proof of claim once the unscheduled creditor becomes aware of the bankruptcy. Thus, an unscheduled creditor, having knowledge of the bankruptcy, cannot elect to sit back and wait until after the distribution to allege the debt to be non-dischargeable. This would presumably prevent a creditor entitled to less than full repayment under the distribution from seeking a strategical advantage by waiting out the bankruptcy proceedings, then trying to collect on the entire debt.

Fiduciary Fraud, Embezzlement or Larceny

Section §523(a)(4) excepts debts for fraud or defalcation "while acting in a fiduciary capacity, embezzlement or larceny." The phrase "while acting in a fiduciary capacity" qualifies the words "fraud or defalcation," and not embezzlement of larceny. The implication being that the section applies even when the debtor has committed embezzlement or larceny while not acting as a fiduciary. See Collier on Bankruptcy 16d ¶523.10. Recently, the Supreme Court in *Bullock v. BankChampaign, N.A*, 133 S.Ct. 1754 (May 13, 2013) held that the term "defalcation"

as used in the Bankruptcy Code requires a culpable state of mind, or gross recklessness, in respect to, the improper nature of the fiduciary's behavior.

For a debt to be excepted from discharge for a fraud or defalcation while the debtor acted as a fiduciary, the debt must be directly related to the fiduciary relationship. For example, a debt arising to a client from an attorney in connection with the attorney's separate real estate development business was held dischargeable despite the attorney/client relationship. *In re Young*, 91 F.3d 1367 (10th Cir. 1996).

The common law definition of larceny, and not the state law definition has been held to apply. Under the common law, larceny was defined as taking another's personal property with the intent to convert or deprive the owner of same. Code §523(a)(4) excepts debts from discharge resulting from the fraudulent appropriation of another's property, whether or not the appropriation was unlawful at the outset, and, therefore, larceny, or unlawfully appropriated by the debtor after the property was entrusted to the debtor's care, and, therefore, an embezzlement. See Collier on Bankruptcy 16d ¶523.10(2).

Domestic Support Obligations

Code §523(a)(5) now provides that debts "for a domestic support obligation" are not dischargeable. The definition of a domestic support obligation codifies some of the case law which had developed under the prior Code. For example, adding "legal guardian or responsible relative" to the standing section of who may enforce a domestic support obligation.

Debts owed by a debtor to a spouse, former spouse or a child are non-dischargeable, even when not in the nature of support, as long as the debts were incurred in the course of a divorce or separation or family court proceeding. Accordingly, the two pronged balancing test under the former §523(a)(15), which had allowed the discharge of certain marital debts made in lieu of a

property distribution, was eliminated under the 2005 Act. Presently, any marital debt, whether in the nature of support, or whether a property settlement, is now non-dischargeable. The definition of a domestic support obligation includes support debts owed or recoverable by a governmental unit. 11 U.S.C. 101(14A)(A)(ii).

Willful and Malicious Injury

§523 (a)(6) excepts debts from discharge for willful and malicious injury. The terms willful and malicious are mutually exclusive, and a plaintiff must prove both to prevail. *In re Risdale*, 286 B.R. 225 (Bkrtcy. W.D.N.Y. 2002). Willful is defined as meaning deliberate or intentional conduct. Thus, for the debt to be excepted from discharge, mere reckless or negligent conduct will not suffice. *Kawaauhau v. Geiger (In re Geiger)*, 118 S.Ct. 974 (1998). Malicious is defined as "wrongful and without just cause or excuse, even in the absence of personal hatred, spite or ill-will." *In re Stelluti*, 94 F.3d 84 (2nd Cir. 1996). Malice may be implied through the acts and conduct of the debtor in the context of the surrounding circumstances. *Id.*

The debtor must have intended that the consequence of her actions would result in the plaintiff's injury. The Supreme Court concluded in *In re Geiger*, 118 S.Ct. 974 (1998), that: "The word "willful" in (a)(6) modifies the word "injury," indicating that non-dischargeability takes a deliberate or intentional injury, not merely a deliberate or intentional act that leads to injury." The Supreme Court, moreover, held that debts arising from recklessly or negligently inflicted injuries do not fall within the compass of §523(a)(6). Only malicious injuries to the plaintiff which the debtor intended to inflict are non-dischargeable.

The cases involving the application of this section typically include the wrongful conversion of secured property or insurance proceeds, and damages awarded under tort claims. Where the creditor seeks to except a debt from discharge based on the wrongful conversion of

collateral, the gravamen of the court's inquiry usually centers around the debtor's actual knowledge of the creditor's security agreement when disposing of the collateral; a fact not always obvious to an unsophisticated debtor granting a purchase money security interest in the course of purchasing furniture or other collateral on credit through a local finance company.

Governmental Fines, Penalties and Forfeitures

Code §523(a)(7) provides that a fine, penalty or forfeiture owed to a governmental unit is non- dischargeable, provided the debt is not owed for actual pecuniary loss other than a tax penalty. The text of the statute does not distinguish between civil or criminal fines. The critical issue under this section may focus on whether the debt is for an actual pecuniary loss, which if it is, allows the debt to be dischargeable. *In re Bill*, 85 B.R. 713 (Bank. D. NJ. 1988).

Code §523(a)(7) also provides two exceptions to the discharge of tax penalties. Code §523(a)(7)(A) provides that a penalty relating to a tax is non-dischargeable to the extent that the tax itself is non-dischargeable. Code §523(a)(7)(B) provides that if the tax penalty was imposed on dischargeable taxes filed more than three years before the filing of the petition, the penalty is also discharged.

Student Loans

Student loans under §523(a)(8) are not dischargeable unless the debtor can show the repayment of the loan would be an undue hardship on the debtor and the debtor's dependents. Unless the debtor obtains a hardship determination, the discharge order will not discharge the student loan. The two issues most likely to arise would center on the definition of student loans, and how to determine whether a student loan is an undue hardship.

The definition of student loans under this provision is not limited to loans guaranteed or funded by the government. Loans guaranteed or funded by a non-profit institution are made non-dischargeable as well.[4] In fact, any obligation to repay funds received as an educational benefit, scholarship or stipend are made non-dischargeable; as well as any loan qualified as an educational loan under §221(d)(1) of the Internal Revenue Code. The provision also applies to overpayments made on loans funded or guaranteed by governmental units or non-profit institutions.

Debts owed directly to an institution for unpaid tuition are not covered under the provision, and are dischargeable. Furthermore, the institution cannot withhold the debtor's transcript for an unpaid tuition bill. The courts have ruled such action constitutes a violation of the discharge injunction. *In re Walker*, 336 B.R. 534 (Bankr. M.D.Fla. 2005).

More likely to be at issue in a typical consumer bankruptcy case is whether the repayment of student loans constitutes an undue hardship on the debtor and debtor's dependents. In the case of *Brunner v. New York State Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987), the Second Circuit outlined a three pronged test to guide courts in making an undue hardship determination. The so-called "Brunner test" is widely followed in the circuits throughout the country, and of course is binding precedent in New York. The three pronged test is as follows:

(i) the debtor cannot maintain, based on current income and expenses a minimal standard of living, if forced to repay the loan;

[4] Loans under the Health Education Assistance Loan Act ("HEAL") are controlled by 42 U.S.C. §292(g), rather than §523(a)(8). Furthermore, the National Health Services Corps ("NHSC") Scholarship Program bars the discharge of NHSC repayment obligations except in certain circumstances. 42 U.S.C. § 254(c)(3).

(ii) there are indications that the state of affairs is likely to persist for a significant portion of the repayment period; and

(iii) the debtor has made good faith efforts to repay the loans.

There is a split of authority on whether courts may find student loans partially dischargeable when the debtor has the ability to pay a portion, but not all, of the student loan debt. Some courts hold to an all or nothing approach, whereby an ability to repay at least part of the obligation will render the entire student loan debt non-dischargeable.

Debts Incurred for Death or Personal Injury Caused While Operating a Vehicle, Vessel or Aircraft While Intoxicated or under the Influence of Drugs.

Code §523(a)(9) excepts from discharge any debts incurred for death or personal injury caused while operating a motor vehicle, vessel or aircraft while intoxicated or under the influence of drugs. The provision was originally added in 1984 to prevent debtors from escaping civil liability resulting from drunk driving.

Only debts incurred for death or personal injury are non-dischargeable. Property damage claims resulting from the debtor's driving while intoxicated do not come under the reach of the provision. *In Re Wiggins*, 180 B.R. 676 (Bankr. M.D. Ala. 1995)

The statute explicitly limits the scope of the provision to the damages incurred by the debtor's operation of a vehicle, thus debts owed under a theory of vicarious liability are still dischargeable. *In re Lewis*, 77 B.R. 972 (Bankr. S.D. Fla. 1987).

Debts Denied Discharge in a Prior Bankruptcy

This provision, found under §523(a)(10), applies only to a denial or waiver of discharge under §727, other than the eight year bar to re-filing found in §727(a)(8). Accordingly, specific

debts found to be non-dischargeable under §523(a) in a prior bankruptcy may still be found dischargeable in a subsequent bankruptcy proceeding, as long as there had been no adverse ruling under §727 in the prior case.

A debt that is reaffirmed under §524 in a prior case remains dischargeable in a subsequent case because a reaffirmation agreement is not considered a waiver of discharge. *In re Loans*, 50 B.R. 801 (Bankr. W.D. Ky. 1985).

Fraudulent or Reckless Actions of the Debtor While Acting in a Fiduciary Capacity to Depository Institutions or Credit Unions

As part of the Crime Control Act of 1990, Congress enacted two provisions limiting dischargeability relating to the debtor's conduct while acting as a fiduciary in federal depository institutions. Code §523(a)(11) excepts from discharge debts arising from a final judgment or order, or by a settlement agreement of the debtor, for any debts for fraud or defalcation committed by the debtor while acting in a fiduciary capacity in a federally insured depository institution or credit union.

Code §523(a)(11) excepts those debts from discharge that arise from the debtor's malicious or reckless failure to fulfill any commitment to a federal depository institutions regulatory agency to maintain the capital of an insured depository institution. The terms "federal depository institutions regulatory agency," "insured credit union" and "insured depository institution" are all defined under §101 of the Bankruptcy Code.

Code §523(e) provides that "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 523(a)(4) or (a)(11)." The term "institutional-affiliated parties" is also defined under §101 of the Bankruptcy Code, which incorporates by reference 3(u) of the Federal Deposit Insurance Act.

Restitution

Code §523(a)(13) excepts debts for restitution arising from Title 18 of the United States Code. The section is limited by its terms to prohibiting discharge of restitution obligations only in federal prosecutions. Although it is likely that restitution arising from state court prosecutions or civil cases would be covered under another part of §523(a), such as subsection (a)(6), which excepts debts for willful and malicious injury. It should also be noted that the Chapter 13 discharge provisions under §1328(a)(3) specifically encompass restitution awarded in a state court civil or criminal action, and is therefore broader than the restitution exception codified under §523(a)(13).

Debts Incurred to Pay Certain Non-Dischargeable Debts

Code §523(a)(14) excepts debts incurred to pay a tax that would otherwise be non-dischargeable under §523(a)(1). The provision was intended to encourage lenders to advance more loans allowing debtors to pay tax obligations. In practice, lenders may not know the debtor's actual purpose when obtaining an unsecured loan, thus most lenders probably would not be aware that the discharge of the debt could be challenged.

The 2005 Act adds sections §523(a)(14A), broadening the scope of the above exception by including debts incurred to pay non-dischargeable tax liabilities to governmental units other than the federal government; and added §523(a)(14B) to prohibit discharge of debts incurred to pay fines or penalties imposed under federal election law.

Post Filing Condominium or Homeowners Association Fees

Code §523(a)(16) excepts from discharge condominium or homeowners association fees that may arise post filing as long as the debtor or the trustee has a legal, equitable or possessory

ownership interest in the condominium or homeowner lot. The current provision under the 2005 Act has been expanded from the former Code provision which had excepted these fees only if the debtor physically occupied the unit or was receiving rent from a tenant post-filing. Code §523(a)(16), however, was not changed respecting pre-filing association fees, which still remain dischargeable under the current version of the Code.

Fees Imposed on a Prisoner for Court Fees

The 2005 Act has narrowed the focus of §523(a)(17) by excepting from discharge the filing fees, costs and expenses *imposed on a prisoner* regardless of an assertion of poverty. The former version of the code, by its express language, did not limit the exception of such court fees and expenses solely to prisoners. As the original provision was part of a legislative reform regarding *in forma pauperis* prisoner litigation, it would appear that the current change was to correct a technical drafting error from the previous language. There is no evidence to suggest that Congress ever intended to broadly limit the dischargeability of court fees and costs for debts that would otherwise be dischargeable in civil actions. See Collier on Bankruptcy 16d ¶523.23.

Debts for Pension Loans

The 2005 Act has added under §523(a)(18) regarding the discharge of debts owed to pension loans and other retirement plans. The provision also clarifies that these types of loans are not to be construed as claims or debts under the Bankruptcy Code. In practice, this provision does not change the manner in which non-payment of pension loan obligations will be treated. Since the debtor essentially takes an advance on her own retirement proceeds, failure to repay the obligation has always resulted in the debtor forfeiting the unpaid funds from the balance of the accumulated pension funds, while also being assessed taxes and penalties for early withdrawal.

Debts from Violation of Federal Securities Laws

Code §523(a)(19) excepts from discharge debts resulting from the violation of either federal or state securities laws, as those laws are defined under the Securities Exchange Act of 1934. The provision also excepts from discharge any debts for "common law fraud, deceit, or manipulation in connection with the purchase or sale of any security." The provision broadly encompasses all such debts whether arising from a judgment, order, consent order, settlement agreement or decree of any federal or state judicial or administrative proceeding; and whether occurring "before, on, or after the date on which the petition was filed."

B. Denial of Discharge Under §727

Discharge Limited to Individuals

Code §727(a)(1) provides that a discharge under Chapter 7 will not be granted unless the debtor is an individual. Under this provision, various incorporated and unincorporated business associations are denied resort to Chapter 7 discharge relief. These entities, nevertheless, may use Chapter 7 for an orderly liquidation of assets and distribution to creditors.

As a Chapter 7 case would involve a complete dissolution of the business entity, a technical discharge would be unnecessary because a discharge granted to a business entity will normally not affect the liabilities of owners or officers, hence no other purpose is served by extending discharge provisions to debtors other than individuals in Chapter 7. See Norton Bankruptcy Law and Practice 2d ¶¶74:2.

The stated legislative purpose of §727(a)(1) is to avoid the trafficking in corporate shells and in bankrupt partnerships. H.R. Rep. No. 595, 95th Cong., 1st Sess. 384 (1977); S. Rep. No. 989, 95th Cong., 2d Sess. 98 (1978).

The court must provide an individual debtor a discharge unless one of the specifically enumerated grounds for denying the discharge is determined to exist. The grounds upon which a discharge may be denied are discussed below.

Fraudulent Transfers and Concealment

Code §727(a)(2) provides that a discharge will be denied if, with intent to hinder, delay, or defraud a creditor or an officer of the estate, the debtor transfers, removes, destroys, mutilates or conceals (1) property of the debtor within one year before the date of filing of the petition; or (2) property of the estate after the date of filing. Note that the Code broadly defines a transfer to include allowing the creation or foreclosure of liens, or "each mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with" property or an interest in property. See 11 U.S.C. 101(54). The discharge will also be denied if, instead of taking these actions, the debtor fraudulently "permitted" the proscribed action to occur. Four elements are involved in an objection under §727(a)(2):

1. requisite intent;
2. specified actions taken or permitted;
3. action with reference to property of the debtor or the estate; and
4. action within one year prior to filing bankruptcy or any time after the filing.

This provision is somewhat analogous to fraudulent conveyance laws, in that transfers of property that would otherwise enure to the benefit of creditors are prohibited. The main difference preventing the debtor from receiving a discharge under this subsection is the scienter requirement. In other words, where the debtor specifically intends to hinder the interests of creditors the court may conclude that the debtor's conduct warrants the denial of a discharge.

As a certain level of pre-bankruptcy planning may be allowable, §727(a)(2) suggests that a denial of discharge under this subsection would also hinge, in large part, on the degree of the debtor's conduct. The line between pre-bankruptcy planning and fraud is not clearly drawn, and must be determined on a case by case basis. An often quoted colloquial phrase may describe the court's approach to weighing the distinction: "when a pig becomes a hog it gets slaughtered." See Norton Bankruptcy Law and Practice 2d ¶¶74:4.

Inadequate or Destroyed Records

Code §727(a)(3) provides that discharge will be denied to the debtor if: "the debtor has concealed, destroyed, mutilated, falsified, or failed to keep or preserve any recorded information, including books, documents, records, and papers, from which the debtor's financial condition or business transactions might be ascertained, unless such act or failure to act was justified under all of the circumstances of the case. . . ."

Code §727(a)(3) deals with two general fact patterns. The first involves concealment, destruction, mutilation, or falsification of financial records. The second general type of activity relates to a failure to keep or preserve records. The first element reinforces the policy of prohibiting discharge in cases where the debtor has actively sought to keep property or information from the estate. The exception for failure to maintain adequate record keeping, however, does not explicitly require proof of intent to defraud, and courts have held that intent is not an element of an exception to discharge based on a failure to keep adequate records. The exception extends beyond cases in which fraudulent purpose can be established. Under this provision, it might be observed that, to qualify for a discharge, the debtor has an affirmative duty to maintain records from which his or her financial affairs and status can be reconstructed. The analysis is two part: the court first determines whether the debtor's records are sufficient and, if

insufficient, whether the failure to maintain sufficient records was justified under the circumstances of the case. See Norton Bankruptcy Law and Practice 2d ¶¶74:9. The plaintiff seeking to have the discharge denied has the burden of proof.

Wrongful Acts in the Case

Code §727(a)(4) specifies four distinct grounds for denying the debtor's Chapter 7 discharge. In general, these objections to discharge parallel actions that are elsewhere defined as bankruptcy crimes.

1) made a false oath or account;

2) presented or used a false claim;

3) gave, offered, received or attempted to obtain money, property or advantage, or promise of money, property, or advantage for acting or forbearing to act; or

4) withheld from an officer of the estate entitled to possession under this title, any recorded information, including books, documents, records and papers, relating to the debtor's property or financial affairs.

Insofar as they relate to denial of discharge, each of the objections listed in §727(a)(4) requires proof that the debtor "knowingly and fraudulently" committed the proscribed action. Thus, in each of these objections, the debtor may avoid denial of discharge by establishing that the acts in question were inadvertent, the result of negligence, or committed in good faith reliance on the advice of counsel. See Norton Bankruptcy Law and Practice 2d ¶¶74:10.

Unsatisfactory Explanations

Code §727(a)(5) establishes a general, catchall standard for denial of discharge that permits the court, in appropriate cases, to deny discharge where proof of specific facts or intent

has been impossible. Code §727(a)(5) provides that discharge will be denied where "the debtor has failed to explain satisfactorily … any loss of assets or deficiency of assets to meet the debtor's liabilities…." This provision does not provide a specific time limitation with respect to loss of assets or deficiency of assets. The objecting creditor, however, bears the burden of showing that the loss occurred "at a time not remote in time" to commencement of the bankruptcy case. Although the burden of proof is on the objecting party, the debtor must come forward with a satisfactory explanation once a loss of assets is shown.

The objection to discharge provided in this section is necessarily broad in scope with imprecise outer limits. Properly construed, the objection should not be sustained based on the substantive character of the explanation. Thus, a debtor who reports a loss of $100,000 because he or she gave that sum to his or her child cannot be said to violate Code §727(a)(5), provided that documentation of the gift is presented. Other objections may be raised regarding the transaction, but §727(a)(5) requires only an explanation of a loss or deficiency of assets, not that the explanation be meritorious. The explanation, therefore, need merely be "satisfactory." "Satisfactory" is not defined by the Code, but to be satisfactory the explanation "must convince the judge." See Norton Bankruptcy Law and Practice 2d ¶¶74:15.

Failure To Obey Orders and Testify

Several of the objections to discharge previously discussed relate to wrongful conduct of the debtor in the current bankruptcy case. In addition to these grounds for objection, §727(a)(6) places on the debtor an affirmative duty to comply with the lawful orders of the Bankruptcy Court and, when called upon, to give full and accurate testimony, as conditions for receiving a discharge in Chapter 7.

Code §727(a)(6) provides that discharge of debts will be denied if the debtor refuses, in a case:

1. to obey any lawful order of the court, other than to respond to a material question or to testify;

2. to refuse to testify or to refuse to respond to a material question approved by the court on the grounds of self-incrimination after the debtor has been granted immunity with respect to the matter for which the privilege was invoked; or

3. to refuse to testify or to refuse to respond to a material question approved by the court on grounds other than the privilege against self-incrimination.

Any lawful court order may trigger the operation of §727(a)(6)(A). For example, the court may deny the discharge of debtors violating a court order not to use insurance proceeds without court approval. On the other hand, §727(a)(6) applies to a debtor's refusal to obey, which should be distinguished from a mere failure to obey. An allegation that the debtor failed to obey, without a showing of willful or intentional disobedience, fails to state a claim.

The provisions of §727(a)(6)(B) and (a)(6)(C) regarding testimony and response to material questions approved by the court represent a change in prior law. Under the Code, a properly invoked privilege against self-incrimination is not a basis for objection to discharge. However, a material question must be answered if immunity is granted concerning the subject matter. This section does not require that immunity be granted whenever the privilege is invoked, only that the privilege may not be involved when immunity has been granted.

Although a debtor properly claiming the privilege against self-incrimination will not be denied a discharge under §727(a)(6)(C), the debtor should not be relieved of a duty to come forward with evidence once a *prima facie* case has been made by the trustee or party in interest objecting to the debtor's discharge under other subsections of §727(a). The debtor should not be

relieved, for example, of the burden to come forward with an explanation once it reasonably appears the debtor has given a false oath in a §727(a)(4) action. Code §727(a)(6)(C) should be available only as a shield, not as a sword.

The application of this objection to cases not involving the privilege may raise difficult fact questions where the debtor's answers to questions are evasive or equivocal. In extreme cases, such answers may amount to a refusal to answer. However, it has generally been held that equivocation and evasion will not normally bar discharge. Generally, §727(a)(6) does not apply to bar a debtor's discharge when the debtor's witnesses refuse to respond, or when the debtor's refusal to respond is inadvertent. Discharge should not be denied when family members of the debtor refuse to comply with a court-ordered examination, at least where the debtor has not taken an active role in arranging for the refusal. See Norton Bankruptcy Law and Practice 2d ¶¶74:16.

Insider Cases

Code §727(a)(7) applies to certain acts committed by the debtor "in connection with another case … concerning an insider." The focus, therefore, is whether the debtor in the other case is an insider of the debtor in the present case. When the debtor is an individual (only individuals are eligible for the §727 discharge), insiders include relatives of the debtor, partnerships in which the debtor is a general partner, general partners of the debtor, and corporations controlled by the debtor.

Code §727(a)(7) strengthens a court's ability to protect the bankruptcy system in general, and provides an effective means "to defeat a discharge to those who may damage the integrity of the bankruptcy system through impropriety in a prior case." For example, the court may deny the discharge of an individual Chapter 7 debtor where, as controlling officer of a Chapter 11

debtor, the individual debtor caused the corporate debtor to violate the terms of a cash collateral order in the Chapter 11 case. The other case need not actually be "prior" to the debtor's Chapter 7 case. The acts which will lead to a denial of discharge under Code §727(a)(7) may occur in another case during the debtor's own Chapter 7 case.

The term "insider" is defined in Code §101(31). Generally, "insider" refers to the relationship of the debtor to entities with whom the debtor has a close personal or business relationship, or entities that control or are controlled by the debtor. An insider, therefore, is one who has a sufficiently close relationship with the debtor to subject the debtor's conduct with respect to that insider to closer scrutiny than that accorded to conduct of those who deal at arm's length with the debtor. An insider may continue to be an insider even after resigning from a debtor corporation in the previous bankruptcy. Courts should look to all the circumstances to determine if the relationship continued after resignation.

A Chapter 7 debtor, however, cannot be his or her own insider in another case. Thus, a Chapter 7 debtor's false oath in his or her own previous bankruptcy case cannot serve as a ground under Code §727(a)(7) for denying discharge in the debtor's subsequent case. Although spouses who file consecutive joint cases may be insiders of one another, this technical argument has been rejected. The debtor's conduct in the previous case may, however, be subject to a criminal prosecution under Title 18 of the United States Code. See Norton Bankruptcy Law and Practice 2d ¶¶74:17.

Prior discharge

Code §727(a)(8) establishes the rule that a debtor is not entitled to a Chapter 7 discharge if he or she has received a prior discharge in a case commenced within eight years before the date of the filing of the current petition. This section establishes the basic premise that the debtor

is not entitled to recurrent relief under discharge provisions within the specified time period. The objective, of course, is to prevent abusive repeat filings. Under §727(a)(9) the bar is six years from a discharge granted in Chapter 12 or 13 cases. The provision of Code §727(a)(8) and §727(a)(9) is mandatory, and equity cannot affect the plain language of the section.

Even if a discharge is not available to a Chapter 7 debtor under §727(a)(8) or (a)(9), the debtor may still file a Chapter 7 in order to avail itself of property protections under the Code. Those protections include the automatic stay, property exemptions, and lien preference and fraudulent conveyance avoidance powers.

The eight-year statutory period refers to the interval between the dates on which bankruptcy cases are commenced. Thus, the fact that a prior discharge occurred within six years prior to filing the current case is not sufficient to establish this objection unless it is also established that the first case was commenced less than eight years prior to the filing of the current case. Further, the party bringing an objection under Code §727(a)(8) must establish that the first case resulted in a discharge that was not subsequently revoked.[5]

The eight-year bar includes cases in which the prior discharge was granted under Chapter 13 and Chapter 12 of the Code. Where the original case was a Chapter 12 or Chapter 13 case, however, the six-year bar does not apply if payments under the prior case totaled (1) 100% of the unsecured claims; or (2) 70% of such claims and the plan was the debtor's best effort and was proposed in good faith. The purpose of this exception is to protect debtors who have made a good faith effort to repay debts in the prior case. For purposes of this provision, the "best effort"

[5] One of the more notable changes under the 2005 Act was the extension of the bar dates for debtors seeking to file a subsequent bankruptcy petition after receiving a prior discharge. In Chapter 7 cases, the bar date has been extended from six to eight years measured from the filing of the original petition. 11 U.S.C. 727(a)(8). The debtor seeking to file a Chapter 13 is barred from receiving a discharge if the debtor had obtained a Chapter 7, 11 or 12 discharge in a case commenced within four years of the current Chapter 13 filing, or if the debtor had received a Chapter 13 discharge within two years of filing. 11 U.S.C. 1328(f). Note that a Chapter 13 debtor is not barred from filing a plan to cure arrearage – the debtor is only barred from receiving a discharge.

standard requires analysis of the factual circumstances of the debtor at the time of the original case. This exception to the six-year rule may provide some incentive for debtors under Chapter 12 or Chapter 13 to propose the best quantitative economic effort payments in excess of 70% of the unsecured debt in their plans.

Code §727(a)(8) and (9) do not apply directly to Chapter 13 cases; instead the 2005 Amendments added §1328(f) to limit such subsequent discharges in Chapter 13 cases. See Norton Bankruptcy Law and Practice 2d ¶¶74:18.

Waiver of Discharge

Code §727(a)(10) provides that a discharge must be denied if the "court approves a written waiver of discharge executed by the debtor after the order for relief under this chapter." A waiver of discharge executed prior to the order of relief, such as in a state court settlement agreement, is unenforceable. The §727(a)(10) waiver waives a discharge of all debts, whereas a reaffirmation agreement in essence waives a discharge of a particular debt. As the order for relief in a voluntary proceeding occurs when the bankruptcy petition is filed, this section requires a waiver executed in writing after the case commences. This is consistent with reaffirmation practice, and represents a clarification of prior Bankruptcy Rules.

There are four requirements for an effective waiver of discharge: (1) the waiver must be approved by the court; (2) the waiver must be in writing; (3) the waiver must be signed by the debtor; and (4) the waiver must be given after the order for relief (i.e., post-petition in voluntary cases; after entry of order in involuntary cases). The Code does not provide guidelines regarding court approval of a waiver. It is doubtful, however, that pro forma approval is contemplated. The better view is that standards analogous to those adopted for reaffirmations should apply. Once a discharge has been granted, however, the right to waive discharge has passed. Further,

the debtor is not entitled to revoke his or her own discharge. See Norton Bankruptcy Law and Practice 2d ¶¶74:19.

Failure to complete instructional course

The 2005 Amendments added a requirement for all debtors to complete an instructional course concerning personal financial management described in Code §111 before the debtor will be granted a Chapter 7 discharge. Excepted from the requirements of completing an instructional course are persons who are unable to complete the requirements because of incapacity, disability, or active military duty in a military combat zone. Additionally, the course is not required for persons who reside in a district for which the U.S. Trustee has determined that the approved instructional courses are not adequate to service the additional individuals who would otherwise be required to complete such instructional courses. The U.S. Trustee is required to evaluate the courses at least once per year. See Norton Bankruptcy Law and Practice 2d ¶¶74:19.3.

Guilty of a felony under §522(q)

The 2005 Amendments added Code §727(a)(12), which requires the court to determine within 10 days before the entry of an order granting a discharge whether there is reasonable cause to believe that: (i) the debtor has been convicted of a felony under 18 U.S.C.A. § 3156 which demonstrates that the filing of the debtor's case was an abuse of Title 11; or (ii) that there is pending any proceeding in which the debtor may be found guilty of such a felony or may be found liable for a debt arising from any violation of the federal security laws as set forth under §522(q)(1)(B). If so, the court must withhold the entry of the discharge order, presumably until the hearing has been concluded and a determination made as to whether such action also

constitutes grounds to deny the debtor a discharge under §727. As Bankruptcy Rule 4004 requires an objection to a discharge under §727(a) to be filed within 60 days after the first date set for the meeting of creditors, it remains to be seen whether courts will consider this provision sufficient to also deny the discharge or whether the failure of a creditor to have filed a timely objection to the discharge will cause the court to allow the entry of a discharge order notwithstanding a finding against the debtor. This provision was added as a part of the 2005 Amendments and aimed at discouraging corporate securities abuse. See Norton Bankruptcy Law and Practice 2d ¶¶74:19.5.

III. CONVERSION AND DISMISSAL OF CASES

Chapter 7 Conversion

Code §706 permits a Chapter 7 debtor to convert a case to another chapter at any time, provided the debtor had not previously converted the case. Any waiver of the debtor's right to initially convert a case under this section is unenforceable. Under §706(b) the court may convert a case to Chapter 11 at any time upon the request of a party in interest and after notice and a hearing. Code §706(c) permits conversion to Chapter 12 or Chapter 13, only if the debtor requests or consents to the conversion. The 2005 Act amended this subsection to include "consent" of the debtor, apparently to facilitate conversion to Chapter 13 where the debtor is subject to a motion for conversion or dismissal under the §707(b) means test. The debtor's case may only be converted to another chapter if the debtor is eligible to be a debtor under that chapter. 11 U.S.C. 706(d).

Chapter 7 Dismissal

Code §707(a) provides for the dismissal of a Chapter 7 case for cause, including unreasonable delay by the debtor that is prejudicial to creditors; non-payment of any fees or charges required under 28 U.S.C. 123 and allows the United States Trustee to bring a motion to dismiss for the debtor's failure to file the documentation required under the Code §521(1).

The 2005 Act substantially overhauled the provisions for dismissal as a "substantial abuse" under former §707(b), and in its place substitutes the so-called "means test" and the mechanism for its enforcement. Of course, the means test was a significant change under the Bankruptcy Code, and is covered more comprehensively in other materials provided as part of this seminar. The means test under §707(b) generally specifies that an ability to pay some portion of debts through Chapter 13 will mandate a dismissal or conversion of the Chapter 7 case, and proscribes a more or less precise measure of a debtor's ability to pay debts through Chapter 13, which if met, can lead to dismissal on motion of the court or any party in interest. Code §707(b), however, allows the United States Trustee, but not other parties, to bring a motion for abuse under this section where the debtor's income falls below the amount triggering the means test, yet may still be alleged an abuse of the Bankruptcy Code. Note that the word "substantial" has been deleted from the former "substantial abuse" standard under this provision, and now all that is required is a showing of an "abuse" of the Bankruptcy Code.

Code §707(c) provides that on motion of a victim of a "crime of violence" or a "drug trafficking crime" as those terms are defined in Title 18 of the United Sates Code, and of which the debtor was convicted, the court may dismiss the bankruptcy case if it is in the best interest of the victim. However, §707(c)(B)(3) states that the court may not dismiss the case if it can be established by a preponderance of the evidence that the filing is necessary to satisfy a domestic support obligation.

Chapter 13 Conversion or Dismissal

In Chapter 13 cases, the debtor may convert a case to Chapter 7 or request dismissal of the case at any time. Any waiver of the debtor's right to have the case converted or dismissed is unenforceable. The debtor, however, may not have the case dismissed if the case had already been converted to another chapter.

Code §1307(c) provides that a Chapter 13 proceeding can be dismissed or converted to another chapter "for cause" on motion of a party in interest or the United States Trustee under several enumerated grounds, generally summarized as failures to comply with the provisions of the case, including the payment of any fees or the filing of required documents. The 2005 Act amended this subsection to include the non-payment of post-petition domestic support obligations to the list. See generally 11 U.S.C. 1307(c)(1) through (11). Another ground for dismissal or conversion is provided in §1307(e) for failure to file pre-petition tax returns required under §1308.

However, the court may not convert a Chapter 13 case to another Chapter unless the debtor requests the conversion. 11 U.S.C. 1308(f). Note that where a motion is made for conversion or dismissal, and the debtor does not appear to contest the motion or request dismissal, the court may convert the case without the debtor's consent.

Also note that valuations of secured property under Chapter 13 no longer apply once the case is converted to Chapter 7.

Dismissal Under Code §521

The 2005 Act provided additional grounds for dismissal of Chapter 7 and Chapter 13 petitions. Code §521(i) states that if the debtor does not file all of the information required by

Code §521(a)[6] by the 45th day after the filing of the case, the case shall be automatically dismissed on the 46th day. The court may extend the time for the filing of the required items by an additional 45 days. This provision intends to remedy, among other problems, those instances where business debtors would operate as debtors in possession for many months without filing schedules and financial affairs, relying on multiple extensions of time from the court.

In the event that the bankruptcy court does not "automatically" dismiss a case on the 46th day, a party in interest may request dismissal, and the court *shall* dismiss the case within five days of such request. The term "request" is unprecedented in the Bankruptcy Code. This term was most likely chosen to avoid courts construing such requests as motions under the federal and local bankruptcy rules, with the attendant minimum noticing requirements.

In a case in which the debtor has failed to file the required items by the 45-day deadline, subject to one 45-day extension, the court may decline to dismiss the case upon the request of a trustee appointed in the case, made prior to the deadline for such filings. The trustee must show that either: (a) the debtor attempted to file the requested data by the deadline; or (b) it is in the interests of creditors not to dismiss the case. See Norton Bankruptcy Law and Practice 2d ¶¶45:4.

Conversion or Dismissal Under Chapter 11

Code §1112 provides the framework for a conversion or dismissal of a chapter 11 case. A debtor may voluntarily convert its case unless: (a) the debtor is not a debtor in possession; (b)

[6] The 2005 Act significantly amended §521 to add several requirements to the documentation a debtor is required to file. Included are statements concerning net income, expected changes in income, and payment advices received by the debtor within sixty days prior to filing.

the case commenced as an involuntary proceeding; or (c) the case was previously converted to a chapter 11 on the request of a party in interest. 11 U.S.C. 1112(a).

A chapter 11 case shall also be converted or dismissed (whichever is in the best interests of creditors and the estate) upon the request of a party in interest upon a showing of cause, unless the court determines the appointment of a chapter 11 trustee or an examiner is in the best interests of the creditors and the estate. 11 U.S.C. 1112(b). The case may not be converted if the court finds and specifically identifies circumstances establishing that converting or dismissing the case is not in the best interests of the creditors and the debtor or any other party-in-interest establishes that (a) there is a reasonable likelihood that a plan will be confirmed in a reasonable period of time; and (b) the grounds for the dismissal are not a continuing loss or diminution and the lack of a reasonable ability to rehabilitate. 11 U.S.C. 1112(b)(2).

Cause for conversion or dismissal includes, but is not limited to, the grounds enumerated in §1112(b)(4) such as gross mismanagement, failure to comply with a court order, failure to pay United States Trustee fees or taxes, failure to pay domestic support obligations, revocation of an order confirming a plan, inability to substantially consummate a plan, a material default of a plan provision, failure to provide information or attend a §341 meeting of creditors or examination ordered by the court. 11 U.S.C. 1112(b)(4). The debtor's bad faith is an additional ground constituting cause for conversion or dismissal. The failure to file lists or schedules is a ground for dismissal under §1112(e), but only the United States Trustee may seek conversion or dismissal on these grounds.

If a motion to convert or dismiss is made, the hearing on such motion must be held within 30 days and the court must render a decision on the motion not later than 15 days after commencement of the hearing 11 U.S.C. 1112(a)(3).

IV. EFFECT OF CONFIRMATION

Binding Effect of Confirmation on All Parties

The provisions of §1327 give powerful effect to the confirmation of a Chapter 13 plan and are similar to provisions found in §1141(d)(2) of the Code with respect to chapter 11 plans. The provisions of a confirmed Chapter 13 plan bind the debtor and each creditor, whether the claim of such creditor is "provided for" by the plan, and whether such creditor has objected to confirmation, accepted the plan or rejected the plan. 11 U.S.C. 1327(a). The debtor and creditors are bound by the provisions set forth in the confirmed plan, and those terms cannot be altered by private agreements, understandings or misunderstandings between the debtor and creditors. Courts have stated that confirmation of a Chapter 13 plan has a *res judicata* effect on all arguments which parties in interest might have made to defeat the plan, or to realize relief from the stay, based on pre-confirmation facts and conditions. *Res judicata* does not apply, however, when a confirmed plan has been dismissed, or when the case is converted to Chapter 7.

There is a split of authority concerning whether a confirmed plan treating a creditor as the holder of a secured claim binds the debtor, even though the stay is lifted post-confirmation and the creditor liquidates its collateral. Some courts hold that the creditor's claim is reduced by whatever the creditor realizes upon post-confirmation liquidation, but the balance of the claim must be paid according to the original plan as a secured claim. A sizable minority of courts will hold that once the secured collateral is liquidated, the balance of the secured claim will be treated as unsecured.

On the other hand, where the debtor's car is destroyed after confirmation and insurance pays the value of the vehicle, §1327(a) limits the secured creditor's recovery to the balance of its secured claim, not the entire proceeds from the insurance policy.

The courts have recognized limits on the binding effect of confirmation under §1327(a). Creditors are entitled to appropriate notice of the hearing on confirmation. Further, when an appeal in an adversary proceeding required to determine lien rights is pending, subsequent confirmation of a plan may not bar the parties from completing the appellate process. Moreover, confirmation of a Chapter 13 plan cannot circumvent procedures to determine rights where an adversary proceeding is required by the Federal Rules of Bankruptcy Procedure. For instance, the debtor cannot insert a provision into a proposed plan which would declare a student loan debt dischargeable as an undue hardship upon confirmation.

Code §1327 does not preclude judicial determination of the amount of claims, the extent of secured claims under §506, or of the amount of arrearages to be cured under §1322(b)(5). Additionally, confirmation of a plan has been held *not* to be *res judicata* concerning issues raised on appeal pertaining to the allowance of a creditor's claim.

Vesting Property of Estate With Debtor

Unless the plan or the order of confirmation provides otherwise, confirmation "vests all of the property of the estate in the debtor." 11 U.S.C. 1327(b). Given that §1306(b) already provides that the debtor remains in possession of property of the estate, the vesting of property in the debtor upon confirmation under §1327(b) must mean something additional. Logically, when property vests in the debtor upon confirmation, there must pass additional rights to the debtor other than the right of possession which the debtor already has under §1306(b). To the extent that §1327(c) vests property in the debtor upon confirmation, the debtors then have a right to dispose of that property after confirmation of the Chapter 13 plan.

Conversion or dismissal of the Chapter 13 case may undo the effects of confirmation under §1327. For example, although confirmation vested property in the debtor free and clear of

a creditor's interest, if a case is dismissed. Code §349(b)(3) re-vests property in the entity in which such property was vested immediately before commencement of the Chapter 13 case.

Property Vests Fee and Clear of Creditor Claims and Interests

Except as provided in the plan or in the order of confirmation, the property vesting in the debtor upon confirmation is "free and clear of any claim or interest of any creditor provided for by the plan." 11 U.S.C. 1327(c). The effect of §1327(c) on liens has been the subject of much debate. It has been held that §1327(c) converts a creditor's claim secured by a lien on real estate into an unsecured claim by vesting the property subject to the lien in the debtor, free and clear of the creditor's lien. Some courts, unwilling to find that §1327(c) invalidates liens, have recognized that confirmation can fix the amount or extent of a lien and effect discharge of the lien upon completion of payments under the plan. Other courts have recognized that §1327(c) provides a sort of "lien avoidance," upon confirmation, by vesting property in the debtor free and clear of the claims or interests of creditors.

The majority of courts, however, hold that liens valid under state law are unaffected by confirmation of a Chapter 13 plan, even when the claim holder has disabled itself from participating in payments by failing to object to confirmation or to file a timely proof of claim.

Notwithstanding the above, at the conclusion of the plan a secured creditor may have the balance of their lien extinguished where the debtor has satisfied the secured portion of the creditor's claim through the plan.

Chapter 13 Discharge

Code §1328 provides for a discharge of a Chapter 13 debtor if (a) all payments under the plan have been paid; (b) the debtor has certified that all domestic support obligations under the

plan have been paid; and (c) no court approved written waiver of discharge has been executed by the debtor, except with respect to the specifically enumerated types of debt that will not be discharged. These excluded debts include, among others, priority tax claims, claims for criminal fines or restitution arising from willful or malicious injuries, death or personal injury caused by a debtor's operation of a motor vehicle while under the influence, fraud, debts not scheduled, fraud as a fiduciary, domestic support obligations and educational loans. 11 U.S.C. 1328. Educational loans may be discharged on a showing of undue hardship under §1328(a)(2). Additionally, debts incurred post-petition that are not provided for under the plan are not discharged. Allowed claims provided for under the plan are discharged unless they are consumer debts incurred absent prior authorization of the chapter 13 trustee where it was practical to obtain such approval. 11 U.S.C. 1328(d).

Effect of Confirmation Under Chapter 11

Similar to the effect of a confirmed Chapter 13 plan, a Chapter 11 plan binds the debtor, any entity issuing securities under the plan, any entity acquiring property under the plan, any creditor, equity security holder or general partner in the debtor. All such entities are bound regardless of whether they are impaired under the plan or whether they voted to accept the plan. 11 U.S.C. 1141(a).

Except under enumerated exceptions or as provided in the plan or confirmation order, property dealt with in the plan vests in the debtor and is free of claims and interests of creditors, equity security holders and general partners in the debtor.

A Chapter 11 discharge 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 debt or personal liability, regardless of whether a discharge of such debt has been waived. 11

U.S.C. §524. Similar to actions that violate the automatic stay, actions that violate §524 are void *ab initio*. *In re Motley*, 268 B.R. 237, 242 (Bankr. C.D. Cal. 2001).

The chapter 11 discharge discharges all debts that arose prior to confirmation regardless of whether a proof of claim was filed, the claim is allowed under §502, or if the claim holder accepted the plan. 11 U.S.C. § 1141(d)(1). However, a chapter 11 discharge does not discharge an individual debtor from any debt excepted from discharge under §523 and will only discharge debt of an individual debtor provided for in the plan when the court grants a discharge upon completion of all payments under the plan.