Creditor Debtor Rights News Letter

Published by the Creditor Debtor Rights Section of the Washington State Bar Association

Volume 37 SUMMER 2019 Number 1

NOTES FROM THE CHAIR

Kevin D. O'Rourke – Southwell & O'Rourke PS

Section Members These are my first notes as Chair of the Creditor/Debtor Section and I look forward to communicating with all of you over the course of my term. Below are: an announcement regarding the retirement of Judge Frank L. Kurtz from a very successful career on the bench, our recent Section election results, and comments on other current events that concern our Section. **Special thanks** to Chantelle Sliman, Judicial Assistant to Judge Kurtz, and Tap Menard, Law Clerk to Judge Kurtz, for their assistance in preparing the material on Judge Kurtz!

HONORABLE FRANK L. KURTZ

Honorable Frank L. Kurtz will complete his 14-year term as a bankruptcy judge for the Eastern District of Washington in November 2019. Although a Yakima resident for close to 40 years, Judge Kurtz's path to Yakima would have seemed unlikely. Born on February 5, 1946, in Omaha, Nebraska, he was one of four children of Louis and Elizabeth Kurtz. After graduating from high school, he elected to stay in Nebraska and attend Creighton University, graduating in 1968 with a B.A. in History. Having spent all his life in the corn fields and meatpacking warehouses of Nebraska, Judge Kurtz decided it was time to get out and see the world. He became an American Peace Corps Volunteer in 1968, spending two years in Jabalpur, India, observing and learning the cultures of a new land as well as helping to drill wells.

Upon his return from India, Judge Kurtz enrolled in the Gonzaga University School of Law and earned his J.D. in 1974. A position with Kirschenmann, Devine and Fortier initially brought him to the Yakima valley and by 1979 Judge Kurtz was practicing bankruptcy law as a partner in the law firm of Kurtz, Hurley, Lara and Adams. As a lawyer, Judge Kurtz was an original incorporator of the Bankruptcy Bar Association of the Eastern District of Washington in 1988 and served as its first co-chair as well as chairman of the Executive Committee of the Creditor/Debtor Section of the Washington State Bar Association. He also served as a Chapter 7 Panel Trustee for the Eastern District of Washington and was recognized in *The Best Lawyers in America*.

In 1966 Gov. Mike Lowry appointed Judge Kurtz to the Washington State Court of Appeals as a Division III Judge. Although headquartered in Spokane, Judge Kurtz spent a substantial amount of time driving around Eastern Washington, as his cases were divided between Yakima, Wenatchee, and Kennewick. During his tenure as a Washington state court judge, Judge Kurtz served as a member of the Court of Appeals Executive Committee and the Board for Judicial Administration. He also chaired the Washington State Judges Ethics Advisory Committee and the Mandatory Continuing Judicial Education Committee. He was acting Chief Judge from 1997-1999 and Chief Judge from 1999-2001.

IN THIS ISSUE

Notes from the Chair 1
By Kevin O'Rourke

Does a Bankruptcy Discharge Trigger the Running of the Statute of Limitations on Actions to Enforce a Deed of Trust? 3
By Jason Wilson-Aguilar, Office of the Chapter 13 Trustee

An Update on Washington State Collection Laws– Private Student Loan Debts 6
By Jonathan Baner, Law Offices of Baner & Baner

Evolving Receivership Opportunities for Creditors of Marijuana Businesses 8
By Dominique Scalia, DBS Law

9th Circuit Update 9
By Christopher Young, Cairncross & Hempelmann

CREDITOR DEBTOR RIGHTS SECTION EXECUTIVE COMMITTEE

Chair
Kevin D. O'Rourke
Southwell & O'Rourke PS
421 W. Riverside Ave Ste 960
Spokane, WA 99201-0402
(509) 624-0159
(509) 624-9231 fax
kevin@southwellorourke.com

Immediate Past Chair
Thomas S. Linde
Schweet Linde & Coulson PLLC
575 S. Michigan Street
Seattle, WA 98108-3316
(206) 381-0125
(206) 381-0101 fax
tomlinde@schweetlaw.com

Chair-Elect
William F. Malaier, Jr.
Ogden Murphy Wallace PLLC
901 5th Avenue, Suite #3500
Seattle, WA 98164-2059
(206) 447-7000
(206) 224-3463 fax
wmalaier@omwlaw.com

Secretary/Treasurer
Bruce Medeiros
Davidson Backman Medeiros PLLC
601 W. Riverside Avenue, Suite #1550
Spokane, WA 99201-0603
(509) 624-4600
(509) 623-1660 fax
bmedeiros@dbm-law.net

Position #1 – Eastern District
Rebecca Sheppard
Sheppard Law Office PC
16114 E. Indiana Avenue, Suite #205
Spokane Valley, WA 99216-1874
(509) 443-3014
(509) 443-3015 fax
rjs@sheppardlaw.com

Position #2 – Eastern District
Melissa Williams
The Office of the Chapter 13 Trustee for Eastern District of WA
801 W. Riverside Avenue, Suite #515
Spokane, WA 99201-0908
(509) 747-8481
melissa.williams@spokane13.org

Position #3 – Northern Division - Western District
Thomas D. Neeleman
Thomas D. Neeleman Esq. LC
1904 Wetmore Avenue, Suite 200
Everett, WA 98201-6110
(425) 212-4800
(425) 212-4802 fax
neeleman@expresslaw.com

Position #4 – King County
J. Todd Tracy
The Tracy Law Group PLLC
1601 5th Avenue, Suite #610
Seattle, WA 98101-1681
(206) 624-9894
(206) 624-8598 fax
todd@thetracylawgroup.com

Position #5 – King County
Ruth Nelson
7742 14th Avenue NW
Seattle, WA 98117-4221
(206) 633-2517
nelsonruthlawoff@qwestoffice.net

Position #6 – Southern Division - Western District
Alexander Kleinberg
Eisenhower & Carlson PLLC
1201 Pacific Avenue, Suite 1200
Tacoma, WA 98402-4395
(253) 572-4500
akleinberg@eisenhowerlaw.com

Position #7 – Southern Division - Western District
Megan Kelly Bartley Rue
Morgan Hill PC
2102 Carriage Street SW, Suite C
Olympia, WA 98502-1049
(360) 357-5700
(360) 357-5761 fax
megan@olympialegal.com

Position #8 – Eastern District - At Large
David Kazemba
Overcast Law Offices, P.S.
23 S. Wenatchee Avenue, Suite 320
Wenatchee, WA 98801-2263
(509) 663-5588
(509) 662-5508 fax
dkazemba@overcastlaw.com

Position #9 – Western District - At Large
John S. Kaplan
Perkins Coie LLP
1201 3rd Avenue, Suite 4900
Seattle, WA 98101-3099
(206) 359-8000
(206) 359-9000 fax
jkaplan@perkinscoie.com

Newsletter Editor
Mark D. Northrup
Miller Nash Graham & Dunn LLP
Pier 70
2801 Alaskan Way, Suite 300
Seattle, WA 98121-1128
(206) 777-7536
(206) 340-9599 fax
mark.northrup@millernash.com

BOG Liaison
Paul A. Swegle
General Counsel, Newyu, Inc.
9416 24th Avenue NW
Seattle, WA 98117-2807
(206) 300-7165
pswegle@gmail.com

YLC Liaison
Eli Enger
4801 E. Broadway Blvd., #311
Tucson, AZ 85711-3653
(509) 308-4297
engere08@gmail.com

Notes From the Chair

Continued from page 1…

On November 1, 2006, after nine years on the Washington State Court of Appeals, Judge Kurtz was appointed as a new bankruptcy judge for the Eastern District of Washington. When Judge Kurtz first arrived, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 had just taken effect and the court's caseload was extremely heavy, so there was no time to ease into his new position. Judge Kurtz quickly became active in the court's Standing Advisory Committee, the Chapter 13 Sub-Committees, and Small Business Working Groups where he helped navigate the court's course through a period of changes. During his years on the bankruptcy bench, he has been actively involved in many judges' panels and conferences, consistently being asked to speak on Ninth Circuit case law updates. He has always been highly regarded as a mediation judge and has regularly been sought out by counsel to participate in their settlement conferences. Judge Kurtz served as Chief Judge of the Bankruptcy Court from 2006-2013. He also served as Chief of the Chief Judges.

In 2013 Judge Kurtz was selected to sit as one of six judges on the Ninth Circuit Bankruptcy Appellate Panel. The BAP office is located in Pasadena, California, but the Panel hears oral arguments throughout the Ninth Circuit as caseload dictates—requiring Judge Kurtz to travel 10 out of 12 months to hear cases on the appellate docket. He is currently serving as the Chief Judge of the BAP.

Judge Kurtz enjoys traveling with his wife, his annual ski trip with friends, and playing golf. The Section wishes Judge Kurtz all the best in his retirement and much joy and happiness in this new chapter of his life.

CONGRATULATIONS NEW EXECUTIVE COMMITTEE MEMBERS

As Chair, I would formally like to congratulate and welcome the following newly elected Executive Committee Members to two-year terms (October 1, 2019-September 30, 2021):

John Read Knapp, Jr., Miller Nash Graham & Dunn, LLP, King County, Position 5

Samuel James Dart, Law Clerk, Honorable Mary Jo Heston, Southern Division of Western District, Position 7

David Alan Kazemba, Overcast Law Offices, P.S. At-Large, Position 8

John Stuart Kaplan, Perkins Coie, LLP, At-Large, Position 9

Continued on page 2…

Notes From the Chair
Continued from page 2…

SAVE THE DATE FOR NWBI

The 33rd Annual Northwest Bankruptcy Institute (NWBI), co-sponsored by the Section and the Oregon State Bar, will be held on April 3-4, 2020, at the Hyatt Regency, 808 Howell Street, Seattle, Washington. NWBI is our Section's premier annual event. Rooms are available at a reduced rate until Friday, March 12, 2020, starting at $209.00 per night. Mark your calendar for this excellent CLE. For more information, please contact Karen Lee, Director of CLE Seminars, Oregon State Bar, 503-431-6382, klee@osbar.org, or visit www.hyatt.com/en-US/group-booking/SEARS/G-ORES.

The Section will also hold its semi-annual Judgment Collection CLE in December 2019. The Section will post on the WSBA website more information as it becomes available at www.wsba.org/legal-community/sections/creditor-debtor-rights-section.

GRANT PROGRAM

The Section recognizes the importance for all individuals to have access to legal services. Many Section members are actively involved in making their expertise available to low-income individuals, both through direct representation and/or educational programs. While financial constraints and/or other limitations may deter individuals from seeking legal services, it is important that community services exist to assist with such issues. Established in 2004, the purpose of the Section's Grant Program is to provide financial assistance to the ongoing operation of these community service programs. Since 2004, the Section has supported many legal service providers and projects with awards totaling $162,548.20. The Grant recipients for 2019 are the Center for Justice and the Chelan Douglas County Volunteer Attorney Services, receiving award amounts of $1,000 and $4,000, respectively.

Have a great fall! ■

DOES A BANKRUPTCY DISCHARGE TRIGGER THE RUNNING OF THE STATUTE OF LIMITATIONS ON ACTIONS TO ENFORCE A DEED OF TRUST?

Jason Wilson-Aguilar – Office of the Chapter 13 Trustee

An action upon a contract or agreement in writing must be commenced within six years. Wash. Rev. Code § 4.16.040(1). A promissory note and deed of trust are written contracts subject to the six year statute of limitations. *Westar Funding, Inc. v. Sorrels*, 157 Wn.App. 777, 239 P.3d 1109, 1113 (2010).

Under an installment note, the six-year statutory period commences for each installment from the time it becomes due and was not paid. The final six-year period on the entire debt begins to run at the maturity date of the note. See, *Cedar West Owners Ass'n v. Nationstar Mortgage*, 7 Wn.App.2d 473, 434 P.3d 554, 556 (2019) ("the six-year statute of limitations on an installment promissory note is triggered by each missed monthly installment payment at the time it is due"); *Herzog v. Herzog*, 23 Wash.2d 382, 161 P.2d 142, 144-55 (Wash. 1945) ("[W]hen recovery is sought on an obligation payable by installments the statute of limitations runs against each installment from the time it becomes due; that is, from the time when an action might be brought to recover it."). Further, "[mere] default will not alone accelerate the payments due on an installment promissory note. Some affirmative action is required by the holder of the note that makes it clear and unequivocal to the payor that the holder has, in fact, declared the entire debt due." *Merceri v. Bank of New York Mellon*, 4 Wn.App.2d 755, 434 P.3d 84, 87-8 (2018).

In *Merceri*, the lender sent the borrower a notice that the entire debt would be accelerated if she failed to cure her default. The notice provided:

> If the default is not cured on or before March 18, 2010, the mortgage payments will be accelerated with the full amount remaining accelerated and becoming due and payable in full, and foreclosure proceedings will be initiated at that time. As such, the failure to cure the default may result in the foreclosure and sale of your property.

Id. at 88 (emphasis in original). The court determined that the notice was not an acceleration of the note. The debtor did not cure the default, but the lender did not subsequently take any "affirmative action in a clear and unequivocal

Continued on page 4…

Does a Bankruptcy Discharge Trigger the Running of the Statute of Limitations on Actions to Enforce a Deed of Trust?
Continued from page 3…

manner indicating that the payments on the loan had been accelerated." *Id*. The lender never declared the entire debt due and did not refuse to accept installment payments. The lender also sent the borrower mortgage statements reflecting the amount due rather than the entire accelerated amount due. Because that notice was not an unequivocal acceleration and the lender's subsequent actions reflected that the debt was not accelerated, the debt was not accelerated and the appellate court overruled the trial court's findings that the debt had in fact been accelerated.

Courts have differed over the import of a bankruptcy discharge on the triggering of the statute of limitations. A starting point in the analysis is *Edmundson v. Bank of America*, 194 Wn.App. 920, 378 P.3d 272 (2016). In that case, the borrowers obtained a loan in July 2007 to purchase real property. The installment promissory note was dated July 12, 2007, was payable in monthly installments beginning September 1, 2007, and matured on August 1, 2037. A deed of trust dated July 12, 2007 secured the promissory note on the debtor's purchased property. The debtors stopped making loan payments on November 1, 2008 and did not make any payments after that. The debtors filed a Chapter 13 bankruptcy case on June 12, 2009 and received a discharge on December 31, 2013. A notice of default dated October 23, 2014 was sent to the borrowers and the successor trustee under the deed of trust subsequently scheduled a trustee's sale of the debtor's real property. In March 2015 the borrowers filed suit to restrain the foreclosure sale and to quiet title to the property. The borrowers asserted that the deed of trust was no longer enforceable.

The *Edmundson* court observed that a bankruptcy discharge extinguishes a debtor's personal liability but that the secured creditor's right to foreclose on the deed of trust passes through bankruptcy unless the lien was avoided or eliminated in the bankruptcy case. *Id*. at 275 (citing *Johnson v. Home Street Bank*, 501 U.S. 78 (1991) and *Dewsnup v. Timm*, 502 U.S. 410 (1992)). The debtors in *Edmundson* did not avoid or eliminate the lien in their bankruptcy case, so the lien survived or passed through the bankruptcy case unaffected.

In reversing the trial court's ruling that the deed of trust became unenforceable once the underlying note became unenforceable due to the discharge, the appellate court noted that

> [n]othing in the Deeds of Trust Act supports the conclusion that the lien of a deed of trust on real property is discharged under state law when the note or other secured obligation is no longer enforceable…The trial court's ruling fails to recognize that enforcement of a promissory note and foreclosure of a deed of trust securing that note are separate remedies of a creditor in the event of a borrower's default. The inability to pursue one remedy does not bar the other.

Id. at 275-76. The lender was thus able to foreclose its security interest and the court could have ended its opinion at that point.

After making its ultimate finding, however, the *Edmundson* court added that "[s]econd[arily], even if we were to accept [the borrowers'] incorrect premise, that would not end the inquiry. *Id*. In explaining its further reasoning, the Edmundson court observed that

> the statute of limitations for each subsequent monthly payment accrued on the first day of each month after November 1, 2008 until the [borrowers] no longer had personal liability under the note. They no longer had such liability as of the date of their bankruptcy discharge.

Id. at 278 (emphasis added).

As set forth in what follows, the foregoing language from Edmundson gave rise to a split of authority, although this split has arguably been resolved (or at least clarified) by an appellate ruling shortly before this issue went to press.

In *Jarvis v. Fed. Nat'l Mortgage Ass'n*, the borrowers' promissory note was payable in installments and matured in the year 2036. No. 16-C5194-RBL, 2017 WL 1438040 (W.D. Wash. April 24, 2017), aff'd, 726 Fed. App'x. 666 (9th Cir. 2018). The borrowers stopped making payments on their mortgage obligation and filed for Chapter 7 bankruptcy in November 2008. The debtors received their discharge on February 23, 2009. The borrowers did not reaffirm the debt in the bankruptcy case nor did the mortgage lender accelerate the note. On February 11, 2016, the borrowers commenced a quiet title action, asserting that the discharge of their personal liability on the note established their last missed payment date that would trigger the running of the six year statute of limitations period. The borrowers asserted that, because no more installments could come due, no future event could extend the lender's time to enforce its deed of trust securing the note. The court noted that the bankruptcy discharge did not eliminate the security interest but also concluded that the discharge did "alert the lender that the limitations period to foreclose on a property held as security has commenced." *Id*. at *2.

Citing *Edmundson*, the *Jarvis* court then observed that

> [t]he last payment owed [under an installment note]

Continued on page 5…

Does a Bankruptcy Discharge Trigger the Running of the Statute of Limitations on Actions to Enforce a Deed of Trust?
Continued from page 4…

> commences the final six year period to enforce a deed of trust securing the loan. This situation occurs when the final payment becomes due, such as when the note matures or a lender unequivocally accelerates the note's maturation… It also occurs at the payment owed immediately prior to the discharge of a borrower's personal liability in bankruptcy, because after discharge a borrower no longer has forthcoming installments he must pay.

Jarvis, 2017 WL 1438040, at *3 (emphasis added).

The lender in *Jarvis* asserted that the *Edmundson* court wrongly noted in dicta that the last installment payment a borrower owes before discharge triggers the final limitations period under a deed of trust. *Id*. at *2. The *Jarvis* court disagreed, holding that

> [t]he discharge of a borrower's personal liability on his loan–the cessation of his installment obligations–is the analog to a note's maturation. In both cases, no more payments could become due that could trigger RCW 4.16.040's limitations period. The last-owed payments before the discharge of a borrower's personal liability on a loan is the date from which a secured creditor has six years to enforce a deed of trust securing the loan.

Id. at *3. See also *Spesock v. U.S. Bank*, No. 18-0092, 2018 WL 4613163, at *4 (W.D. Wa. Sept. 26, 2018) (noting that, "[w]hen a note is discharged in a Chapter 7 bankruptcy, the statute of limitations to enforce the corresponding deed of trust runs from the date the last payment on the note was due prior to the Chapter 7 discharge").

In contrast to *Edmundson* and *Jarvis*, the bankruptcy court in the Western District of Washington subsequently held that a discharge does not trigger commencement of the statute of limitations under an installment note. In *re Griffith*, No. 18-12420-TWD (Bankr. W.D. Wa. Dec. 7, 2018) (oral ruling). In *Griffith*, the debtors asserted that the lender's ability to enforce its deed of trust expired six years after the debtors' personal liability was discharged in the debtors' prior Chapter 7 bankruptcy case, arguing that the discharge amounted to an acceleration under the note from which the six year statute of limitations would begin to run. The court disagreed.

In *Griffith*, the debtors received their discharge in the Chapter 7 case on September 15, 2010. Reviewing the Washington State Court of Appeals decision in *Edmundson*, the bankruptcy court held that a bankruptcy discharges a debtor's in personam liability but not the debtor's in rem liability or the validity of the underlying deed of trust. In *re Griffith*, No. 18-12420-TWD (Bankr. W.D. Wa. Dec. 7, 2018) (oral ruling) citing *Edmundson*, 378 P.3d at 276 and finding that "nothing under either federal or state law supports the conclusion that the discharge of personal liability on the note also discharges the lien on the deed of trust securing the note. The deed of trust is enforceable." Further reviewing the second part of the Court of Appeals decision in *Edmundson* regarding the statute of limitations, the bankruptcy court concluded that that part of the decision was dicta only and not central to the Court of Appeals' decision.

The *Griffith* bankruptcy court also specifically discussed the Court of Appeals' contention that "the statute of limitations for each subsequent monthly payment accrued on the first day of each month after November 1, 2008 until the [the borrowers] no longer had personal liability under the note." The bankruptcy court in *Griffith* noted that the first part of that statement was well-supported by Washington state case law but that the Court of Appeals cited no authority for the second part of the statement. The bankruptcy court found that the Court of Appeals lost track of the two separate remedies of the lender: the in personam liability that was discharged in the bankruptcy and the surviving in rem claim under the deed of trust. The *Griffith* court therefore specifically rejected the implied notion in *Edmundson* that a bankruptcy discharge could be an acceleration under the promissory note that would trigger the running of the six year statute of limitations for enforcement of the obligation. In so doing, the court rejected the implication that a bankruptcy discharge was the equivalent of an acceleration under the note. The court observed that "Washington State law is clear that acceleration of an installment note does not occur automatically, is the lender's option, and must be exercised by some unequivocal, affirmative action by the lender." In *re Griffith*, No. 18-12420-TWD (Bankr. W.D. Wa. Dec. 7, 2018) (oral ruling) (citing *Merceri v. Bank of New York Mellon*, 434 P.3d 755, 87-88 (Wash. App. 2018). Further, "[t]here is no provision of the Bankruptcy Code," the court asserted,

> that says discharge equates to acceleration or maturation of an installment note. The effect of the bankruptcy discharge is to eliminate the personal liability on the installment note, not to accelerate the amounts due under an installment note. Since in rem liability remains unaffected by a bankruptcy discharge and acceleration can only occur by affirmative action of the lender, it does not follow that a bankruptcy discharge can be a substitute for acceleration and start the statute of limitations on the non-discharged in rem obligation. After the bankruptcy discharge, the terms of the deed of trust govern when the six year statute of limitations starts on the surviving in rem claim.

Continued on page 6…

Does a Bankruptcy Discharge Trigger the Running of the Statute of Limitations on Actions to Enforce a Deed of Trust?
Continued from page 5…

In *re Griffith*, No. 18-12420-TWD (Bankr. W.D. Wa. Dec. 7, 2018) (oral ruling). Because the lender in *Griffith* never accelerated the note and the discharge was not an acceleration, the statute of limitations to enforce the security interest had not commenced and the court overruled the debtors' objection to claim.

The *Griffith* bankruptcy court issued a substantively identical ruling in a subsequent case. On appeal, however, the District Court reversed that decision. *See*, *Hernandez v. Franklin Credit Mgmt. Corp*., Adv. Proc. No. 18-01159-TWD, rev'd, No. 19-0207JCC (W.D. Wa. Aug. 13, 2019). In its ruling, the District Court in *Hernandez* held that the statute of limitations did begin to accrue on the last date an installment payment was due prior to the debtor's discharge:

> The Bankruptcy Court erred by treating the rule announced in *Edmundson* regarding the applicable statute of limitations as dicta and instead ruling that "under Washington law the statute of limitations for an action to enforce a deed of trust securing an installment note can be triggered only by natural maturation or acceleration."
>
> The Washington State Court of Appeals expressly stated in *Edmundson* that the statute of limitations on enforcement of a deed of trust payable in installments accrues when the last installment payment is due prior to discharge of a borrower's personal liability on the corresponding promissory note. 378 P.3d 277. The court of appeals based its reasoning on long-standing precedent from the Washington State Supreme Court holding that the statute of limitations accrues "against each installment from the time it becomes due; that is, from the time when an action might be brought to recover it."

Hernandez v. Franklin Credit Mgmt. Corp., No. 19-0207JCC, at *4-5 (W.D. Wa. Aug. 13, 2019). See, also, *U.S. Bank N.A. v. Kendall*, 2019 WL 2750171 (Wash. Ct. App. 2019).

Finally, the District Court in *Hernandez* also opined that it "does not see any reason to conclude that the Washington State Supreme Court would reach a contrary decision." *Hernandez v. Franklin Credit Mgmt. Corp*., No. 19-0207JCC, at *5. That the Washington State Supreme Court would, in fact, agree with the *Jarvis/Hernandez* line of cases is a reasonable prediction, although one that remains untested. Regardless, *Hernandez* plainly deals a serious—perhaps fatal—blow to the legal argument the bankruptcy court approved in *Griffith*. ■

AN UPDATE ON WASHINGTON STATE COLLECTION LAWS – PRIVATE STUDENT LOAN DEBTS

Jonathan Baner – Baner and Baner Law Firm, Tacoma

On June 1, 2018 the Student Opportunity, Assistance, and Relief Act ("the Act") became effective. The Washington legislature's express intent in passing the Act was to help student loan borrowers in default avoid the loss of professional licenses or certifications, which hinders repayment, and to help student loan borrowers in default maintain financial stability and avoid the hardships of bank account and wage garnishment by making the postjudgment interest rate for private student loan debt more comparable to the market rate and by increasing the exemptions for bank account and wage garnishments. *See*, "Findings—Intent—2018 c 199," incorporated into RCW 67.08100.

The Act accomplishes these objectives by amending a number of statutes: RCW 67.08.100, 4.56.110, 6.01.060, 3 6.15.010, 6.27.100, 6.27.105, 6.27.140, and 6.27.150; and by repealing RCW 2.48.165, 18.04.420, 18.08.470, 5 18.11.270, 18.16.230, 18.20.200, 18.27.360, 18.39.465, 18.43.160, 6 18.46.055, 18.76.100, 18.85.341, 18.96.190, 18.104.115, 18.106.290, 7 18.130.125, 18.140.200, 18.145.125, 18.160.085, 18.165.280, 8 18.170.163, 18.180.050, 18.185.055, and 28A.410.105.

APPLICATION TO PRIVATE STUDENT LOANS

Amended RCW 6.01.060 defines "private student loan" as "any loan not guaranteed by the federal or state government that is used solely for personal use to finance postsecondary education and costs of attendance at an educational institution. A private student loan includes a loan made solely

Continued on page 7…

An Update on Washington State Collection Laws – Private Student Loan Debts

Continued from page 6…

to refinance a private student loan. A private student loan does not include an extension of credit made under an open-end consumer credit plan … or any other loan that is secured by real property or a dwelling."

POSTJUDGMENT INTEREST RATE; LICENSE REVOCATION; GARNISHMENT

☐ The Act amends Washington's judgment statute (RCW 4.56.110(4)) by mandating that private student loan judgments shall, unless "founded on written contracts," bear interest at 2 percent above the prime rate (i.e. about 7 percent in June 2018). This provision effects the expressed intent of the legislature to make "the postjudgment interest rate for private student loan debt more comparable to the market rate" and amended RCW 4.56.110(5) makes the new provision an exception to RCW 19.52.020, which provides the basis for awarding postjudgment interest at 12 percent. It is notable that despite the new reduced interest mandate, RCW 4.56.110(1) continues to provide that a judgment based on a written contract "shall bear interest at the rate specified in the contract." This suggests that if the underlying contract interest rate is higher than 2 percent above the prime rate, postjudgment interest at the higher contract rate could be awarded. Unless the underlying contract rate were 12 percent, however, the new provision would likely still place borrowers in a better position than the old statute.

☐ The Act repeals multiple provisions in Washington statutes that permitted regulators of 26 professions to suspend the professional licenses or certificates of student loan borrowers who had defaulted on their loans. The legislature terminated this right to suspend licenses and certificates based on its common sense conclusion that such aggressive and counterproductive collection laws did little more than hinder a borrower's ability to support himself/herself and their families, much less repay their obligations. Significantly, with the repeal of former RCW 67.08.100(8), this benefit applies to all student loans, whether private or not.

☐ The Act's biggest practical impact may be its new limits on garnishment. A garnishment for private student loan debt must now be specifically stated in the writ of garnishment and is limited by a "basic exempt amount" that is the greater of 85percent of disposable earnings or 50 times the minimum hourly wage "of the highest minimum wage law in the state at the time the earnings are payable." RCW 6.27.100, -105, -140, -150. Accordingly, a private debt creditor can garnish only 15 percent of disposable earnings or the amount in excess of 50 times the state minimum wage calculated on a weekly basis. By contrast, a non-private student loan garnishment exempts only the greater of 35 times the federal minimum hourly wage or 75 percent of disposable earnings.

The Act also exempts $2,500 from bank account garnishments. RCW 6.15.010(1)(d)(ii)(B). This means that a debtor must be left with at least a total of $2,500 in his or her bank account(s) following a garnishment or other execution process. By contrast, the non-private student loan exemption is only $500.

Finally, the Act exempts from collection "a cell phone, personal computer, and printer." RCW 6.15.010(c). This exemption is not limited to private student loan debts.

THE TAKEAWAYS:

1 Private student loan debt will likely be deemed less valuable in the marketplace as the options to compel payment become more limited.

2 Assume that private student loan debt will now bear postjudgment interest at seven percent when calculating margins.

3 Attorneys must update their collection forms: the writ of garnishment; exemption forms; notice of garnishment; and the explanation of the debtor's rights.

Garnishment of private student loan debtors will yield a substantially smaller return. Although a garnishment for child support can attach up to 50 percent of disposable earnings and a regular judgment can attach 25 percent of disposable earnings, a garnishment based on a private student loan debt can now attach only 15 percent of disposable earnings. The exempt amount calculated at 50 times the state minimum wage is also more than double the 35 times the federal minimum wage exemption for other debts. ■

WSBA Creditor Debtor Rights Section Newsletter

CALL FOR ARTICLES

The Newsletter welcomes your submissions. If you have a suggestion for an article or would like to discuss a topic, please let me know as soon as possible.

Please submit your articles electronically in Word format to *mark.northrup@millernash.com.*

JOIN THE SECTION LIST SERVE

To learn more about how to join the Creditor Debtor Rights Section members-only list serve, email sections@wsba.org.

EVOLVING RECEIVERSHIP OPPORTUNITIES FOR CREDITORS OF MARIJUANA BUSINESSES

Dominique Scalia – DBS Law, Seattle

The Ninth Circuit recently decided an appeal that is helping to define the degree to which a connection to the marijuana industry will disqualify debtors from seeking bankruptcy protection. *See, Gregory Garvin v. Cook Investments NW, SPNWY, LLC*, 922 F.3d 1031 (2019). In a favorable decision for the debtor—a real estate holding company that leased a portion of its property to a marijuana business—the Ninth Circuit made it possible for debtors to confirm Chapter 11 plans, even if such debtors have (or had) executory contracts with marijuana businesses, so long as they can reject the contracts, use no marijuana-derived funds to support the plan, and still complete the plan. Specifically, the court analyzed 11 U.S.C. §1129(a)(3)'s requirement that a plan not be proposed "by any means forbidden by law" and concluded that this language requires an examination solely of "the proposal of a plan, not the terms of the plan." *Garvin*, 922 F.3d at 1035. While this may look like a very small crack in the door into bankruptcy court for the marijuana industry, it is the widest yet in any circuit.

Notwithstanding this shift, the posture of bankruptcy courts nationwide has generally been hostile toward the marijuana industry and anyone related to it. *See, e.g., In re Arenas*, 535 B.R. 845 (10th Cir. B.A.P. (Colo.) 2015) (affirming dismissal of petition of individuals operating marijuana business as sole proprietorship); *In re Medpoint Mgmt., LLC*, 528 B.R. 178 (Bankr. D. Ariz. 2015), *vacated in part*, No. BAPAZ151130KUJAJU, 2016 WL 3251581 (B.A.P. 9th Cir. June 3, 2016) (dismissing involuntary petition filed against management company providing services to marijuana businesses in Arizona); *In re Rent-Rite Super Kegs W. Ltd.*, 484 B.R. 799 (Bankr. D. Colo. 2012) (dismissing petition by landowner that leased property to marijuana businesses). Accordingly, state-court receiverships remain, at least in Washington, the most common avenue for marijuana-related debtors to engage in a court-based insolvency proceeding—and are still the only path for marijuana businesses themselves.

State-level regulations in Washington (not to mention the federal Controlled Substances Act) leave creditors of marijuana businesses largely without recourse. While creditors can obtain judgments against marijuana businesses, executing on the debtor's marijuana assets has thus far proved impossible without the appointment of a receiver. Unlike Oregon, which provides secured creditors with opportunities to foreclose directly or even take over marijuana businesses (*see* OAR 845-025-1260 and 1275), creditors in Washington cannot take possession of marijuana assets without themselves being duly licensed by the Liquor and Cannabis Board ("LCB"). In fact, given all the regulations governing transfers of marijuana products, it is not entirely clear a creditor could take possession through foreclosure even if it did have its own license.

These receiverships, however, have their own challenges. The limited number of available licenses for marijuana businesses has created a secondary market that gives receivers an asset to sell in most cases, even where the business is otherwise defunct. The process of transferring the license, however, is onerous and time-consuming. A purchaser must obtain LCB approval to receive the license, even if it has already passed required background checks and holds other licenses. The process currently takes several months in the very best-case scenario, and can take much longer.

Meanwhile, the license must remain tied to its previously-approved location or it is subject to cancellation. WAC 314-55-135(6). This regulation in fact specifies that in the absence of an approved licensed location, "persons…will be discontinued." This leaves landlords without the opportunity to re-rent the location and if the receivership estate is without cash to pay rent, the license could be lost if the landlord is not willing to be patient and cooperate with the receiver's occupation of the location.

Fortunately, many petitioners in marijuana receiverships are themselves the debtor's landlord. In such cases, open communication about the realistic duration of the receivership is key and generally has proven sufficient where the landlord's patience means the difference between a valueless estate and the landlord eventually receiving back-rent from sale proceeds.

In some cases, the LCB has shown a willingness to impose a kind of temporary suspension on a license that allows the receiver to vacate a leased premises pending LCB approval of a sale. But this prospect is risky in itself. If the buyer backs out or does not obtain LCB approval, the suspension can end and the license can be left without an approved location.

As one final hurdle, the LCB has passed new regulations (effective December 1, 2018) governing receiverships in the industry. Under WAC 314-55-137, receivers must be pre-

Continued on page 9…

Evolving Receivership Opportunities for Creditors of Marijuana Businesses
Continued from page 8…

approved by LCB (this was already true in practice) and can be appointed over no more than three producers/processors or no more than five retailers at a time. The same receiver cannot simultaneously hold both a retail license and a producer/processor license. This means that out of the five receivers known to the author with current LCB approval, any receiver active in a separate producer/processor case will be unavailable to be appointed in a retail case, and vice versa.

This new regulation garnered significant push-back from the legal community during the public comment period. In a highly-regulated and specialized industry like marijuana, receivers should be qualified and experienced to the extent possible. Such strict limitations on the ability to serve over multiple license-types and multiple licenses has the effect of limiting the availability of receiverships for creditors (and debtors)—and the regulation came with no explanatory rationale from the LCB.

Despite these challenges, receivership remains the primary remedy available for creditors to recover from marijuana businesses and, in the author's experience, creditors' interest in and use of this remedy continues to increase. If Washington is to meet its goals of bringing this industry out of the shadows and eliminating the black market for marijuana, creditors must be afforded practical and useful opportunities to protect themselves and their economic interests. Marijuana businesses will never be able to participate fully in Washington's larger business community and economy until their relationships with investors, lenders, employees, vendors, and all other potential creditors become more closely aligned with other industries. The LCB has arguably taken a step in the wrong direction on that front, but the author's hopes remain high that both state- and federal-level policies will shift in the years ahead. ■

NINTH CIRCUIT UPDATE

Christopher Young – Cairncross & Hempelmann, Seattle

Daff v. Good (In re Swintek), 906 F.3d 1100 (9th Cir. 2018)

At issue: whether 11 U.S.C. §108(c) tolls the time during which a California Superior Court Order for Appearance and Examination ("ORAP") lien may be renewed. The bankruptcy court determined that it did not and entered summary judgment for the Chapter 7 trustee. The bankruptcy appellate panel reversed, concluding that *Spirtos v. Moreno (In re Spirtos)*, 221 F.3d 1079 (9th Cir. 2000), controlled the issue. The panel, holding that §108(c) tolls the period in which a creditor may execute on a lien because doing so constitutes the continuation of the original action, affirmed the bankruptcy appellate panel's reversal.

By way of assignment, Good acquired two nine-year-old money judgments against the debtor in 2009. In 2010, Good renewed the judgments. In June 2010, Good obtained a court-issued ORAP, requiring the debtor to appear for supplemental proceedings. By serving the ORAP on the debtor, Good created an ORAP lien encumbering the debtor's personal property. *See* CAL. CIV. PROC. CODE § 708.110(d); *S. Cal. Bank v. Zimmerman (In re Hilde)*, 120 F.3d 950, 956 (9th Cir. 1997).

Following the debtor's Chapter 7 filing in August 2010, Good filed an adversary complaint seeking a declaration that her ORAP lien primed any interest of the Chapter 7 trustee, Daff. On cross motions for summary judgment, Daff argued that the lien had expired at the end of the statutory one-year term; Good argued that because the debtor filed after the ORAP lien was created, §108(c) tolled the lien.

The panel began its analysis by noting that its decision would hinge on the interplay between the automatic stay under §362(a) and the tolling provision, §108(c). The stay, which is quite broad, applies to actions to collect or recover on a claim. *Burton v. Infinity Capital Mgmt.*, 862 F.3d 740, 746-47 (9th Cir. 2017). Among other things, the stay applies to the commencement or continuation of an action, the enforcement of a judgment, or any act to enforce a lien. 11 U.S.C. §362(a)(1), (2), (4). Because bankruptcy cases can take years to conclude, the Code provides a tolling statute to preserve the interests of creditors who are precluded from taking action by the stay. 11 U.S.C. §108(c) ("if applicable nonbankruptcy law … fixes a period for commencing or continuing a civil action in a court other than a bankruptcy court on a claim against the debtor, … and such period has not expired before the date of the filing of the petition, then such period does not expire until … 30 days after notice of

Continued on page 10…

Ninth Circuit Update
Continued from page 9…

the termination or expiration of the stay under section 362"). The nonbankrutpcy law at issue was California's ORAP statute, which provides a mechanism for creditors to conduct supplemental proceedings against a judgment debtor. CAL. CIV. PROC. CODE § 708.110(a). By serving the order on the judgment debtor, the judgment creditor creates a lien against the judgment debtor's personal property, which lien is valid for one year unless renewed or terminated. CAL. CIV. PROC. CODE §708.110(d).

The panel then addressed Daff's statutory construction argument. Because §108(c)'s language matches the language of §362(a)(1) (commencing or continuing an action), but §108(c) does not include language from §362(a)'s other subsections (such as enforcing a judgment), such identical language should be interpreted so that §108(c) applies only to continuing an action, not enforcing a judgment. Moreover, Daff reasoned, "treating the enforcement of a judgment as the continuation of a civil action would render the subsections of the stay provision redundant." Op. at 8.

The panel, however, dismissed Daff's argument, which it noted was premised on the assumption that §362(a)'s enumerated categories of forbidden creditor actions are mutually exclusive. They are not. 3 COLLIER ON BANKRUPTCY ¶ 362.03 (Alan N. Resnick & Henry J. Sommers, eds., 16th ed. 2017) (§362(a)'s "language is from time to time duplicative," which ensures "virtually all acts to collect claims and all actions that would affect property of the estate are stayed").

Significantly, Daff's argument did not account for Ninth Circuit precedent. In *Spirtos*, the panel held that §108(c) tolled the period in which a judgment creditor could renew a California state court judgment, 221 F.3d at 1080; and in *Miner Corp. v. Hunters Run Ltd. P'ship (In re Hunters Run Ltd. P'ship)*, the panel held that §108(c) tolled the time during which a creditor could enforce a mechanic's lien, 875 F.2d 1425, 1428 (9th Cir. 1989). In other words, §108(c) "extends the limitations period so long as the creditor is barred by the automatic stay from enforcing its judgment against the property of the estate." *Spirtos*, 221 F.3d at 1081 (citing *Hunters Run*, 875 F.2d at 1428).

While Daff attempted to distinguish the mechanic's lien in *Hunters Run* from the judgment lien at issue, the panel opined that *Hunters Run* and *Spritos* are in accord with other circuit precedent that holds §108(c) tolls the time during which a judgment lien may be renewed. *Morton v. Nat'l Bank of N.Y.C. (In re Morton)*, 866 F.2d 561, 566 (2d Cir. 1989) (because the judgment lien fixed the time during which the judgment could be enforced, "[s]uch an execution is supplemental to the original action that gave rise to the judgment, and is part of a continuing action against the debtor") (internal quotations and citation omitted). Accordingly, the panel held "that the period in which a creditor may enforce a judgment by executing on a lien constitutes the continuation of the original action that resulted in the judgment." Op. at 14.

Hon. Kim M. Wardlaw's dissent emphasizes §108(c)'s plain language, which should apply to toll fixed periods of time only "for commencing or continuing a civil action [.]" Op. at 14 (citing 11 U.S.C. § 108(c)); *see, also, United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 242 (1989) ("The plain language of legislation should be conclusive, except in the rare cases in which the literal application of a statute will produce a result demonstrably at odds with the intention of its drafters."). In Judge Wardlaw's view, Good's ORAP lien was secret in nature and attached only to personal property, and accordingly, should not be subject to the Code's tolling provision; after all, an ORAP lien is a mechanism to enforce a judgment, which by its very terms ends a civil action. Using another canon of statutory interpretation, Judge Wardlaw would hold §108(c) to be inapplicable to toll fixed periods for enforcing judgments—exactly what an ORAP lien is created to do. *See, In re Hilde*, 120 F.3d 950, 955 (1997) ("When a statute omits a specific matter from its coverage, the inclusion of such a matter in another statute on a related subject demonstrates an intent to omit the matter from the coverage of the statute in which it is not mentioned.").

For Judge Wardlaw, *Spirtos* and *Hunters Run* are inapposite as each concerned renewing a claim, not priority. First, at issue in *Spirtos* was a judgment, not a lien, and renewing a judgment is the type of continuation of a civil action contemplated by §108(c). The majority goes too far in extending *Spirtos*'s holding to an ORAP lien.

Second, *Hunters Run* involved a mechanic's lien that would expire within eight months unless an action was commenced to foreclose it. Thus, the tolling issue there concerned the time during which a creditor may commence a civil action—clearly fitting within §108(c)'s scope.

Third, the judgment and lien in *Spirtos* and *Hunters Run* were recorded and publicly available. In both cases, renewing the judgment or filing suit to enforce the mechanic's lien constituted commencing or continuing a civil action, and §108(c) operated to save the creditors' claims. Here, the ORAP lien is secret, created by service, and upon expiration, "only deprives Good of priority." Op. at 17. But §108(c)'s purpose is to prevent debtors from using a bankruptcy filing as a means of invalidating a claim via statutes of limitation.

Continued on page 11…

Ninth Circuit Update
Continued from page 10…

Section 108(c)'s "purpose is not forwarded by application" to disputes regarding loss of priority. Op. at 18 (quoting *Hazen First State Bank v. Speight*, 888 F.2d 574, 577 (8th Cir. 1989) (holding §108(c) inapplicable to a subordination agreement's expiration)).

Finally, Judge Wardlaw dismissed the bankruptcy appellate panel's concern that if §108(c) failed to toll an ORAP lien, debtors would be empowered to file bankruptcy just to eliminate such claims while enjoying the automatic stay's protections, because the instant facts do not bear out such a concern—that is, the record did not show, and Good did not claim, that the debtor would benefit from Good's loss of priority. And notwithstanding the dissent's textualist overtones, Judge Wardlaw concluded by noting that the majority's opinion could create inequitable results between creditors, which could not possibly be what Congress intended.

Wilson v. Rigby, 909 F.3d 306 (9th Cir. 2018)

At issue: whether a Chapter 7 debtor may exempt a portion of her homestead property's appreciation which accrued post-petition by increasing her homestead exemption claim to the maximum amount authorized under Washington law; and if so, whether the debtor may amend her existing homestead exemption claim to capture a portion of such appreciation. The bankruptcy and district courts ruled that the debtor could not amend her claim exemption. A majority of the panel affirmed, but a lone district judge sitting by designation entered a powerful, 35 page dissent.

On December 18, 2013, Wilson filed her Chapter 7 petition. As of the petition date, Wilson's condominium's estimated value was $250,000, which was subject to a $246,440 mortgage. Wilson scheduled her homestead exemption as $3,560, which equaled the equity she held in her home at that time. On July 18, 2016, Wilson amended her schedules to list the property's value as $412,500 and to claim all fair market value up to the statutory limit. Wilson listed Washington's homestead exemption as the basis for the claimed exemption.

The panel began its analysis by noting that under the "snapshot" rule, a debtor's exemptions are fixed at the petition date. *Wolfe v. Jacobson (In re Jacobson)*, 676 F.3d 1193, 1199 (9th Cir. 2012). The snapshot rule determines which exemptions a debtor may claim and the value of such exemptions. *Gebhart v. Gaughan (In re Gebhart)*, 621 F.3d 1206, 1211 (9th Cir. 2010). The snapshot rule is expressly stated in §522(a)(2), which defines an exemption's value for §522 purposes as fair market value as of the petition date, or the date on which the property subject to the exemption becomes estate property. *See, also,* 11 U.S.C. §541(a)(1) (as of the petition date, all the debtor's legal or equitable interests become the estate's). Following the transfer of the debtor's property to the estate, all "Proceeds, product, offspring, rents, or profits" of same enure to the estate. 11 U.S.C. §541(a)(6); *Schwaber v. Reed (In re Reed)*, 940 F.2d 1317, 1323 (9th Cir. 1991) (interpreting §541(a)(6) to mean appreciation in value of a debtor's home enures to the bankruptcy estate, not the debtor). According to the panel, the value of an exemption is fixed by reference to the petition date.

The panel addressed Wilson's argument that Ninth Circuit precedent allows debtors to benefit from the post-petition appreciation in value of their homestead. *E.g.*, *Alsberg v. Robertson (In re Alsberg)*, 68 F.3d 312, 314 (9th Cir. 1995). The panel distinguished *Alsberg* on the ground that California's homestead exemption statute differs materially from Washington's. *Compare* CAL. CIV. PROC. CODE §704.730, *with* RCW 6.13.030. According to the panel, under California law, debtors are entitled to claim an exempt amount based on demographic criteria, not home equity, as under Washington law. "Because the value that can be claimed in California is determined by demographic criteria, the homestead amount claimed at filing may exceed home equity on that petition date." Op. at 9. Wilson was entitled to that homestead exemption she could claim on the petition date, which under Washington law, means her net equity as of the petition date.

Hon. Paul C. Huck, United States District Judge for the U.S. District Court for Southern Florida, authored the dissenting opinion. From Judge Huck's perspective, fundamental bankruptcy principles and existing Ninth Circuit precedent should permit Wilson to "exempt a portion of her homestead property's appreciation which accrued postpetition by increasing her homestead exemption to claim the maximum amount authorized by Washington law," and to "amend her existing homestead exemption claim in order to obtain a portion of that appreciation." Op. at 13.

Judge Huck's dissent presents six bases supporting reversal: (i) binding precedent controls and mandates reversal; (ii) persuasive case law suggests reversal is warranted; (iii) exemption amounts are not determined at the petition date; (iv) post-petition appreciation enures to the estate; (v) the snapshot rule; and (vi) guiding bankruptcy principles.

First, *Robertson v. Alsberg (In re Alsberg)*, 161 B.R. 680 (B.A.P. 9th Cir. 1993), *aff'd*, 68 F.3d 312 (9th Cir. 1995), and *In re Gebhart*, 621 F.3d 1206 (9th Cir. 2010), as Ninth Circuit control and mandate reversal. In *Alsberg*, the debtor's homestead was appraised at $259,000 as of the petition date. Believing there to be no equity in the homestead, the debtor did not schedule a homestead exemption. Apparently,

Continued on page 12…

Ninth Circuit Update

Continued from page 11…

the property appreciated in value, as the trustee netted $121,000 from its post-petition sale. The debtor subsequently amended his schedules to claim the maximum exemption allowed under California law, $45,000. The debtor argued that because there was no equity in the property as of the petition date, the estate never had an interest in the property, and thus, the $121,000 should be paid to the debtor, only. Rejecting that argument, the bankruptcy court ruled that the debtor was entitled to the full homestead exemption of $45,000 "because the amount allowable as a homestead is determined when property is sold." 161 B.R. at 682. In considering the trustee's appeal, the bankruptcy appellate panel affirmed, finding that the post-petition appreciation initially vested in the estate, but because an applicable exemption existed, the estate asset of post-petition appreciation would be exempted from the estate. Significantly for Judge Huck, the bankruptcy appellate panel relied on *In re Hyman*, 967 F.2d 1316 (9th Cir. 1992) to reach its conclusion that the homestead exemption amount is determined at the time of sale: "The debtor's right to use the exemption comes into play not upon the filing of the petition, but only if and when the trustee attempts to sell the property." 68 F.3d at 314 (quoting *Hyman*, 967 F.2d at 1321).

While the consolidated appeals addressed in *Gebhart* are factually and legally distinguishable from Wilson's instant appeal, nevertheless *Gebhart* holds that a trustee is not bound by the debtor's scheduled homestead valuation and the debtor cannot prevent the sale of appreciated homestead property even where equity exceeds the statutory maximum exemption amount. Significantly for Judge Huck, the panel in *Gebhart* affirmed the lower courts, which held, consistent with *Alsberg*, that even if the debtor were not entitled to exempt the homestead property itself, the debtor was entitled to the full homestead exemption amount, a portion of which was based on post-petition appreciation of property. 621 F.3d at 1210.

Second, *Straffi v. Morgan (In re Morgan)*, 2017 WL 436257 (D.N.J. Feb. 1, 2017), a factually analogous case, offers persuasive authority that a debtor is entitled to use post-petition appreciation to fund fully a homestead exemption, and that the debtor is entitled to amend her exemption claim by augmenting it to take advantage of such post-petition appreciation.

Third, the majority conflates dicta interpreted out of context with a rule. According to Judge Huck, the majority based its statement that exemption amounts are fixed as of the petition date from reading out of context dicta from *Gebhart*. But the majority's interpretation—that a debtor's homestead exemption, claimed under Washington law, cannot exceed the amount that a debtor claimed on the petition date—is irreconcilable with what the *Gebhart* court actually did (permit the debtors to amend their exemption claims and use a portion of the appreciated property value to do so), and with *Alsberg*. Additionally, consistent with Ninth Circuit precedent, Washington law provides that the amount of a debtor's homestead exemption is determined when the property is sold. *Sweet v. O'Leary*, 88 Wash. App. 199, 200 (1997); *see also Hyman*, 967 F.2d at 1321.

Fourth, the principle that post-petition appreciation enures to the estate is not remarkable in Judge Huck's view, and does not mean a debtor has no "right to revestment of a portion of the net proceeds from the sale of that property pursuant to debtor's homestead exemption." Op. at 41. Simply put, all of a debtor's property must initially enure to the estate before sale proceeds of same are distributed to those claiming interests in the property. *See also Gebhart*, 621 F.3d at 1211 ("the estate is entitled to postpetition appreciation in the value of property a portion of which is otherwise exempt").

Fifth, the Bankruptcy Code states that exemptions are to be determined in accordance with federal or state law applicable on the petition date. 11 U.S.C. §522(b)(3)(A). The majority interprets that statement to extend to a debtor's right to claim an exemption, rather than whether the debtor is entitled to an exemption under the exemption law in force as of the petition date. Under Judge Huck's interpretation, the snapshot rule is not at issue in Wilson's appeal.

Sixth, the rule fashioned by the majority runs counter to three fundamental bankruptcy principles: (1) given the bankruptcy goal of a fresh start for debtors, homestead exemptions should be liberally construed in the debtor's favor, *Schwab v. Reilly*, 560 U.S. 770, 791 (2010); (2) bankruptcy courts are not authorized to deny exemptions unless the Bankruptcy Code so provides, *Law v. Siegel*, 134 S. Ct. 1188, 1197 (2014); and (3) debtors are permitted to amend schedules as a matter of right, *Martinson v. Michael (In re Michael)*, 163 F.3d 526, 529 (9th Cir. 1998), *abrogated on other grounds*, 134 S. Ct. at 1188.

Accordingly, Judge Huck would reverse to allow Wilson to amend her homestead exemption claim to capture the full exemption to which she is entitled.

Continued on page 13…

Ninth Circuit Update

Continued from page 12…

Cobb v. City of Stockton (In re City of Stockton), 909 F.3d 1256 (9th Cir. 2018)

At issue: whether equitable mootness precludes an appeal of a bankruptcy court order denying an objection to the City of Stockton's Chapter 9 Plan of Adjustment. A majority of the panel held that it does.

Where a creditor challenges a plan of reorganization on appeal but fails to seek a stay of the order confirming the plan, the appeal may be dismissed as equitably moot. *See JPMCC 2007-C1 Grasslawn Lodging, LLC v. Transwest Resort Props., Inc. (In re Transwest Resort Props., Inc.)*, 801 F.3d 1161, 1167 (9th Cir. 2015). The panel has previously identified the following factors to determine whether an appeal is equitably moot: (1) whether a stay was sought; (2) whether the plan has been substantially consummated; (3) the requested relief's effect on third parties not before the court; and (4) whether the court can fashion relief without unleashing chaos. *Transwest Resort Props.*, 801 F.3d at 1167-68.

The majority began its analysis by revisiting the salient points in Stockton's pre- and post-confirmation history. Among other things, the city's plan, which became effective in February 2015, provides for the payment of $1.5 billion to twenty classes of claims. Pursuant to the confirmed plan, the city has wired over $13 million to retirees and institutional investors, assigned leases, conveyed real property title, and continues to make plan payments.

Cobb objected to the plan because he sought to have his inverse condemnation claim against the city excepted from discharge. In addition to traditional eminent domain proceedings, California law provides for "quick-take" condemnation in which the locality takes possession after depositing the appraised compensation amount. CAL. CONST. art. I, § 19; CAL. CIV. PROC. CODE § 1255.010; *see also Mt. San Jacinto Cmty. Coll. Dist. v. Superior Court of Riverside Cty.*, 151 P.3d 1166, 1168 (Cal. 2007). If the property owner withdraws the appraised compensation, she waives all claims and defenses but for a claim for greater compensation. CAL. CIV. PROC. CODE § 1255.260.

The city appraised Cobb's parcel and deposited the appraised value. Cobb withdrew the compensation funds held on deposit. Stockton's city council issued an Order for Prejudgment Possession in the city's favor and initiated formal eminent domain proceedings. Seven years later, the city's eminent domain action was dismissed because it had not been brought to trial within the requisite five-year time frame. Cobb tried to return the withdrawn funds, which the city would not accept, explaining that the withdrawal was final under California law. Cobb filed a complaint in California state court seeking relief for inverse condemnation, alleging that the amount of just compensation had never been determined. The state court sustained the city's demurrer because, among other reasons, more than five years had elapsed since the taking occurred. On appeal, the California Court of Appeals reversed, as it concluded that Cobb's complaint was timely because the city's occupation did not become wrongful until the eminent domain action was dismissed. The city subsequently filed its Chapter 9 petition. Thus, in Stockton's Chapter 9 case, Cobb holds an unliquidated, disputed, and unsecured claim for money damages.

Cobb objected to the city's plan, which classified his claim as a general, unsecured claim, arguing that his claim was protected by the U.S. Constitution's Fifth and Fourteenth Amendments and, accordingly, could not be impaired. The bankruptcy court overruled Cobb's objection because Cobb's claim was for greater compensation, only; that the Bankruptcy Clause in the U.S. Constitution does not authorize bankruptcy courts to adjust debts for greater compensation; and if the debt were reduced to judgment, such judgment would be deemed a general unsecured claim. Cobb filed a timely appeal with the Eastern District of California but failed to seek a stay of plan confirmation from the bankruptcy court. The parties stipulated to direct appeal to the Ninth Circuit.

The panel then explained why equitable mootness required dismissal of Cobb's appeal. First, Cobb failed to seek a stay of the confirmation order. Because "[f]inality is essential to the success of bankruptcy reorganization plans[,]" the Ninth Circuit requires parties challenging a reorganization plan on appeal to seek a stay of proceedings. *See Trone v. Roberts Farms, Inc. (In re Roberts Farms, Inc.)*, 652 F.2d 793, 798 (9th Cir. 1981). After all, by requesting a stay, the appellant puts affected parties on notice that the plan at issue may be subject to appellate review.

Second, there was no dispute that the plan had been substantially consummated, as the city had operated under the plan for years, during which time the city made payments and transferred property.

Third, the panel reasoned that the requested relief, if granted, would bear unduly on innocent parties because reversing the confirmation would "undermine the settlements negotiated with unions, pension plan participants and retirees, bond creditors, and capital market creditors, all of which were built into the reorganization plan." Op. at 15. The panel dismissed Cobb's argument that his claim was merely monetary and

Continued on page 14…

Ninth Circuit Update
Continued from page 13…

would have little impact on interested parties because his multi-million dollar claim "on its face" would impact the city considerably. *Id.*; *see, also, Franklin High Yield Tax-Free Income Fund v. City of Stockton (In re City of Stockton)*, 542 B.R. 261, 278 (B.A.P. 9th Cir. 2015) ("To reverse [Stockton's] Confirmation Order at this point would have a potentially devastating impact on creditor constituencies whose settlements with the City were incorporated in the Plan and who are not appearing before us in this appeal."). Among other reasons, allowing the claim would force the city to reconsider its long-term projections and budget, upon which the bankruptcy court's feasibility findings relied. *Franklin*, 542 B.R. at 276.

Fourth, the panel concluded that it could not fashion equitable relief without unwinding the confirmed plan. Cobb's appeal asked the panel to reverse the confirmation order, which, in Cobb's view, should lead to the Chapter 9 case's dismissal because an inability to confirm a Chapter 9 plan warrants dismissal. By reversing the confirmation order, the panel would unleash chaos into the case by undoing "years of carefully negotiated settlements." Op. at 18; *see also Franklin*, 542 B.R. at 278 ("Reversing [Stockton's] Confirmation Order would 'knock the props out from under' the plan and would leave the bankruptcy court with an unmanageable situation on remand.") (internal citation omitted). Accordingly, the panel held that equitable mootness required dismissal of Cobb's appeal.

The panel then brushed aside Cobb's constitutional challenge because bankruptcy impacts the Takings Clause only where the creditor holds in rem rights. After all, monetary claims can be adjusted in bankruptcy. Here, the panel explained, Cobb had foregone any in rem rights when the quick take funds were withdrawn, and when he allowed the city to build a public road on the property. Even if the opposite were true, property rights protected by the Fifth Amendment are capable of being adjusted in bankruptcy. *See Bennett v. Jefferson Cty.*, 2018 WL 3892979, at *7 (11th Cir. 2018) (quoting *Henderson v. United States*, 568 U.S. 266, 271 (2013) ("[T]he mere fact that a potential or actual violation of a constitutional right exists does not generally excuse a party's failure to comply with procedural rules for assertion of the right. A 'constitutional right, or a right of any other sort, may be forfeited in criminal as well as civil cases by the failure to make timely assertion of the right before a tribunal having jurisdiction to determine it.'"); *see also George v. City of Morro Bay (In re George)*, 322 F.3d 586, 590-91 (9th Cir. 2003) (per curiam) (approving bankruptcy court's dismissal of takings claim in its entirety). But here, Cobb filed an unsecured proof of claim, never sought to have his debt excepted from discharge or otherwise have his claim ruled secured, and failed to object to the disclosure statement. Accordingly, the Fifth Amendment does not exempt Cobb's claim from reorganization, and the bankruptcy court properly overruled his objection.

Hon. Michelle Freidland authored a thoughtful dissent. Because the Takings Clause "constrains the powers granted to Congress by the Bankruptcy Clause of Article I," Judge Friedland would have heard the merits of Cobb's appeal and allowed Cobb's inverse condemnation action to go forward in state court.

Notwithstanding the majority's focus, Judge Friedland opined that equitable mootness was not implicated by Cobb's appeal. While Cobb initially framed his appeal as an objection to the plan, he sought only to have his claim "pass through bankruptcy unaffected." *In re Towers*, 162 F.3d 952, 953 (7th Cir. 1998). Because Cobb's individual claim should have been excepted from discharge, Cobb's requested relief would not unwind the plan. After all, assuming Cobb were to prevail, his claim would exist outside of the plan, the terms of which would remain undisturbed. While the majority invokes *Franklin* for support of its conclusion that Cobb's requested relief could jeopardize the city's reorganization, the bankruptcy appellate panel in that case actually noted that claims solely for monetary relief would not require a plan to be disturbed, and thus would not be moot. *Franklin*, 542 B.R. at 277.

Even if invoking equitable mootness was warranted, the factors in determining whether it requires dismissing Cobb's appeal had not been satisfied. It would have been futile for Cobb to seek a stay of the confirmation order when asserting that his claim should not even be part of the plan. And because he already asked the bankruptcy court to rule on whether his claim was protected by the Fifth and Fourteenth Amendments, and the court did so, it would have been unnecessary for Cobb to seek a stay in order for the bankruptcy court to consider the question.

As for the appeal's merits, Judge Friedland disagreed with the majority's conclusions that (i) Cobb waived all property rights under California law, and (ii) a claim for just compensation can be reduced in bankruptcy. First, the majority mischaracterizes Cobb's claim as merely statutory. However, when the city condemned the property, Cobb obtained a constitutional right to just compensation. While it may be correct to characterize Cobb's claim as a statutory claim for money damages, the claim is nevertheless a constitutional claim, too. Moreover, when Cobb withdrew the quick-take funds, his right to just compensation did not disappear. *See, Mt. San Jacinto*, 151 P.3d at 1175 (explaining that the quick-take mechanism's constitutionality rests in part on allowing continuing claims for greater compensation following withdrawal of quick-take funds).

Continued on page 15…

Ninth Circuit Update
Continued from page 14…

Second, irrespective of Title 11, the city should be obligated under the Constitution to provide just compensation for any taking of private property. While the Constitution empowers Congress to enact uniform bankruptcy laws, U.S. Const. art. I, § 8, cl. 4, Congress "is of course subject to the strictures of the Bill of Rights, and may not transgress those strictures," *Cal. Bankers Ass'n v. Shultz*, 416 U.S. 21, 77 (1974). *See also Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555 (1935) (noting that "[t]he bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment"); *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 149, 155 (1974) (approving reorganization notwithstanding potentially underfunded takings because creditors had recourse to a mechanism for recovering just compensation deficiencies); *United States v. Sec. Indus. Bank*, 459 U.S. 70 (1982) (reconfirming that "[t]he bankruptcy power is subject to the Fifth Amendment's prohibition against taking private property without just compensation"). Accordingly, Judge Friedland would except Cobb's claim from discharge, allowing the claim to pass through the city's bankruptcy.

Easley v. Collection Service of Nevada, 910 F.3d 1286 (9th Cir. 2018)

At issue: whether 11 U.S.C. §362(k) authorizes an award of attorneys' fees and costs incurred by a debtor in successfully challenging an initial award under §362(k). In a 2015 decision, the panel held that §362(k) authorizes an award for fees incurred in defending a judgment entered pursuant to that statute. *In re Schwartz-Tallard*, 803 F.3d 1095, 1101 (9th Cir. 2015) (en banc). Reversing the district court, the panel clarified that §362(k) authorizes an award to a debtor who successfully challenges such an appeal.

The panel began by relaying the facts. On October 31, 2012, the Easleys filed for chapter 13 bankruptcy. The Easleys' schedules listed Bennet Medical Services as the holder of an unsecured, non-priority claim. Bennett, however, had assigned its claim to Collection Service of Nevada ("CSN"), which did not receive notice of the bankruptcy. In July 2013, CSN commenced a collection action in state court. In April 2014, the Easleys received a writ of execution on their earnings from CSN. On April 22, 2014, counsel for the Easleys issued a demand letter to CSN to stop the garnishment. However, the garnishment continued for weeks.

On June 13, 2014, the Easleys moved for a contempt order based on CSN's violating the automatic stay. The bankruptcy court concluded that CSN had willfully violated the stay and awarded $1,295 in damages, as well as $1,277 in attorneys' fees, to the Easleys. The Easleys appealed the award, arguing that the bankruptcy court failed to account for all the attorneys' fees incurred to end the stay violation. The district court affirmed the actual damages award but remanded the attorneys' fee calculation because at that time, the panel entered its decision in *Schwartz-Tallard*. On remand, the bankruptcy court awarded an additional $16,324.40 in attorneys' fees to the Easleys; however, it did not award any fees and costs incurred in the Easleys' appeal on the basis that it lacked jurisdiction to do so, as there was a pending application for the same fees before the district court.

The district court denied the Easleys' motion for fees incurred in their appeal because (1) they failed to file points and authority in support of their fee request, as required by District of Nevada Civil Local Rule 7-2(d), and (2) it interpreted *Schwartz-Tallard* to entitle a party to an award of attorneys' fees only when that party succeeds in defending its judgment award under §362(k) on appeal, and because the Easleys challenged their own award, and not CNS, the Easleys could not recover their appellate fees under §362(k).

The panel then noted that it reviews both district court rulings based on local rules and award of attorneys' fees for abuse of discretion. *All. of Nonprofits for Ins., Risk Retention Grp. v. Kipper*, 712 F.3d 1316, 1327 (9th Cir. 2013); *Shaw v. City of Sacramento*, 250 F.3d 1289, 1293-94 (9th Cir. 2001). Nevertheless, where the primary issue on appeal is legal rather than factual, the panel reviews fee awards de novo. *Harris v. Maricopa Cty. Superior Court*, 631 F.3d 963, 970 (9th Cir. 2011).

The panel then analyzed the district court's application of Local Rule 7-2(d). Although it is the rare case in which the panel questions a district court's application of local rules, *United States v. Warren*, 601 F.2d 471, 474 (9th Cir. 1979), the panel explained that the Easleys' appeal was one of those rare cases. In support of their request for an award of fees incurred on appeal, the Easleys submitted a "motion for attorney fees and cost for appellate work." Op. at 8. Which motion, although not labeled a memorandum of points and authorities, clearly was a request for appellate fees supported by time records and legal authority. Accordingly, the panel determined that the district court abused its discretion in denying the request for relief under the local rule.

Next, the panel clarified *Schwartz-Tallard* for the district court. Absent statutory authority, fees are not awarded to the prevailing party. *Key Tronic Corp. v. United States*, 511 U.S. 809, 819 (1994) (explaining the American Rule). Section 362(k)(1) authorizes attorneys' fee awards to debtors actually

Continued on page 16…

Ninth Circuit Update

Continued from page 15…

damaged by willful stay violations. The panel had previously held that once the stay violation has ended, attorneys' fees no longer represent actual damages. *Sternberg v. Johnston*, 595 F.3d 937, 947 (9th Cir. 2010). *Schwartz-Tallard* overruled *Sternberg.* 803 F.3d at 1101 (holding that §362(k) is best read as authorizing an award of attorneys' fees and costs incurred in prosecuting an action for damages under the statute). After all, by permitting debtors to recover fees and costs, the Code permits debtors to take actions to protect themselves and their estates where otherwise they would not have the means to do so. 803 F.3d at 1100. And, where a party is entitled to an award at trial, that party is generally able to recover fees incurred in defending on appeal. 803 F.3d at 1101.

By interpreting *Schwartz-Tallard* to deny the Easleys their appellate fees and costs because they themselves appealed the district court's decision, the district court erred. Section 362(k) not only provides for damages, but it is also a fee-shifting statute that shifts fees in one direction only—to the debtor. *See Blixseth v. Yellowstone Mountain Club, LLC*, 854 F.3d 626, 629 n.3 (9th Cir. 2017) (fee-shifting rather than damages provision). Moreover, fee-shifting statutes allow for fees on fees. *In re Nucorp Energy, Inc*., 764 F.2d 655, 659-60 (9th Cir. 1985) ("In statutory fee cases, federal courts, including our own, have uniformly held that time spent in establishing the entitlement to and amount of the fee is compensable."). By permitting fees on fees, the underlying fee award is not diluted by the necessary time and effort spent to protect the award on appeal. *Nucorp*, 764 F.2d at 660; *Se. Legal Def. Grp. v. Adams*, 657 F.2d 1118, 1126 (9th Cir. 1981). Where a creditor fails in challenging an award on appeal, the panel reasoned, "the party who violated the stay should continue to pay for its harmful behavior." Op. at 12.

Accordingly, the panel reversed and remanded.

IPC (USA), Inc. v. Ellis (In re Pettit Oil Co.), 917 F.3d 1130 (9th Cir. 2019)

At issue: whether a trustee's interest in sale proceeds of consigned goods held by the debtor-consignee on the petition date is superior to the consignor's interest where the consignor failed to perfect its interest in the consigned goods prior to the petition date. The panel held so, affirming the bankruptcy appellate panel's affirmance of the bankruptcy court's summary judgment in favor of the trustee.

Prior to the petition date, the debtor distributed bulk petroleum products. As part of its business operations, the debtor used "card lock" sites from which customers purchased fuel using access cards. The debtor had executed a consignment agreement with IPC pursuant to which IPC delivered consigned fuel to the debtor's card lock sites and paid the debtor a monthly commission. Title to the fuel remained with IPC until transferred to the purchaser, who paid IPC directly through invoices prepared by the debtor. According to the agreement, if a purchaser paid the debtor rather than IPC, the debtor would remit such payment to IPC. Such proceeds were either cash or accounts receivable. IPC never filed a financing statement to perfect its interests in the consigned fuel or the proceeds therefrom. IPC appealed the bankruptcy court's ruling that its interests in the proceeds were property of the estate, arguing that UCC §9-319(a) covers goods but not the proceeds of same.

The panel began its analysis by discussing §544(a)(1) and a trustee's avoiding powers, explaining that a creditor, such as IPC, can overcome the trustee's interest in an estate asset only if it can show that its interest primes a judicial lien. IPC argued that even though UCC §9-319(a) provided the debtor with the same rights and title in the fuel that IPC had, IPC's interests in the accounts and proceeds therefrom were superior to the debtor's because the text of §9-319(a) does not expressly mention proceeds. The panel rejected this argument on several grounds. First, the panel cited "numerous references" in the UCC that treat a consignment as a security interest. As such, it stands to reason that a consignor's interests in goods should be construed to be a security interest for purposes of perfection and priority, unless the UCC states otherwise. The panel pointed specifically to §9-324(b), under which a perfected security interest in inventory primes a conflicting interest in the same inventory and also has priority in the proceeds of same. The panel reasoned that because IPC would have had a perfected security interest in the fuel sale proceeds if it had perfected its interest in the fuel itself, that the reciprocal rule should also be given effect; namely, IPC couldn't have priority in the fuel proceeds because it failed to perfect its interest in the fuel.

Second, using a canon of statutory interpretation, the panel interpreted the statute as a whole, and gave effect to each word so as not to render other provisions inconsistent, meaningless, or superfluous. *United States v. Neal*, 776 F.3d 645, 652 (9th Cir. 2015). The panel held that in interpreting Article 9 as a whole, the term "goods" in §9-319(a) includes the proceeds of such goods and that "Article 9's priority and perfection rules apply with equal force to such proceeds."

Third, the panel distinguished retention of title for default and remedy purposes from the determination of priority among competing interests in goods and proceeds. *See,* UCC § 9-202, Comment 3.a.

Continued on page 17…

Ninth Circuit Update

Continued from page 16…

Fourth, the policy underpinning Article 9's statutory scheme supports the panel's holding; after all, by perfecting security interests, creditors put third parties on notice that they have security interests in goods held by others. *See In re Valley Media, Inc.*, 279 B.R. 105, 125 (Bankr. D. Del. 2002) (noting that §9-319(a)'s purpose is "to protect general creditors of the consignee from claims of consignors that have undisclosed consignment arrangements with the consignee that create secret liens on the inventory"). By holding that Article 9's perfection rules apply to proceeds as well as goods, the panel honored Article 9's notice purpose, which protects creditors who would otherwise misbelieve that certain collateral proceeds would be sufficient to secure a debtor's obligations.

Finally, the panel rejected IPC's additional argument that §544(a) doesn't contain a "reachback" provision allowing the trustee to claim an interest in proceeds generated prior to the petition date. Because §544 grants a trustee "a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien," and because the trustee's interest in fuel proceeds was the same as IPC's, the trustee, like IPC, could have secured a lien on the proceeds. Accordingly, the panel affirmed.

Vibe Micro, Inc. v. SIG Cap., LLC (In re 8Speed8, Inc.), 921 F.3d 1193 (9th Cir. 2019)

At issue: whether the 50 percent shareholder of an involuntary debtor who successfully obtains dismissal has standing to seek an award of fees on the debtor's behalf under §303(i). A majority of the panel affirmed the district court's affirmance of the bankruptcy court's fee request denial. Circuit Judge Mark J. Bennett authored a thoughtful dissent.

At the time of filing, Vibe owned 50 percent of 8Speed8's voting stock. SIG owned contingent shares in 8Speed8 and was a creditor of same. SIG filed an involuntary petition against 8Speed8, which never made an appearance. Instead, Vibe moved to dismiss the case, asking for costs, fees and actual and punitive damages on 8Speed8's behalf under §303(i). At the dismissal hearing, SIG conceded that dismissal was appropriate and the bankruptcy court dismissed the case. However, the court denied Vibe's request for fees and damages under §303(i) on the ground that Vibe did not have standing under §303(i).

The panel majority concluded that *Miles v. Okun (In re Miles)*, 430 F.3d 1083, 1093-94 (9th Cir. 2005) (holding that under §303(i) only the debtor has standing to seek statutory damages resulting from an involuntary filing), easily disposed of Vibe's appeal. Additionally, the panel reasoned, §303(i)'s language is discretionary and, accordingly, a bankruptcy court may refrain from awarding fees and costs.

Believing that the majority relied too heavily on *Miles*, Judge Bennett would not impose such an absolute, inflexible rule, especially to the facts at hand. Deadlocked governance prevented 8Speed8 from appearing in the action and Vibe, an equity-holder, sought an award on behalf of 8Speed8 for obtaining dismissal of the involuntary filing. Additionally, §303(i)(1) expressly permits an award "in favor of the debtor." 11 U.S.C. §303(i)(1). And since §303(i)'s fee-shifting mechanism is designed to deter frivolous filings, Judge Bennett would have remanded for further fact-finding.

Garvin v. Cook Inv. NW et al., 922 F.3d 1031 (9th Cir. 2019)

At issue: whether §1129(a)(3) directs bankruptcy courts to consider whether a plan's substantive provisions violate non-bankruptcy law. In deciding an issue of first impression in the Circuit, the panel affirmed confirmation of the plan because its proposal was not by means forbidden by law.

Five real estate holding companies voluntarily sought Chapter 11 protection. The cases were administratively consolidated. One of the debtors leased real property to a limited liability company that used the premises to grow marijuana. Although apparently in compliance with Washington law, the lease presumably ran afoul of the Federal Controlled Substances Act, 21 U.S.C. §856, which criminalizes leasing space knowingly for the purpose of manufacturing any controlled substance. The bankruptcy court denied the U.S. Trustee's motion to dismiss but invited the Trustee to renew the motion at confirmation.

The debtors' plan provided for the repayment in full of creditors' claims even though it rejected the grow-operation lease. The Trustee filed the sole objection to the plan arguing that it violated §1129(a)(3); however, the Trustee did not renew its dismissal motion at confirmation.

On appeal, the Trustee challenged the bankruptcy court's (i) denial of its motion to dismiss and (ii) confirmation of the plan. First, the panel agreed with the district court that by failing to renew the motion to dismiss, the Trustee had waived its argument that the grow-operation lease evidenced gross mismanagement of the estate under §1112(b)(4)(B). Among other reasons, neither the bankruptcy court nor the district court had an opportunity to consider whether the debtors cured the cause for dismissal within a reasonable time. *See* 11

Continued on page 18…

Ninth Circuit Update

Continued from page 17…

U.S.C. §1129(b)(2) (unusual circumstances exception).

Second, the panel explained that it need only resort to statutory interpretation to resolve the Trustee's confirmation appeal. Section 1129(a)(3) precludes plan confirmation where the plan has been proposed by means forbidden by law. The Trustee argued that because the debtors continue to receive rent from the grow-operation lease, the plan was proposed by means forbidden by law and thus the plan should not have been confirmed. Reviewing *de novo* the bankruptcy court's interpretation of §1129(a)(3), *Tighe v. Celebrity Home Entm't, Inc. (In re Celebrity Home Entm't, Inc.)*, 210 F.3d 995, 997 (9th Cir. 2000), the panel held that §1129(a)(3) directs bankruptcy courts to consider the means by which a plan has been proposed and not the plan's terms, *see Irving Tanning Co. v. Superintendent of Ins. (In re Irving Tanning Co.)*, 496 B.R. 644, 660 (B.A.P. 1st Cir. 2013); *In re Gen. Dev. Corp.*, 135 B.R. 1002, 1007 (Bankr. S.D. Fla. 1991); *but see In re Rent-Rite Super Kegs W. Ltd.*, 484 B.R. 799, 809 (Bankr. D. Colo. 2012) (dismissing Chapter 11 case where debtor could not confirm a plan because a significant portion of its income came from illegal activity). The panel disagreed with *Super Kegs* because that decision failed to reconcile that court's opinion with §1129(a)(3)'s use of the term "proposed" rather than "implementation." Moreover, the panel reasoned, notwithstanding plan confirmation, debtors remain subject to dismissal motions and criminal proceedings. *See In re Food City, Inc.*, 110 B.R. 808, 812 (Bankr. W.D. Tex. 1990). Accordingly, the panel confirmed. ■

☐ Voting Membership: I am an active WSBA member. Please enroll me as a voting member of the Creditor Debtor Rights Section. My $30 annual dues are enclosed.

☐ Non-voting membership: I am not an active WSBA member. Please enroll me as a subscriber member so I can participate and receive your informational newsletter. My $30 is enclosed.

Name____________________

Firm ____________________

Address ____________________

City/State/Zip ____________________

Phone ____________________

Fax ____________________

Email ____________________

Join Today!

The officers of the Creditor Debtor Rights Section urge you to become a voting member of this important section. All members of the Washington State Bar Association are eligible. Simply fill out the form below and mail with a check for $30 to:

Creditor Debtor Rights Section
Washington State Bar Association
1325 Fourth Avenue, Suite 600
Seattle, WA 98101-2539

Current Year: Jan. 1, 2020 – Dec. 31, 2020

Office Use Only
Date
Check #
Total $

RENEW YOUR SECTION MEMBERSHIP

You can use the new myWSBA webpage to renew your membership in the section. Go to www.mywsba.org, and click "join a section" to renew your membership today!

This is a publication of a section of the Washington State Bar Association. All opinions and comments in this publication represent the views of the authors and do not necessarily have the endorsement of the Association or its officers or agents.