Benchnotes

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Eleventh Circuit Opinion Highlights Difficulty of Obtaining Sanctions for Discharge Violations Post-*Taggart*

In *In re Roth*,[1] the Eleventh Circuit Court of Appeals held that monthly information statements sent by a secured lender regarding a debtor's discharged personal liability on a mortgage does not violate the discharge injunction in § 524, even when such letters continued after the delivery of a cease-and-desist notice and two lawsuits being filed. Even if a violation had occurred, the lender would not have been subject to contempt sanctions in light of the U.S. Supreme Court's holding in *Taggart* that there must be "no fair ground of doubt" that the conduct at issue violated the discharge injunction.

The debtor filed a chapter 13 petition and stated that she would surrender a parcel of non-homestead real property. After three years of plan payments, the debtor received a discharge. Although the secured lender never foreclosed, it started sending the debtor monthly information statements post-discharge that (1) stated an amount due and due date, (2) contained a "voluntary" payment coupon and (3) contained a disclaimer stating that the information statement was not intended as an attempt to collect a discharged debt.

The debtor sent the lender a cease-and-desist letter and, when the statements continued, filed a Fair Debt Collection Practices Act action and a motion for sanctions for violating the discharge injunction. The bankruptcy court denied the sanctions motion, and the district court affirmed. The debtor appealed.

The Eleventh Circuit held that the test for whether an act violates the discharge injunction is whether "the objective effect of the creditor's action is to pressure the debtor to repay a discharged debt."[2] Applying this standard, the court found that the debtor had not shown "an improper attempt at debt collection," given the clear disclaimer in the information statements and the "voluntary" label on the payment coupon. The court reasoned that § 524(f) expressly permits a debtor to pay back a discharged debt voluntarily, and that the monthly statements were merely providing "helpful" guidance to the debtor of that option.

Since the court found that the lender's information statements did not violate the discharge injunction, it was not required to consider whether sanctions would have been appropriate. Nevertheless, in *dicta*, the court stated that "even if we reached a different conclusion ... we would nonetheless find that sanctions under § 105 are unavailable under the Supreme Court's recent decision in *Taggart*."[3] The court continued, "The *Taggart* standard is a rigorous one: [I]n order to find that sanctions are appropriate here, we would have to hold that 'there is no objectively reasonable basis for concluding that [the lender's] conduct might be lawful.'"[4] Because the lower courts and the Eleventh Circuit had found that no violation of the discharge injunction occurred, there was more than a fair ground of doubt about whether the discharge order barred the lender's conduct.

The Eleventh Circuit's decision highlights just how difficult it now is to obtain sanctions for a discharge violation. If continued information statements after the transmission of a cease-and-desist letter and the filing of two lawsuits by the discharged debtor do not constitute harassment in violation of the discharge injunction, then it is fair to ask the following question: What type of conduct would actually violate the discharge injunction? If the test for determining a violation is indeed that rigorous, then it is difficult to conceive of many fact patterns where *Taggart*'s "no fair ground of doubt" standard would be met.

Plan Providing Better Treatment for Class Members Who Backstop Rights Offering Deemed Confirmable

In *In re Peabody Energy Corp.*,[5] the Eighth Circuit Court of Appeals upheld confirmation of a reorganization plan over the objection of an *ad hoc* committee of creditors that alleged that the plan unfairly discriminated against them *vis-à-vis* other members of their class by providing better treatment to such creditors based on their agreement to backstop the debtors' rights offering. In so holding, the court rejected the *ad hoc* committee's argument that the plan violated the Supreme Court's seminal ruling in *Bank of America v. 203 N. LaSalle St. P'ship*.

The debtor, a large coal company, filed a chapter 11 petition in part to address a dispute with several of its secured and senior unsecured creditors. Post-petition, the parties to the dispute went to voluntary mediation and reached a settlement that paved the way for a reorganization plan. Members of the objecting *ad hoc* committee did not participate in the mediation, although they did receive notice of it.

1 *Roth v. Nationstar Mortg. LLC (In re Roth)*, 2019 WL 4047509 (11th Cir. Aug. 28, 2019).
2 *Id.* at *4 (citing *In re McLean*, 794 F.3d 1313, 1322 (11th Cir. 2015)).
3 *Id.* at *5 (citing *Taggart v. Lorenzen*, 139 S. Ct. 1795, 1799 (2019)).
4 *Id.*
5 *Ad Hoc Comm. of Non-Consenting Creditors v. Peabody Energy Corp. (In re Peabody Energy Corp.)*, 2019 WL 3756884 (8th Cir. Aug. 9, 2019).

The plan called for the debtors to raise $1.5 billion in new money to fund distributions to creditors and the chapter 11 process. Common stock would be sold to creditors to raise half of the funds; the remaining $750 million would be raised by offering preferred stock to the settling creditors at a discount. In order to be eligible to purchase the preferred stock, a creditor needed to (1) purchase a certain amount of preferred stock, (2) commit to backstop the stock sales and (3) support the plan. One tranche of the preferred stock offering was offered solely to the settling creditors, whereas other tranches were made available to all creditors. The *ad hoc* committee members elected not to participate in any part of the private placement and objected to the plan. The plan was supported by all 20 creditor classes and approved by the bankruptcy and district courts.

The Eighth Circuit affirmed the lower courts' approval of the plan. The primary legal argument asserted by the *ad hoc* committee was that the right of the settling creditors to participate in the private placement resulted in unequal treatment of creditors within the same class in violation of § 1123(a)(4), which mandates that a chapter 11 plan must "provide the same treatment for each claim or interest of a particular class." The *ad hoc* committee also argued that *203 N. LaSalle* precluded plan confirmation, noting that the Supreme Court rejected a reorganization plan in that case because it gave a debtor's prebankruptcy equityholders the exclusive opportunity to receive ownership interests in the reorganized debtor on account of, at least in part, the old equity's prior interest.[6]

The court rejected the *ad hoc* committee's arguments, noting that other circuits have agreed that "a reorganization plan may treat one set of claim holders more favorably than another so long as the treatment is not for the claim but for distinct, legitimate rights or contributions from the favored group separate from the claim."[7] Here, the court found that the opportunity to participate in the private placement was not "treatment for" the settling creditors' claims, but rather was consideration for the new commitments being made by them.

In addition, the court distinguished *203 N. LaSalle* by noting that here, unlike there, the objectors were not completely excluded from the opportunity to participate in the private placement. The *ad hoc* committee members, the court found, had elected not to participate.

Miscellaneous

• *In re Big Dog II LLC*, 602 B.R. 64 (Bankr. N.D. Fla. 2019) (bankruptcy court found that secured creditor with limited equity cushion of between 3 to 14 percent is not adequately protected when there is evidence of deferred maintenance and needed repairs; however, denial of creditor's request for stay relief was appropriate in light of evidence that debtor had ability to quickly refinance property);

• *In re Wright*, --- B.R. ----, 2019 WL 3315428 (Bankr. D. Conn. 2019) (bankruptcy court denied confirmation of chapter 13 plan wherein debtor proposed that interest would not accrue on her nondischargeable student loan debt during five-year payment period of her chapter 13 plan; bankruptcy court found that while § 1322(b)(2) allows for chapter 13 plan to modify repayment terms of nondischargeable student loan, it does not allow court to partially discharge student loan obligation; suspension of otherwise nondischargeable interest accruing would have constituted partial discharge);

• *Advance Credit Inc. v. Gamboa (In re Gamboa)*, 2019 WL 3917180 (11th Cir. Aug. 19, 2019) (Eleventh Circuit held that chapter 13 debtor could claim homestead exemption under Florida law for his trailer and surrounding 14-acre parcel of land, notwithstanding fact that land was zoned as agricultural, not residential, property; in order to establish homestead in Florida, debtor only need to (1) show intent to make the property his permanent residence, and (2) live on the property);

• *Conrad v. Dehart (In re Conrad)*, 2019 WL 3800226 (Bankr. M.D. Pa. Aug. 13, 2019) (chapter 13 debtors moved to modify their confirmed chapter 13 plan, and trustee objected; court held that party seeking to modify confirmed chapter 13 plan does not have to make threshold showing of "change in circumstances"; Nevertheless, motion was denied because debtors were not proposing to commit all of their monthly disposable income and were seeking to reduce 100 percent distribution to unsecured creditors just over seven months after plan was confirmed);

• *Double Eagle Energy Services LLC v. Markwest Utica EMG LLC*, 2019 WL 4010687 (5th Cir. Aug. 26, 2019) (chapter 11 debtor brought action against defendants in bankruptcy court for breach of contract relying on "related to" jurisdiction; debtor subsequently assigned cause of action to one of its creditors, and defendants moved for dismissal of suit on theory that assignment terminated subject-matter jurisdiction; Fifth Circuit held that "time-of-filing rule" is hornbook law; if related-to jurisdiction exists at outset of lawsuit, court retains jurisdiction even if basis for such jurisdiction subsequently disappears);

• *In re FirstEnergy Solutions Corp.*, 2019 WL 4127191 (Bankr. N.D. Ohio Aug. 29, 2019) (at disclosure statement phase of case, bankruptcy court held that debtors' plan was patently unconfirmable because it contained broadly worded third-party releases in favor of nondebtors; acknowledging circuit split on issue of third-party releases, court stated: "While possible within the Sixth Circuit, the nonconsensual release of third-party claims against nondebtors remains an exception, not the rule. [S]uch an injunction is a dramatic measure to be used cautiously ... [and therefore] enjoining a non-consenting creditor's claim is only appropriate in unusual circumstances.");

• *In re Life Partners Holdings Inc.*, 2019 WL 3987707 (Bankr. N.D. Tex. Aug. 22, 2019) (bankruptcy court held that increased U.S. Trustee fee schedule for large chapter 11 cases set forth in 28 U.S.C. § 1930(a)(6) does not apply to chapter 11 cases that were filed prior to amendment's effective date; even if increased fee schedule did apply, court held that it is unconstitutional because it violates Uniformity and Bankruptcy Clauses of Constitution given that certain jurisdictions have elected not to implement U.S. Trustee Program);

6 *Id.* at *4 (discussing *Bank of Am. Nat'l Trust & Sav. Ass'n v. 203 N. LaSalle St. P'ship*, 526 U.S. 434, 119 S. Ct. 1411 (1999)).

7 *Id.*

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• *In re Sterling*, 2019 WL 3788242 (7th Cir. Aug. 13, 2019) (Seventh Circuit held that even though creditor had received notice of chapter 7 debtor's discharge, creditor's collection lawyer did not violate discharge injunction when he had debtor jailed for nonpayment of discharged debt, because lawyer had not been informed by his client of discharge; conversely, reversing lower courts, Seventh Circuit found that creditor was in contempt for violating discharge injunction, even though creditor itself did not attempt to collect debt; creditor knew of discharge and was bound by conduct of its lawyer);

• *Thomas v. Department of Education (In re Thomas)*, 931 F.3d 449 (5th Cir. 2019) (unemployed chapter 7 debtor with less than $200 per month in income and degenerative condition that made it impossible for her to obtain employment that involved standing sought to discharge her student loan debt; expanding on *Brunner* test and its own precedent, Fifth Circuit held that student loans must not be discharged "unless requiring repayment would impose intolerable difficulties on the debtor"; court rejected arguments by debtor and *amici* that from practical and policy standpoint, *Brunner* no longer suits the times, concluding that recent revisions to Bankruptcy Code evince intent to limit bankruptcy's use as means of offloading student loan debt except in all but most compelling circumstances);

• *Todeschi v. Juarez (In re Juarez)*, 603 B.R. 610 (B.A.P. 9th Cir. 2019) (addressing issue on which courts are divided, Ninth Circuit BAP held that individual chapter 11 debtor does not violate absolute-priority rule in cramdown by retaining exempt property without paying creditors in full; debtor was not retaining exempt property on account of its interest but was rather retaining it by operation of exemption statutes, which exclude such property from estate); and

• *Touroo v. Terry (In re Touroo)*, 2019 WL 2590751 (E.D. Mich. June 25, 2019) (debtors completed all of their ordinary chapter 13 plan payments but failed to turn their 2017 tax refund over to trustee; two weeks after last scheduled plan payment, trustee filed motion to dismiss case without discharge due to debtors' failure to turn over refund; bankruptcy court dismissed case, believing that it did not have discretion to allow late plan payment, under §§ 1322(d) and 1329(c), which generally prohibit chapter 13 plans from running longer than five years; noting split in authority, district court held that bankruptcy courts have discretion to allow debtor to cure payment default under chapter 13 plan more than five years after confirmation). abi