Sidenotes File

to accompany

The ABCs of Debt: A Case Study Approach to Debtor/Creditor Relations and Bankruptcy Law

Sixth Edition

Stephen P. Parsons, J.D.

Copyright © 2022 CCH Incorporated.

Published by Wolters Kluwer in New York.

Wolters Kluwer Legal & Regulatory US serves customers worldwide with CCH, Aspen Publishers, and Kluwer Law International products. (www.WKLegaledu.com)

No part of this publication may be reproduced or transmitted in any form or by any means, electronic or mechanical, including photocopy, recording, or utilized by any information storage or retrieval system, without written permission from the publisher. For information about permissions or to request permissions online, visit us at www.WKLegaledu.com, or a written request may be faxed to our permissions department at 212-771-0803.

To contact Customer Service, e-mail customer.service@wolterskluwer.com, call

1-800-234-1660, fax 1-800-901-9075, or mail correspondence to:

Wolters Kluwer

Attn: Order Department

PO Box 990

Frederick, MD 21705

ABCs of Debt 6th edition

Sidenotes File

Chapter One

Side Note 1-1: Origins of Consumer Debt in America

The origins of what has become modern-day consumer credit go back to 1812 when Cowperthwaite & Sons, a New York City furniture retailer, began allowing customers to pay for their furniture in installments. The practice of selling on credit coincided with the industrial revolution and fueled the demand for farm equipment like Cyrus McCormick's Virginia Reaper and home appliances like the new Singer sewing machine. An excellent source for learning more about the history of consumer credit is *Financing the American Dream: A Cultural History of Consumer Credit*, by Lendol Calder (Princeton, N.J.: Princeton U. Press, 1999).

Side Note 1-2: Debtors, Creditors, and the Constitutional Convention of 1787

Debtor-creditor relations played a significant role in the decision of this country's founding generation to hold what is now remembered as the constitutional convention in Philadelphia, Pennsylvania, in the summer of 1787. You may find it interesting to learn more about the history of Shay's Rebellion (which actually began in the summer of 1786 and resulted in bloodshed in January 1787) and its role in inspiring the convention in Philadelphia the following summer that resulted in the writing of our Constitution. As one early historian said concerning the rebels, "They groaned under ancient debts, made still more burdensome by an increase in interest." Here are some good sources to learn more: *History of the Insurrections in Massachusetts in 1786 and of the Rebellion Consequent Thereon*, by Gorge Richards Minot (New York: Da Capo Press, 1971; original dated 1788); *Shay's Rebellion: The Making of an American Agrarian Insurrection*, by David P. Szatmary (Amherst: University of Massachusetts Press, 1980); *Shay's Rebellion*, by Leonard L. Richards (Philadelphia: University of Pennsylvania Press, 2002); and *The Summer of 1787: The Men Who Wrote the Constitution*, by David O. Stewart (New York: Simon & Schuster, 2007).

Chapter Two

Side Note 2-1: Credit Reports and the Regulation of CRAs

For the Individual Consumer

A credit report is a compilation of the debt history and bill-payment record of a consumer. Credit reports are compiled by businesses known as credit reporting agencies (CRAs)or credit bureaus using information supplied by a consumer's creditors (e.g., credit card issuers, mortgage holders, auto financing companies, landlords), debt collection agencies (see Chapter Six), and public records including court records (e.g., bankruptcy filings and collection suits). The reports are compiled and sold by the

credit reporting agency to persons and businesses authorized to investigate the credit worthiness or financial responsibility of the consumer. CRAs and the contents of credit reports, access to them, use of them, and correction of errors in them is governed by the Fair Credit Reporting Act (FCRA), 15 U.S.C. §1681 et seq., and its implementing regulation, Regulation V (12 CFR Part 222). Many states supplement the provisions of the FCRA with their own statutes or regulations. Separate from the credit report itself, credit reporting agencies calculate and make available for purchase a credit score for the consumer.

There are a number of different credit scoring models but the most popular one is the FICO credit-risk score developed by Fair Isaac Corporation of San Rafael, California. FICO scores range between 300 and 850: the higher the score, the greater the perceived credit worthiness of the consumer. The score is calculated based on a statistical analysis of the relevant data in the consumer's credit report (e.g., length of credit history; types of loans or credit obtained; timeliness of payments; on revolving credit accounts, the ratio of balance owed to credit limits; credit or loan applications denied; collection actions and court judgments; tax or other involuntary liens; bankruptcies filed). In 2021 the median FICO score was 711.

The data contained in the credit report, and the credit score in particular, are used by those authorized to access the data to make decisions such as whether to make a loan or extend credit to the consumer, whether to lease a house or apartment to them, whether to issue a policy of insurance and the amount of the premium (consumers with higher credit scores often get lower premiums), and even whether to hire them for a job. The consumer's credit score may not only determine whether a loan will be made or credit extended, but the size of loan or amount of credit the lender is willing to extend to the consumer and even the interest rate to be charged. Consumers who present safer credit risks to lenders often receive more generous loans or higher credit limits at lower interest rates and even lower premium rates on insurance.

Approximately 3 billion consumer credit reports are issued by credit reporting agencies each year in the United States and more than 36 billion updates are made to credit reports annually.

Today, about 96% of employers to perform routine background checks on job applicants which typically include accessing the applicant's credit history. Such practices raise a number of questions regarding relevance and privacy: Is it right for a well-qualified person in need of a job to be eliminated from consideration solely because of a poor credit history? Should we have more controls on the circumstances under which an employer can check a worker's credit history? Should we have more controls over the use that an inquiring employer can make of that information? In a handful of states, restrictions have been adopted limiting the use of a credit report/score in making employment decisions unless one's credit risk is specifically relevant to the position. Your state? Worth a look.

The Federal Reserve Board's Regulation B, 12 CFR Part 202, implementing the Equal Credit Opportunity Act, requires that any scoring model used to calculate a credit score be "empirically derived, demonstrably and statistically sound." A lender cannot use any credit score that was calculated on a scoring model using prohibited factors such as gender, race, color, religion, national origin, marital status, that all or part of the applicant's income derives from public assistance, or that the applicant is or is likely to become a parent. The age of an applicant cannot be used as a negative factor by the scoring model though it can be considered as a relevant predictive variable. When credit is denied to an applicant, the applicant is entitled to be notified in writing of the adverse action and, upon request made within 60 days following the notification, be given specific reasons for the denial. General statements that the application did not meet the lender's minimum requirements or that the applicant's

credit score was too low are insufficient. The Dodd-Frank Act requires the lender to provide the borrower with their credit score any time that score was a factor in the decision to deny a loan or credit application.

Example If a consumer applies for a car loan and is turned down, it is insufficient for the lender to explain the denial by saying, “Your credit score wasn’t high enough.” The lender must advise the consumer in writing of the denial and, if the applicant timely requests an explanation, say something like, “According to your credit report you made several late payments on your last car loan,” or “You’re carrying too much credit card debt from month to month for us to feel confident that you can handle these payments.” Anytime the credit score was a reason for the denial the lender must also tell the borrower what their credit score was.

There are 30-some-odd true CRAs around the country but only three nationally recognized agencies:

- Experian (www.experian.com)
- Equifax (www.equifax.com) and
- TransUnion (www.transunion.com)

These three CRAs maintain records on almost 225 million Americans compiled from more than 10,000 information providers.

Personal information that appears in a consumer’s credit report includes full name—including maiden name and known variations used (e.g., Bob for Robert, Beth for Elizabeth)—nicknames, current and recent addresses, Social Security number, driver’s license by state of issue and number, date of birth, and current and previous employers.

Financial/credit information appearing in the report includes a list of accounts opened in the consumer’s name or that list the consumer as an authorized user (e.g., as on a spouse’s account); account details, including date the account was opened and type of account (e.g., revolving credit or installment loan); loan or credit limit; payment terms; balances; and payment history, including late payments. Closed or inactive accounts may stay on the report for several years after the last activity in them. Unpaid child support obligations and overdrawn checking accounts may also be reported and shown.

Information acquired from public records and made part of the report may include bankruptcy filings, collection suits and judgments, foreclosure actions and repossessions, involuntary liens, prejudgment attachments, writs of execution, wage garnishments, criminal arrests including both convictions and non-convictions. Most public record information remains on the report for seven years.

Information that cannot be included in a credit report includes checking or savings accounts, bankruptcies that are more than ten years old, charged-off debts or debts placed for collection that are more than seven years old, gender, ethnicity, religion, political affiliation, medical history, or criminal non-convictions more than seven years old.

The FCRA carefully regulates who can access a consumer’s credit report. Persons and entities entitled to access a consumer’s credit report and score are:

- Potential lenders or extenders of credit

- Potential landlords
- Current creditors making inquiry to determine whether the consumer continues to meet the terms of an account
- Insurance companies to whom the creditor has made application
- Employers and potential employers (usually only with the consumer's written consent)
- Companies the consumer allows to monitor their account for signs of identity theft
- Agencies considering the consumer's application for a government license or benefit
- A state or local child support enforcement agency
- Any government agency (although they may be allowed to view only certain portions)
- Someone using the report to provide a product or service the consumer has requested
- Anyone having written authorization from the consumer
- The consumer himself

Lawyers and paralegals engaging in collection efforts on behalf of clients must use great caution before attempting to access a debtor's credit report without the debtor's written consent. 41 U.S.C. §1681q provides as follows:

Any person who knowingly and willfully obtains information on a consumer from a consumer reporting agency under false pretenses shall be fined under Title 18, imprisoned for not more than two years, or both.

Ethical Problem: Jim is a legal professional working for the attorney who represents Carroll Properties, Inc., a real estate leasing company. Carroll Properties has leased a house to a couple, Mike and Shirley Dunbar, for the past year. The lease is up and the Dunbars would like to renew but they made a couple of late payments near the end of the year's lease term. Carroll Properties hasn't decided whether to re-lease the space to them. The client has asked its lawyer to check the Dunbars' credit report and the lawyer has assigned that task to Jim. Can Jim legally and ethically go ahead and access the Dunbars' credit report without more?

Ethical Problem: Jim's supervising attorney has also been retained by Kimberly Chang to file a negligence lawsuit against William Dupree. Chang was involved in a car accident in which Dupree was the other driver, and Chang alleges that Dupree was at fault. Jim's supervising attorney directs him to access Dupree's credit report to see what assets and liabilities it might disclose. Can Jim legally and ethically access Dupree's credit report without more? Would it be okay for Jim to contact the credit reporting agency and identify himself as a bank officer considering a loan to Dupree in order to obtain the credit report? Why or why not?

Major issues that arise in connection with credit reports are the frequency of errors contained in them and the difficulty consumers have historically encountered in getting errors removed or corrected. A

Consumer Reports study published in 2021 found that one-third of reports contained some kind of error (https://www.consumerreports.org/credit-scores-reports/consumers-found-errors-in-their-credit-reports-a6996937910/). Partially in response to this problem and partially in response to the growing problem of identity theft, Congress passed the Fair and Accurate Credit Transactions Act (FACTA). FACTA amended the FCRA to allow consumers to obtain a free copy of their credit report once every 12 months from each of the three leading CRAs (Equifax, Experian, and TransUnion). In cooperation with the Federal Trade Commission, the three companies operate the Web site www.annualcreditreport.com where consumers may request their report. The free report mandated by FACTA is a summary only and does not include the consumer's credit score. The consumer must pay a small fee to receive his or her credit score unless he or she has been denied a loan or credit based on the score, in which case the lender denying the application must disclose the score to the consumer.

Under FCRA, both the CRA and the information provider are responsible to correct inaccurate or incomplete information in a credit report. When the consumer notifies the CRA of a dispute concerning an inaccurate or incomplete entry, the agency must investigate the dispute within 30 days of receipt unless it deems the complaint frivolous and respond in writing to the consumer when the investigation is complete. The agency must also contact the information provider, who must investigate and respond to the credit agency. If one credit reporting agency confirms an inaccuracy and corrects it, it must also notify the other two national agencies so those records can be corrected as well. The Illustration below shows a consumer dispute letter form.

Illustration: CONSUMER DISPUTE LETTER REGARDING ALLEGED CREDIT REPORT ERROR

Date

Your Name

Your Address, City, State, Zip Code

Complaint Department

Name of Company

Address

City, State, Zip Code

Dear Sir or Madam:

I am writing to dispute the following information in my file. I have circled the items I dispute on the attached copy of the report I received.

This item (identify item(s) disputed by name of source, such as creditors or tax court, and identify type of item, such as credit account, judgment, etc.) is (inaccurate or incomplete) because (describe what is inaccurate or incomplete and why). I am requesting that the item be removed (or request another specific change) to correct the information.

Enclosed are copies of (use this sentence if applicable and describe any enclosed documentation, such as payment records, court documents) supporting my position. Please reinvestigate this (these) matter(s) and (delete or correct) the disputed item(s) as soon as possible.

Sincerely,

Your name

Enclosures: (List what you are enclosing.)

(Source: Federal Trade Commission Consumer Protection Web site: www.ftc.gov/bcp/edu/pubs/consumer/credit/cre21.shtms)

FACTA also contains provisions intended to help reduce identity theft, including authorizing consumers to place alerts on their credit histories if identity theft is suspected or if deploying overseas in the military, thereby making fraudulent applications for credit more difficult. Under FACTA, mortgage lenders must now provide consumer borrowers with a Credit Disclosure Notice that includes their credit scores, range of scores, credit bureaus, scoring models, and factors affecting their scores.

Notwithstanding these attempts at regulation, the number of errors found in consumer credit reports remains high and many "investigations" into complaints of errors amount to nothing more than reconfirming inaccurate information provided by creditors.

The FCRA creates a private cause of action for consumers to recover for willful failure of the CRA to comply with its various requirements and to recover actual damages or statutory damages up to $1,000, as well as punitive damages and attorney's fees. See 15 U.S.C. §1681(n). Though the obligation to follow reasonable procedures to assure maximum possible accuracy in credit reports they compile on consumers, the Supreme Court, in *TransUnion v. Ramirez*, 2021 WL 2599472 (June 25, 2021), held that such action was not actionable by a consumer unless and until the CRA releases inaccurate information included in a credit report to a third party even though the statutory language itself imposes no such condition to recover on the protected consumer and appears to authorize recovery upon proof of the mere failure of the CRA to fulfill its obligations under the Act.

Side Note 2-1 in the Extra Materials file located on the companion web site to the textbook contains more information on credit reports and the regulation of CRAs.

For a Business Entity

When a loan is made or credit extended to a business entity, it is usually referred to as a trade credit transaction. There are a number of business credit reporting agencies that collect trade credit information on corporations including limited liability companies and some other types of business, rather than consumers, using the business's name and employer identification number (EIN) assigned by the IRS. Some of the leading business credit bureaus (not to be confused with companies that provide ratings for corporate bonds) are Dun & Bradstreet, Experian Business, Equifax Business, and Business Credit, USA.

In addition to a credit report, these business credit bureaus calculate a credit score for businesses, usually using a scoring model producing a score range of 0 to 100 with 75 or better being good to excellent. The information in the credit report and the business credit score is made available to

subscribing members of the credit bureau for a fee. Business credit bureaus are subject to the provisions of the Equal Credit Opportunity Act and Federal Reserve Board Regulation B to the extent applicable. They are not subject to the provisions of FCRA except to the extent that they may collect consumer data.

Credit reports and scores can become confusing for sole proprietorships (an unincorporated business having a single owner) and partnerships (an unincorporated for-profit business owned by more than one person) that engage in business depending on the credit worthiness of their individual owners. The credit report for such a business may contain a mix of personal as well as business data and the credit score may be based on both personal and business transactions and circumstances.

Side Note 2-2: Who Uses Payday and Car Title Loans?

Though the median annual income for a payday/car title borrower is less than $25,000, a 2010 investigation by National Public Radio's Planet Money ("Inside a Payday Loan Shop" at www.npr.org/sections/money/2010/05/the_tuesday_podcast_payday_len.html) revealed that a significant number of regular users of payday loan shops are solidly middle class. Payday and car title loans are often justified by the financial services industry as providing a quick, convenient, short-term loan source. However, 80 percent of payday and car title loan customers renew or roll over their loan once or more. In fact, the average payday/car title loan customer takes out a loan nine times per year, a debt trap that keeps such debtors perpetually in debt and quickly paying more in interest and fees than was borrowed.

Payday and car title loans are, needless to say, controversial. Consumer advocates consider them predatory lending that takes advantage of unsophisticated, and sometimes desperate, lower-income consumers. Business advocates consider them a fair lending practice, subject, like other loans, to provisions of the federal Truth in Lending Act (TILA) and Regulation Z (12 C.F.R. Part 226) promulgated under TILA, requiring lenders to disclose in writing the finance charge (a dollar amount) and the annual percentage rate (APR) to the consumer.

After releasing its formal research report on payday lending in March 2014 (available online at www.consumerfinance.gov/data-research/research-reports /cfpb-data-points-payday-lending/) and a subsequent report on car title loans in May 2016 (available online at www.consumerfinance.gov/about-us/newsroom /cfpb-finds-one-five-auto-title-loan-borrowers-have-vehicle-seized-failing -repay-debt/) the Consumer Financial Protection Bureau promulgated formal regulations of these loans now found at 12 CFR part 1041. These regulations require that a lender reasonably determine that the consumer has the ability to repay the loan before making it, limit the number of times a loan can be renewed (three times in most cases) and the number of months in a year the debtor can owe the lender for the loan (nine months in most cases), restrict the making of new loans to a consumer who has or recently had other outstanding loans, require lenders to provide advance notice to the consumer before attempting to withdraw payment from the consumer's account, and prohibit the lender from attempting to withdraw payment from a consumer's account after two consecutive attempts have failed unless the consumer specifically consents to further attempts.

Side Note 2-3 (Not referenced in the text): Buy Now Pay Later Loans

The COVID 19 pandemic and resulting shut down accelerated the popularity of online shopping. It also breathed life into a type of loan that has been around forever but seems to have found its moment as a result of this crises: **buy now pay later loan** (BNPL) also known as a **point-of sale loan**. In a BNPL transaction, the merchant arranges with a BNPL service (e.g., Afterpay, PayPal Holdings, Inc., Affirm, Inc., Klarna Inc., Splitit, Sezzle, Perpay Inc., Openpay, Quadpay, Inc., or LatitudePay) to offer buyers the BNPL option for payment at the point of sale. If the buyer chooses the BNPL option, payment is deferred to short-term installments of usually 3-6 months while the buyer receives their merchandise immediately (making it more appealing than a layaway arrangement). The merchant also receives immediate payment of the full price of the merchandise sold minus a small % retained by BNPL service (but a % smaller than that charged by most credit cards making it more appealing to merchant sellers). The buyer then makes the agreed installment payments to the BNPL service. The BNPL loan is proving popular with buyers not only because of the deferred payment arrangement but also because most BNPL services do no credit check prior to making the loan and many charge no interest or fees on the amount deferred, unless payments are not made on time.

According to a report from Worldpay, the payment processing firm owned by Fidelity National Information Services Inc., global e-commerce transactions totaled $4.6 trillion in 2020. BNPL sales accounted for 2.1% of that total, or about $97 billion, an amount that is projected to double by 2024. See the article at www.cnbc.com/2021/09/21/how-buy-now-pay-later-became-a-100-billion-industry.html.

The concern about such a convenient loan arrangement is that it is so fast and easy that it may encourage overspending and subsequent default. See if you can determine whether and to what extent BNPL loans have continued to claim a larger share of e-commerce transactions globally and nationally since 2020 and what the default rate is proving to be on such loans.

Chapter Four

Side Note 4-1: Origins of the Modern Debt Buying Industry

There has always been some market for debts that a creditor has given up on and is considering writing off as uncollectible. But the industry boomed as a result of the Savings and Loan crisis of the 1980s (read the history at www.fdic.gov/bank/historical/history/167_188.pdf) when 118 state and federally insured savings and loan (S&L) institutions holding $43 billion in assets failed over a 2-year period. The Federal Deposit Insurance Corporation (FDIC), which insures deposits in those institutions, took over those failing S&Ls and made good all amounts on deposit at the expense of the taxpayers. The Resolution Trade Corporation (RTC) was then formed by the FDIC and began to actively seek buyers willing to purchase the assets of closed S&Ls, including both current and delinquent accounts. Auctions were held around the country at which performing and nonperforming accounts were bundled and sold to the highest bidder with no opportunity by the bidder to evaluate the specific accounts in the bundle purchased. Thus was birthed the modern debt buying industry.

Side Note 4-2: Reasonable Consumer or Least Sophisticated Consumer?

Though the FDCPA does not expressly require it, a number of federal circuits have determined that §§804-808 of the FDCPA are to be applied using the least sophisticated consumer standard (see, e.g., *In re Crawford*, 758 F.3d 1254 (11th Cir. 2014)) rather than a reasonable consumer standard (see, e.g., *Smith v. Consumer Credit, Inc*., 167 F.3d 1052, 1054 (6th Cir. 1999)). The least sophisticated standard is intended to protect even the most naïve or overly trusting consumers from deceptive debt collection practices. You may want to see if your federal circuit has adopted the least sophisticated consumer standard for interpreting the abuse provisions of the FDCPA. If not, does your circuit follow the reasonable consumer standard or some other standard that it has articulated? If your state regulates debt collection practices, what standard have your state courts adopted for applying the state act?

Side Note 4-3 (Not referenced in the text): **The Need to Show Concrete Harm other than Confusion and Anxiety to Recover for Violations of the Fair Debt Collection Practices Act**

The ability of a debtor to recover damages under the Fair Debt Collection Practices Act for a debt collector's use of false or misleading representations (discussed in Chapter 4A2 of the text) has recently been hampered by court decisions in two federal circuits. Relying on *Spokeo, Inc. v. Robins*, 578 U.S. 586 (2016) (holding a mere procedural violation of the Fair Credit Reporting Act is not a sufficiently concrete injury to satisfy Article III of the Constitution which limits judicial power to resolving actual cases and controversies), the Sixth and Seventh Circuits have held that mere confusion, anxiety, and fear of future harm arising from a misleading communication from a debt collector are insufficient injuries to give a debtor Article III standing to sue for violation of the FDCPA. See *Garland v. Orlans*, 999 F.3d 432, 438 (6th Cir. 2021) (letter from law firm stating that the foreclosure process had been initiated, but that foreclosure prevention alternatives might be available, was allegedly sent without a meaningful review of foreclosure files by an attorney, and thus, deceptively implied that communication was from an attorney) and *Brunett v. Convergent Outsourcing, Inc*., 982 F.3d 1067, 1068 (7th Cir. 2020) (debt collector's letter to debtor offering to accept 50% of balance in satisfaction of debt but stating that it would be required to report any release of indebtedness greater than $600 to IRS was deemed confusing and intimidating by debtor). Both courts agreed that "the state of confusion is not itself an injury." Have the federal courts of your circuit applied *Spokeo* to impose a 'concrete injury' requirement on debtor's suing for violations of the FDCRA when the statute itself imposes no such requirement? The law routinely allows recovery for mental anxiety in the tort area, so why should such injury be insufficiently concrete under the FDCPA? Could these decisions reflect the desire of conservative judges, who might feel Congress has gone too far in providing remedies for debtors, to protect businesses from a degree of accountability intended by Congress?

Side Note 4-4: (Not referenced in the text): Phantom Debt

In February 2015, Andrew Therrien, a resident of Rhode Island, began receiving demands to make good on a payday loan that he had never taken out and did not owe. When the harassment of various debt collectors escalated to ridiculous levels, including one threat to rape his wife, Therrien decided to get to the bottom of it. Over the following two years, what he uncovered was a jaw-dropping scheme pursuant to which persons with access to debtor information from online applications for payday or other short-term loans used that information to create fictitious debt obligations then sold those phantom debt

portfolios to multiple debt collectors who proceeded to harass the named debtors for debts they did not owe. You can read about this remarkable case at www.bloomberg.com/news/features/2017-12-06/millions-are-hounded-for-debt-they-don-t-owe-one-victim-fought-back-with-a-vengeance.

It's important to remember that most debt collectors are honest, ethical persons engaged in a legitimate business while complying with the law. But the audacity and corruption of the bad apples attracted to that business appear bottomless. Read about recent (as of 2021) actions taken by the FTC to shut down phantom debt schemes at www.ftc.gov/news-events/press-releases/2019/07/phantom-debt-brokers-collectors-settle-ftc-new-york-ag-charges and www.ftc.gov/system/files/documents/cases/stark_doc354stipperminjhirshetal_redacted.pdf. Take a look at this article written by AARP warning senior citizens about phantom debt schemes: www.aarp.org/money/scams-fraud/info-2021/debt-scams.html. Does your state have its own legislation regulating debt collection practices? What criminal penalties are available under your state's criminal code for individuals who engage in these types of phantom debt scams?

Chapter Five

Side Note 5-1: Sample Postjudgment Interrogatories

POSTJUDGMENT INTERROGATORIES
FROM CAPITAL CITY MEDICAL EQUIPMENT (CCME) TO PEARL MURPHY
[STYLE OF CASE OMITTED FROM ILLUSTRATION]

INTERROGATORIES IN AID OF JUDGMENT

Because you have failed to pay the full amount of the judgment against you entered in favor of plaintiff, plaintiff has the right to attempt to enforce that judgment by execution on your assets. Plaintiff also may inquire concerning the existence and location of those assets.

Pursuant to Rules 33 and 69 of the Columbiana Rules of Civil Procedure you are required to make full and complete answers to the questions set forth below. These answers must be made in writing, under oath, within thirty (30) days after service upon you. Attach additional sheets if necessary to completely answer questions.

Should you fail to answer, the court may enter an order imposing sanctions against you. If you do not understand your duty to answer these questions, you should consult a lawyer.

1. EMPLOYMENT: State whether you are currently employed. If so, state whether you are paid weekly, semimonthly, biweekly, monthly, or in some other fashion. If you are self-employed, state the name of your business, address, nature of your business, and annual income.

ANSWER:

2. ACCOUNTS: State whether or not you maintain any checking or savings accounts. If so, state the name and location of the banks or savings and loan association or building and loan association or credit union

and the branch or branches thereof, the identification (account) numbers of each account, and the amount or amounts you have in each account. If you maintain any of these jointly with another person, give their name and address. Also provide the above information with respect to any such bank accounts that were maintained and were closed within the past twelve (12) months.

ANSWER:

3. REAL ESTATE: Do you have an ownership or interest in any real estate anywhere in the United States? If so, set forth a brief description thereof, including the lot size and type of construction; the location, including the state, county, and municipality; the volume and page number of the official record; and state further whether you own it solely or together with any other person or persons and give their full name and address. If any of the above properties are mortgaged, supply the name and address of the lender[s], the date and amount of the mortgage, where it is recorded, the monthly payments, and the balance now due.

ANSWER:

4. DEBTS, NOTES & JUDGMENTS: State the names and addresses of any and all persons whom you believe owe you money and set forth in detail the amount of money owed, the terms of payment, and whether or not you have written evidence of this indebtedness and, if so, the location of such writing. Also, state if the matter is in litigation and, if so, give full details. If you hold a judgment or judgments as security for any of these debts, state where and when the judgment was recorded, and the county, number, and term where the judgment is recorded. If you hold this judgment jointly with any other person or persons, give their name and address.

ANSWER:

5. INSURANCE: State whether or not you are the owner of any life insurance contracts. If so, state the serial or policy number or numbers of said contract, the face amount, the exact name and address of the insurance company, the named beneficiary or beneficiaries and their present address. If you own this insurance jointly with any other person or persons, give their name and address.

ANSWER:

6. MORTGAGES: State whether you own any mortgages against real estate owned by any other person in the United States. If so, state whether or not you own this mortgage with any other person or persons and, if so, supply their full name and address. State further the names and addresses of all borrowers and the state and county where said mortgage is recorded together with the number of the volume and the page number.

ANSWER:

7. AGREEMENTS: State whether you have any agreements involving the purchase of any real estate anywhere in the United States. If so, state with whom this agreement is made, and state whether or not any persons are joined with you in the agreement. Supply full names and addresses of all parties concerned. If the agreement is recorded, provide the state and county of recordation, volume and page numbers.

ANSWER:

8. STOCKS, SHARES, OR INTERESTS: State whether or not you own any stocks, shares, or interests in any corporation or unincorporated association or partnership, limited or general, and state the location thereof. Include the names and addresses of the organizations and include the serial numbers of the shares or stock. If you own any of the stock, shares, or interests jointly with any other person or persons, give their name and address.

ANSWER:

9. GOVERNMENT, MUNICIPAL, OR CORPORATE BONDS: State whether or not you own individually or jointly any corporate or governmental bonds including U.S. Savings Bonds. If so, include the face amount, serial numbers, and maturity date, and state the present location thereof. If you own any of these bonds jointly with any other person or persons, give their name and address.

ANSWER:

10. SAFETY DEPOSIT BOXES: State whether or not you maintain any safety deposit box or boxes. If so, include the names of the bank or banks, branch or branches, and the identification number or other designation of the box or boxes. Include a full description of the contents and also the amount of cash among those contents. If you maintain any of these jointly with any other person or persons, give their full name and address.

ANSWER:

11. TRANSFERRED ASSETS AND GIFTS: If, since the date this debt to [creditor] was first incurred, you have transferred any assets (real property, personal property, chose in action) to any person and/or, if you have given any gift of any assets, including money, to any person, set forth, in detail, a description of the property, the type of transaction, and the name and address of the transferee or recipient.

ANSWER:

12. INHERITANCE: State whether or not, to your knowledge, you are now or will be a beneficiary of or will inherit any money from any decedent in the United States, and state the place and date of death, the legal representative of the estate, and the location of the court where the said estate is administered or to be administered.

ANSWER:

13. ANNUITIES: State whether you are a beneficiary of any trust fund and, if so, state the names and addresses of the trustees and the amount of the payment and when the payment is received.

ANSWER:

14. PERSONAL PROPERTY: Set forth a full description of all furnishings and any other items of personal property (including jewelry) with full description, value, and present location. State also whether or not there are any encumbrances against that property and, if so, the name and address of the encumbrance holder, the date of the encumbrance, the original amount of that encumbrance, the present balance of that encumbrance, and the transaction that gave rise to the existence of the encumbrance. If you own any personal property jointly with any other person or persons, give their name and address.

ANSWER:

15. RENTAL INCOME: State whether you are the recipient, directly or indirectly, of any income for the rental of any real or personal property, and, if so, state specifically the source of payment, the person from whom such payments are received, and the amount and date when those payments are received.

ANSWER:

16. MOTOR VEHICLES: State whether or not you own any motor vehicles. Include a full description of such motor vehicles, including color, model, title number, serial number, and registration plate number. Also show the exact name or names in which the motor vehicles are registered, the present value of those motor vehicles, and their present location and place of regular storage or parking. State also whether or not there are any liens or encumbrances against those motor vehicles and, if so, the name and address of the encumbrance, the present balance of the encumbrance, and the transaction that gave rise to the existence of the encumbrance.

ANSWER:

17. PENSION: State whether you are a participant in or the recipient of any pension or annuity fund and, if so, state specifically the source of payment, the person to whom such payments are made, the amount of the payments, and date when those payments are received.

ANSWER:

18. OTHER ASSETS: If you have any asset or assets that are not disclosed in the preceding 17 interrogatories, please set forth all details concerning those assets.

ANSWER:

[Attorney's signature and certificate of service omitted from illustration.]

Chapter Six

Side Note 6-1: A Historical Timeline of Debt Punishment/Forgiveness Attitudes and Practices

2400-1600 B.C.E.—Clean Slate proclamations by various kings of ancient Sumeria, Assyria, and Babylon mandate the periodic forgiveness of debt and the restoration of land given as security or persons sold for debt. E.g., Code of Hammurabi §117 (circa 1754 B.C.E.): "If any one fail to meet a claim for debt, and sell himself, his wife, his son, and daughter for money or give them away to forced labor, they shall work for three years in the house of the man who bought them and in the fourth year they shall be set free."

1400 B.C.E.—Moses' law mandates a Sabbatical Year every seven years, when all debts are to be forgiven. At the end of every seventh Sabbatical Year (thought to be every 50th year) a Year of Jubilee is declared when debts are forgiven, slaves freed, and land taken for nonpayment of debt is returned to former owners or their heirs (other than the houses of laypersons within walled cities).

1000 B.C.E.—By this time, credit arrangements are firmly established as basis of commerce by and among Assyria, Babylon, and Egypt.

500 B.C.E.—Ancient Greece has no bankruptcy relief laws. Debtors, their families, or servants can be reduced to serfdom or even slavery for unpaid debt (debt slavery). Crises develop when such portion of the farming class is in jail or enslaved that there aren't enough workers to tend the crops. Crisis temporarily relieved in Athens by the Seisachtheia (burden-shaking) laws of Solon in 594 B.C.E. that cancel existing debt, mandate the return of debtor's forfeited property, and end debt slavery. Other Greek city-states limit the term of debt slavery to five years and protect debtors from severe abuse (protection of life and limb).

250 B.C.E.—In the days of the Roman Republic, debtors, or their families or servants, can be sold into slavery, imprisoned, and even killed by creditors. (It is said that in Roman times, creditors not only divided the debtor's property, but they also took him to the public plaza and bodily divided him.)

100 C.E.—Under the Caesars, the Roman Empire adopts some debt collection laws, including the appointment of a trustee to sell off a merchant debtor's assets after the merchant ceases business still owing money. The trustee is called the curator bonorum (caretaker) of the debtor's property for the benefit of creditors. Practice of cession bonorum (cesstion of goods) allows debtor to surrender property to creditor to avoid imprisonment.

1285—England's Statute of Merchants allows imprisonment of merchant debtors.

1400—In Italian city states, the defaulting merchant's trade bench or selling counter is destroyed to publicly announce his failure, literally banca rotta (broken bench), which may be the source of our modern word, bankruptcy.

1542—The state of being bankrupt is made an official crime in England, mandating a hearing before the chancellor, and is punishable by confiscation of property and imprisonment.

1570—Under Queen Elizabeth I of England, the first official bankruptcy law is passed by Parliament. It is exclusively a creditor's device, involuntary for the debtor. The creditor can formally declare a merchant bankrupt and seek official relief, including confiscation of property, imprisonment, and corporal punishment, the last of which could include having the debtor pilloried (a form of public humiliation that involved having hands and head locked in place by wooden stock) or having an ear cut off. In Padua, Italy, the bankrupt is required to appear nearly naked in the Palace of Justice and to slap his buttocks three times against "The Rock of Shame" while loudly proclaiming, "I declare bankruptcy!"

1705—England's Statute of Queen Anne marks the first attempt at a humane reform of bankruptcy law. At the request of the debtor and with creditors' consent, debt can be discharged following liquidation of assets. The death penalty for the debtor is allowed for committing fraud in bankruptcy but is only known to have been enforced five times.

1788—The U.S. Constitution is ratified, including Article I, §8, which authorizes Congress "[t]o establish…uniform laws on the subject of bankruptcies throughout the United States." In its first session, Congress considers adopting a bankruptcy law but demurs. Without federal rules, states follow their colonial practices based on English precedent, including imprisonment and pillorying.

1800—The Panic of 1797 in America leads to the imprisonment of thousands of debtors by the states, including the "Financier of the Revolution," Robert Morris. As a result, Congress passes the first federal bankruptcy law. It allows only creditors to declare a person bankrupt. Debts can be discharged after

liquidation of the debtor's assets if he has been cooperative and two-thirds of his creditors consent. Repealed in 1803.

1833—Federal imprisonment for debt is abolished in the United States by act of Congress (now 28 U.S.C. §2007). Individual states begin to follow suit.

1841—The economic depression of 1837 results in Congress passing its second bankruptcy law, which for the first time permits debtors, including nonmerchants, to voluntarily file for bankruptcy relief. Due to high administrative costs, questions of constitutionality, and the discontent of creditors, the law is repealed in 1843.

1867—Following the turmoil of the Civil War, northern creditors want a system to collect from southern debtors. Congress passes a third bankruptcy law to enable them to do so, but it is repealed in 1878, again due to high administrative costs, an unwieldy bureaucracy, and little return to creditors.

1898—The economic panic of 1893 results in passage of the landmark Nelson Act, initiating the modern effort to balance debtor/creditor interests. The law, formally called the Bankruptcy Act, acknowledges the new credit economy, provides for a debtor-initiated discharge of debts, allows debtors to keep significant exempt property, and establishes the bankruptcy referee (predecessor of the modern bankruptcy judge) as the designated officer of the U.S. district court to administer the law.

Bankruptcy Act   The predecessor of the current Bankruptcy Code. Enacted in 1898 and superseded in 1978.

Bankruptcy referee   Office created under Bankruptcy Act of 1898. Predecessor to the modern bankruptcy judge.

1938—The Chandler Act amends the existing Bankruptcy Act to allow reorganizations in bankruptcy for both individual and business debtors (today known as Chapter 13 and Chapter 11 bankruptcies, respectively), enabling debtors with the means to repay all or a part of their debts under court supervision as an alternative to liquidation. For the first time, bankruptcy becomes a viable option to achieve economic survival rather than the failure of liquidation.

1978—The Bankruptcy Reform Act substantially rewrites the nation's bankruptcy law. Now formally known as the Bankruptcy Code, the law contains the current chapter numbering (Chapter 7, Chapter 13, Chapter 11, etc.), bankruptcy judges are given expanded judicial powers to administer bankruptcy cases, Chapter 11 business reorganizations are made more feasible, and states are given the option to “opt out” of the Code's property exemptions and apply their own exemption laws instead.

Bankruptcy Reform Act   The 1978 statute that introduced the current Code. Also the name of the 1994 statute that amended the Code.

1982—The U.S. Supreme Court decides *Northern Pipeline Construction Co. v. Marathon Pipeline Co*., 458 U.S. 50 (1982), declaring the Bankruptcy Reform Act of 1978 unconstitutional. The Court rules that Congress had overstepped its bounds in granting bankruptcy judges, created under Article I of the Constitution, powers of Article III judges in administering the Code. The Court grants Congress a grace period to amend the Bankruptcy Reform Act to cure the defect.

1984—The Bankruptcy Amendments and Federal Judgeship Act finally address the Northern Pipeline decision, reconstituting bankruptcy courts and judges as units of the U.S. district courts, with bankruptcy proceedings officially "referred" to bankruptcy courts under the standing orders of the district courts.

1986—The Code is amended to create the Chapter 12 proceeding for family farmers with regular income on a test basis and to make permanent the U.S. Trustee system to help administer bankruptcy cases, a system that had been tested on a pilot basis since 1978.

1994—The Bankruptcy Reform Act of 1994 further amends the Code to clarify when bankruptcy courts can conduct jury trials, to expedite bankruptcy proceedings, to encourage individual debtors to use Chapter 13 to reschedule their debts rather than Chapter 7 to liquidate, and to aid creditors in recovering claims against bankrupt estates.

1996—For the first time ever, one million Americans file for bankruptcy in a single year.

2005—After over a decade of study and debate, Congress passes the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA), a significant amendment to the Code, intended to reduce the number of individual consumer bankruptcies and encourage repayment by making it more difficult for individual debtors to file for Chapter 7 liquidation relief and to force more of them to file for Chapter 13 reorganization. The Chapter 12 family farmer proceeding is made permanent and expanded to include family fishermen. The Chapter 15 proceeding is added to provide a mechanism for dealing with bankruptcy proceedings across international borders.

2011—The U.S. Supreme Court decides *Stern v. Marshall*, 564 U.S. 462 (2011), reviving *Northern Pipeline* concerns over the constitutional power of Article I bankruptcy courts to decide core proceedings.

2020— The Small Business Reorganization Act of 2019 amending Chapter 11 by adding new Subchapter V to streamline reorganization for small business debtors becomes effective.

Side Note 6-2: Online Resources for Learning about Bankruptcy

The Bankruptcy Code, Rules, Forms, and General Information

- Title 11 of the U.S. Code (http://uscode.house.gov/ or www.law.cornell.edu/uscode/text/11)
- Rules of Bankruptcy Procedure (www.uscourts.gov/rules-policies/current-rules-practice-procedure)
- Official Bankruptcy Forms (www.uscourts.gov/forms/bankruptcy-forms)
- Administrative Office of the Federal Courts' Federal Judiciary Home Page (www.uscourts.gov)
- United States Trustees Program (administered by the U.S. Department of Justice) (www.usdoj.gov/ust)
- Administrative Office of the U.S. Courts, Bankruptcy Basics (www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics)

- Electronic Bankruptcy Noticing Center (https://bankruptcynotices.uscourts.gov/)
- Cornell University Law School's Legal Information Institute's Bankruptcy Information Page (www.law.cornell.edu/search/site/bankruptcy)
- FindLaw's Internet Guide to Bankruptcy Law (http://corporate.findlaw.com/law-library/the-internet-guide-to-bankruptcy-law.html)
- Bernstein's Dictionary of Bankruptcy Terminology (https://bernsteinlaw.com/resources/bankruptcy-dictionary/)
- NOLO Bankruptcy in Your State (www.thebankruptcysite.org/topics/bankruptcy-your-state)

Organizations Concerned with Bankruptcy Practice

- American Bankruptcy Institute (www.abiworld.org)
- National Bankruptcy Conference (http://nbconf.org/)
- The American College of Bankruptcy (www.amercol.org)
- National Association of Bankruptcy Trustees (https://www.nabt.com/)
- National Association of Chapter 13 Bankruptcy Trustees (https://nactt43.wildapricot.org/)
- National Association of Consumer Bankruptcy Attorneys (www.nacba.org)
- National Consumer Law Center (www.nclc.org)
- The Commercial Law League of America (www.clla.org)

Bankruptcy Blogs, Podcasts, and Other News and Information Sites

- ABA Journal Asked & Answered Podcasts (https://www.abajournal.com/topic/asked_answered)
- ABI Blog Exchange (https://www.abi.org/member-resources/blogs)
- ABI Newsroom Podcasts (https://www.abi.org/newsroom/podcasts)
- ABI St. John’s Blog (https://www.abi.org/member-resources/st-johns-case-blog)
- ABI Videos (https://www.abi.org/newsroom/abi-media/videos)
- Bankruptcy Law Network (www.bankruptcylawnetwork.com)
- Bankruptcy Litigation Blog (http://www.bankruptcylitigationblog.com/)

- Best Case Community (https://www.bestcase.com/community/)
- Credit Slips Blog on Credit, Finance and Bankruptcy (https://www.creditslips.org/)
- LAW 360: Bankruptcy (www.law360.com/bankruptcy)
- New Generation Research (NGR) (http://newgenerationresearch.com)
- Sheppard/Mullin Finance and Bankruptcy Blog (http://www.bankruptcylawblog.com)
- Start Fresh Today Bankruptcy Blog (https://www.startfreshtoday.com/blog/)
- The Georgia Bankruptcy Blog (https://www.georgiabankruptcyblog.com/)
- The Daily Bankruptcy News (http://bkinformation.com/news/dailynews.htm)
- New Generation Research (NGR) (http://newgenerationresearch.com)
- Wall Street Journal Pro Bankruptcy (www.wsj.com/pro/bankruptcy)
- Weil Restructuring (https://restructuring.weil.com/)

Chapter Seven

Side Note 7-1: Who Can Deduct a Charitable Contribution Expense and in What Amount as Part of the Means Test?

The issue of limiting a debtor's deductions for charitable contributions to a religious organization raises First Amendment Free Exercise Clause issues that have never been completely resolved. In the Religious Liberty and Charitable Donation Clarification Act of 2006, Congress made clear that its intent in the Religious Liberty and Charitable Contribution Protection Act of 1998 was that debtors in bankruptcy be allowed to claim charitable contribution expenses as part of their adjustment of income as part of the means test. Such contributions cannot be disallowed as being not reasonably necessary to the support of the debtor and dependents as part of the Chapter 7 means test. Notwithstanding that, per the language of the form, listed contributions must be "continuing." A debtor who has rarely if ever made charitable contributions may not enter an amount here on the grounds that they intend to begin making those contributions without drawing a challenge. Moreover, trustees will generally limit the amount claimed to 10 to 15% of the debtor's gross income (and §1325(b)(2)(A)(ii) specifically limits this deduction to 15% of the debtor's gross income for purposes of determining a Chapter 13 debtor's disposable income). Though there is no such statutory limitation on the charitable contribution deduction in the Chapter 7 means test, the U.S. Trustee Program has taken the position that such contributions by a Chapter 7 debtor should not be allowed in excess of 15% of gross income (see

Statement of U.S. Trustee at
www.justice.gov/sites/default/files/ust/legacy/2015/03/03/ch7_line_by_line.pdf).

Regarding charitable contributions as legitimate living expenses in calculating a Chapter 7 debtor's current monthly income for purposes of the means test (or a Chapter 13 debtor's disposable income as we will see later), it is worth noting the growing body of research suggesting that that low-income Americans tend to give a higher percentage of their income to charity per capita than do high-income Americans. In 2014, the wealthiest 20 percent gave an average of 1.3 percent to charity (favoring colleges, universities, arts organizations, and museums), whereas the poorest 20 percent gave an average of 3.2 percent (favoring religious organizations and social services entities). Why do you think that is the case? Does having less equate to greater sensitivity to need? Is the drive to increase wealth inconsistent with favoring communal support? Do the wealthy put their self-interests above that of others? Do the self-made wealthy have an unconscious desire to hang on to what they've accumulated? See Poor People Really are more Charitable than the Rich, by Joe Mellor, The London Economic, June 28, 2018 (www.thelondoneconomic.com/news/environment/poor-people-really-are-more-charitable-than-the-rich-according-to-new-research-93441); *Why the Rich Don't Give*, by Ken Stern, in The Atlantic magazine, April 2013; and *How America Gives*, a study done by the Chronicle of Philanthropy (http://philanthropy.com) in August 2012; and Poor Americans Are Country's Most Charitable Demographic, Philanthropy News, May 31, 2009, available online at https://philanthropynewsdigest.org/news/poor-americans-are-country-s-most-charitable-demographic; and *Higher Social Class Predicts Increased Unethical Behavior*, by Paul Piff, in the Proceedings of the National Academy of Sciences, February 2012, discussed in *The Money-Empathy Gap*, by Lisa Miller, New York magazine, June 29, 2012 available online at http://nymag.com/news/features/money-brain-2012-7. For an article challenging the premise that the poor give more per capita than the wealthy, see *Are Rich People Really Less Generous*, by Benjamin Purdy, Texas A&M University, The Econofact Network, May 5, 2020, available online at https://econofact.org/are-rich-people-really-less-generous.

Chapter Eight

Side Note 8-1: The History of Property Exemptions in Bankruptcy

The Bankruptcy Act of 1898, our first "modern" bankruptcy statute, did not set out any federal exemptions and applied state law exclusively. You can read *Hanover Nat'l Bank v. Moyses*, 186 U.S. 181 (1902) to see how the court ruled on a constitutional attack on the 1898 Act's failure to adopt uniform exemptions in a statute supposedly intended to produce a uniform procedure nationwide. And read *In re Sullivan*, 680 F.2d 1131 (7th Cir. 1982), cert. denied, 459 U.S. 992 (1983) to see how the *Moyses* doctrine was applied to the "opt out" provision when it was first introduced to the Code. The federal Bankruptcy Code is in fact a good example of how federalism works in our legal system.

Today, a debtor's right to claim property as exempt is deemed sacrosanct even where the debtor uses the bankruptcy process in bad faith and to commit a fraud on creditors. See *Law v. Siegel*, 571 U.S. 415 (2014) (bankruptcy court inappropriately surcharged debtor's homestead exemption to pay administrative costs of trustee incurred in multi-year litigation that concluded in a finding that debtor had listed a fictitious second mortgage on his home to create the appearance of there being no equity for the estate in the home; a bankruptcy court may not exercise its authority under §105(a) to "carry

out" the provisions of the Code or its inherent power to sanction abusive litigation practices by taking action otherwise prohibited by the Code such as §522(k), which makes exempt property "not liable for payment of any administrative expense").

Chapter Nine

Side Note 9-1: **Can Entity Debtors Recover Damages for Willful Violation of the Automatic Stay?**

Since §362(k)(1) references "an individual injured…" most courts limit the recovery of damages for willful violation to individual debtors and disallow them to entity debtors (corporations, limited liability companies, partnerships, trusts, etc.) (see, e.g. *In re Spookyworld, Inc*., 346 F.3d 1, 6 (1st Cir. 2003)). However, a minority construe "individual" to include an entity debtor (see, e.g., *Budget Service Co. v. Better Homes of Virginia, Inc*., 804 F.2d 289, 292 (4th Cir. 1986)), finding it difficult to accept that Congress meant to give remedy for intentional violation to individual debtors only and emphasizing the important role of §362k in repairing and deterring willful violations. You might want to determine how the courts of your federal district come down on this issue.

Chapter Ten

Side Note 10-1: More on the Right to Setoff

The right to setoff can get complicated. For example, in order for setoff to work the debts must be mutual. In part that means that both claims must be valid. Sometimes setoff is sought where one debt is admitted but the other is contested. There can be no setoff until the validity of the contested claim is determined. Mutuality also means the parties must be indebted to each other in the same or similar capacity. If X owes Y a debt personally and Y owes X a debt personally, there is mutuality and setoff will work. But what if X owes Y a debt personally but Y owes X a debt in X's capacity as trustee of a trust rather than personally? There may be no mutuality there and no setoff allowed.

Where a governmental entity is involved, there may be a problem of sovereign immunity. Assume a debtor owes the government a debt but also has a claim against the government which debtor wants to use to setoff the debt to the government. The government, however, claims sovereign immunity as to the claim of the debtor. Section 106 of the Code thankfully deals with this situation providing that sovereign immunity alone does not prevent setoff of the claims. See *In re Microage Corp*., 288 B.R. 842 (Bankr. D. Ariz. 2003) for a good discussion of how §106 works.

Side Note 10-2: More on 'reasonably equivalent value" in a §548 fraudulent transfer action

As noted in the text, the Supreme Court in *United States v. Cartwright*, 411 U.S. 546, 551 (1973) interpreted the phrase "reasonably equivalent value" in §548 to mean the fair market value of the property involved as of the date of the transfer, or more specifically, the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts. Applying a strict fair market value

standard to determine reasonable equivalence does not always work, however, particularly where the benefit received by the transferee is indirect or intangible. See, e.g., *Mellon Bank N.A. v. Metro Commcns., Inc*., 945 F.2d 635, 644-645 (3d Cir. 1991) (value of transfer was the intangible benefit of improving debtor's ability to borrow capital), and *In re Jumer's Castle Lodge, Inc*., 338 B.R. 344 (C.D. Ill. 2006) (debtor received more in value than it transferred, since transfer made it more attractive to investors and financiers). The most that can be said about reasonable equivalence, then, is that it "should depend on all the facts of each case an important element of which is market value. Such a rule requires case-by-case adjudication with fair market value of the property transferred as a starting point." *In re Morris Communication NC, Inc*., 914 F.2d 458, 466-467 (4th Cir. 1990).

A good case in which to see how the courts analyze the reasonably equivalent value concern in a §548 fraudulent transfer case as well as how the transferee concepts of §550 work is *In re Tousa, Inc*., 680 F.3d 1298 (11th Cir. 2012). Read and analyze the case by answering the following: What was the property of the debtor transferred in that case? What made the transfer fraudulent under §548? What was the reasonably equivalent value argument made by the defendants? Did it matter that the defendants received value indirectly rather than directly? What was the factual argument of defendants that they were not entities for whose benefit the transfer was made?

Chapter Twelve

Side Note 12-1: Other Issues Surrounding the Potential Discharge of Student Loan Debt

Can a bankruptcy court declare only part of a student loan dischargeable based on undue hardship or is it an all or nothing proposition? Take a look at *In re Saxman*, 325 F.3d 1168 (9th Cir. 2003) and *In re Hornsby*, 144 F.3d 433 (6th. Cir. 1998). If you are not in the Ninth or Sixth circuits, you might want to see where your see if the courts of your district or circuit have addressed this question.

Are exam prep loans (e.g., ACT or GRA exam prep, CPA or bar exam prep, etc.) dischargeable in bankruptcy or are they a type of student loan that must meet the undue hardship test to be discharged? Interestingly, there is a split on this question. A 2016 New York case found such a loan not to be an educational loan and thus to be dischargeable without a showing of undue hardship. See *In re Campbell*, 547 B.R. 49 (Bankr. E.D.N.Y. 2016) citing decisions taking both sides of the question. You might want to see how the courts of your federal district or circuit have ruled on this issue.

A good scholastic article dealing with the policy behind the undue hardship test for discharging student loans is *The Real Student-Loan Scandal: Undue Hardship Discharge Litigation*, by Rafael I. Pardo and Michelle R. Lacy in Am Bankr. L.J. Volume 83, Issue 1 2009 (accessible online at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1121226). Do you agree or disagree with the conclusion of the article? Remember that what constitutes undue hardship is not defined in the Code. Should courts sympathetic to the need for change in this area simply redefine what undue hardship means or should we await congressional action?

Side Note 12-2: **Further Discussion of the Anti-discrimination Protections of §525**

Corporate debtors are protected by the anti-discrimination provisions of §525 as well as individual debtors. An interesting case construing the "solely because" language of §525(a) in the context of a regulated corporate debtor is *FCC v. NextWave Personal Communications, Inc*., 537 U.S. 293 (2003) in which the FCC's sought to justify revoking the license of the debtor for failure to pay a discharged debt by its mandate to regulate licensees based on their financial soundness. Read the opinion of Justice Scalia to see how that argument worked out for them.

Section 525 protections have been found to attach *prior* to the actual bankruptcy filing but not all courts agree. See *In re Mayo*, 322 B.R. 712 (Bkrtcy. D. Vt. 2005); but compare *In re Kanouse*, 168 B.R. 441 (S.D. Fla. 1994), (aff'd 53 F.3d 1286, certiorari denied, 516 U.S. 930).

The applicability of the antidiscrimination provisions in employment raises the question of whether they create a new private right of action for employment discrimination supplementing other common law and statutory protections for workers (see *In re Lesniewski*, 246 B.R. 202 (E.D. Pa. 2000).

Chapter Fourteen

Side Note 14-1: Impact of Bankruptcy on the Individual Debtor's Credit Rating

An individual debtor's filing for bankruptcy is reported to credit reporting agencies and reflected in their credit history and credit score. Under the Fair Credit Reporting Act (FCRA), a bankruptcy filing as a public record can appear on the debtor's credit history for ten years following the date of filing (15 U.S.C. §1681c) though some agencies voluntarily retain records on Chapter 13 filings for only seven years to encourage debtors to choose that option. Specific debt obligations owed by the debtor at the time bankruptcy is filed remain on the credit report for seven years following the original delinquency date of such obligation (which may have preceded the date of the bankruptcy petition and so will be removed from the report before the bankruptcy proceeding itself is removed). A debt obligation discharged in the bankruptcy case may remain on the credit report until the time to remove it expires but will be labeled "discharged in bankruptcy." The debtor's credit score that is calculated by the credit reporting agencies and used by creditors in the decision to make new loans or extensions of credit is of course impacted negatively by the bankruptcy filing and may take years to repair. Post-bankruptcy, debtors may be able to secure new loans or credit but often at significantly higher interest rates due to the damage done.

Chapter Sixteen

Side Note 16-1: Plan Modification in light of the Policy Behind Chapter 13 Debt Adjustment for Individuals

A thoughtful article on modification of Chapter 13 plans is *Modified Plans of Reorganization and the Basic Chapter 13 Bargain*, by Professor David Gray Carlson accessible online at file:///C:/Users/Owner/Downloads/SSRN-id1554019.pdf. If you are interested in the policy behind the Chapter 13 debt adjustment procedure you may enjoy this article. What does Carlson mean by the "basic Chapter 13 bargain"? Why are many bankruptcy courts resistant to proposed modifications of Chapter 13 plans? What does Carlson argue that such courts are missing?

Side Note 16-2: Espinoza: Discharging Student Loan Debt Without Proving Undue Hardship

Student loan obligations are nondischargeable in a Chapter 13 case to the same extent as in a Chapter 7 case: only upon a showing of undue hardship. But in *United Student Aid Funds, Inc. v. Espinoza*, 559 U.S. 260 (2010) a Chapter 13 debtor proposed a plan to pay only the principal balance of his student loans and to discharge the accrued prepetition interest. But debtor never made a claim of undue hardship. The creditor failed to file a timely adversary proceeding objecting to the dischargeability of the debt (within 60 days following the first meeting of creditors per FRBP 4007) or to confirmation and the plan was confirmed and a discharge granted. Three years later the creditor asked that the discharge be set aside so it could collect the discharged portion of the debt. The Supreme Court found that the creditor's rights had not been violated since it had received adequate notice of the plan and its contents and the discharge was upheld despite there having been no undue hardship determination. After *Espinoza*, are other Chapter 13 debtors with student loan debts likely to succeed in discharging all or part of that debt without an undue hardship determination as that debtor did? What will the standing trustee probably do now when they spot a plan proposing to discharge such a debt? Can such a plan meet the good faith requirement required for confirmation?

Side Note 16-3: How Many Chapter 13 Cases Actually Succeed?

The available empirical data going back 25 years seems to indicate that, nationwide, only one out of every three Chapter 13 cases succeeds in the sense that the debtor pays as scheduled throughout the term of a confirmed plan and receives a discharge at the end. There is considerable variation from state to state and even district to district, but nationwide that percentage appears accurate. See, e.g., *The Pretend Solution: An Empirical Study of Bankruptcy Outcomes*, 90 Tex. L. Rev. 103, 107-111 (2011) (only one in three cases filed under Chapter 13 ends in discharge); Scott F. Norberg & Andrew J. Velkey, *Debtor Discharge and Creditor Repayment in Chapter 13*, 39 Creighton L. Rev. 473, 505, n.70 (2006) ("The overall discharge rate for the debtors in the seven districts covered by the Project was exactly the oft-repeated statistic of one-third."); Gordon Bermant & Ed Flynn, *Measuring Projected Performance in Chapter 13: Comparisons Across the States*, 19 Am. Bankr. Inst. J. 22, 22 (July-Aug. 2000); Henry E. Hildebrand, III, *Administering Chapter 13—At What Price*?, 13 Am. Bankr. Inst. J. 16,

16 (July-Aug. 1994); Katherine Porter, *The Pretend Solution: An Empirical Study of Bankruptcy Outcomes*, 90 Tex. L. Rev. 103 (2011).

But not everyone agrees that an uncompleted Chapter 13 plan is necessarily a failure. See, e.g., Gordon Bermant, *What Is "Success" in Chapter 13? Why Should We Care*? 23 Am. Bankr. Inst. J. 20, 65 (Sept. 2004), arguing that plan completion and discharge are not essential to success if the plan goes on long enough that debtor's finances are substantially reordered.

Chapter Seventeen

Side Note 17-1: Should Individuals be Allowed to File under Chapter 11?

The topic of individuals filing in Chapter 11 is an interesting and controversial one. That chapter of the Code seems designed for businesses rather than individuals. Research some of the criticisms historically raised to individuals being allowed to file in Chapter 11 at all. A good place to start is by reading *The Sub Rosa Subchapter: Individuals in Chapter 11 after BAPCPA*, by Judge Bruce A. Markell (University of Illinois Law Review, Vol. 2007 page 67) (accessible online at https://www.illinoislawreview.org/wp-content/ilr-content/articles/2007/1/Markell.pdf . What do you think? Should individuals should be able to file under Chapter 11?

Side Note 17-2: Change in the Venue Statute for Chapter 11 Cases?

In June 2021 H.R. 4193, the Bankruptcy Venue Reform Act of 2021, was introduced in Congress with bipartisan support. The bill would require that Chapter 11 proceedings actually take place in the federal district where the debtor has its principal place of business or principal assets. The option to file in the same district where the case of an affiliate, general partner, or partner would be eliminated. According to its sponsors, the bill aims to, "ensure that the employees, small businesses, and local communities that are most impacted by a Chapter 11 bankruptcy are able to fully and fairly participate in the proceedings." (As quoted in *Legislative Highlights*, ABI Journal, August 2021, page 10.) You can see the text of the proposed legislation and track its current status at www.congress.gov/bill/117th-congress/house-bill/4193.

Side Note 17-3: More on the Role of the Bankruptcy Examiner

Historically, appointment of a bankruptcy examiner is rare. One study found that an examiner is requested in only 9 percent of all cases, and appointed in just 4 percent of cases. See, Jonathon C. Lipson & Christopher Fiore Marotta, *Examining Success*, Temple University Legal Studies Research Paper No. 2015-17 (2015) (accessible online at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2568178). On the other hand, when examiners do get involved, their impact can be significant. For example, in 2009, prominent

Chicago attorney Anton Valukus was appointed by the court in the Lehman Bros. bankruptcy case to report on the causes of Lehman's demise. A year later Valukus and his team produced a 2,200-page report detailing a culture of excessive risk taking, duplicity, and outright fraud at the investment firm, including a dubious accounting trick that fraudulently removed encumbered assets from the firm's balance sheet and allowed it to grossly overstate liquidity.

Professor Daniel J. Bussel feels that examiners should be used more often in the bankruptcy process. In his article, *A Third Way: Examiners as Inquisitors*, 90 Am. Bankr. Law J. 59 (2016) (accessible online at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2587273), Bussel observes that the American bankruptcy system has its roots in the English chancery courts which did not employ adversarial methods. Examiners can play a neutral but informed role to investigate facts and assess and apply the law to resolve difficult legal disputes within bankruptcy cases. This "inquisitorial model" was successfully used in the case of *In re Tribune Company*, Bankr. Case No. 08-13141 (Oct. 31, 2011 Bankr. Del.) (Opinion on Confirmation accessible online at https://casetext.com/case/in-re-tribune-co-13) to investigate highly complicated pre-and postpetition transfers that were to be incorporated in a plan of reorganization, confirmation of which was being held up because of disputes over the transfers. More than a mediator, the examiner was authorized to hire attorneys and financial advisors and to issue subpoenas for oral deposition and production of documents. After three months of intense work, the examiner issued a four-volume, 1,400-page narrative and legal analysis that demonstrated that the transactions at issue were fraudulent, and therefore the plan was not confirmable. Professor Bussel notes that examiners have been used in this way in several subsequent bankruptcy cases to investigate and mediate claims by creditors of improper financial dealing, uncovering facts and vindicating legal rights far more quickly and economically than in adversarial litigation. At present, the examiner model works best with larger cases, where there are ample resources for conducting investigations expeditiously. However, Professor Bussel concludes, more courts should be willing to willing to opt for examiners under §1104(c) as an alternative to confidential settlements and protracted litigation.

Side Note 17-4: History of the Necessity Doctrine

The history and development of the necessity doctrine illustrates the extent to which common law rules and practices still influence modern statutory practice as under the Code. The doctrine arose out of the common law 'necessity of payment' doctrine established in railroad reorganization cases in the late 1800's. *In re K-Mar*t, 359 F.3d 866, 871 (7th Cir. 2004) criticized the common law origin of the doctrine saying, "A 'doctrine of necessity' is just a fancy name for a power to depart from the Code" and said authorization for motions must be found in the Code itself but not all courts agree. The doctrine also calls attention to §105(a) of the Code ("The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title") that bankruptcy judges have historically relied on to fashion equitable remedies and procedures not expressly addressed in the Code. Is that section essentially an invitation to utilize common law principles in Code cases where the Code is silent?

Chapter Eighteen

Side Note 18-1: More on the §363(b)(1) Sale as a Sub Rosa Plan of Reorganization

Clearly the driving force behind bankruptcy court's allowing the §363(b)(1) sale over an objection that it is effectively a *sub rosa* plan of reorganization is the desire to maximize the return to the estate (see, e.g., *In re Ames Dept. Stores, Inc*., 136 B.R. 357, 359 (Bankr. S.D.N.Y. 1992). In contrast to the tolerant attitude toward this procedure in *In re Lionel Corp*. cited in the text, read *In re Braniff Airways, Inc*., 700 F.2d 935 (5th Cir. 1938). And see how various courts have adopted more specific requirements to clarify the "sound business purpose" test of *In re Lionel Corp*. See, e.g., *In re Titusville Country Club*, 128 B.R. 396 (Bankr. W.D. Pa. 1991); *In re Plabell Rubber Products, Inc*., 149 B.R. 475, 479 (Bankr. N.D. Ohio 1992); *In re Weatherly Frozen Food Group, Inc*., 149 B.R. 480, 483 (Bankr. N.D. Ohio 1992); and *In re Delaware & Hudson Ry. Co*., 124 B.R. 169 (Bankr. D. Del. 1991). You might want to see where your federal district or circuit stands on this.

For a particularly insightful case applying most of the factors mentioned in the text used by courts to evaluate a §363 motion to sell (notwithstanding a plan of reorganization proposed by creditors), see *In re GSC, Inc.*, 435 B.R. 132 (Bankr. S.D.N.Y. 2011).

Statistics regarding the percentage of cases in which §363 sales occur taken from *UCLA-LoPucki Research Database, 363 Sales of All or Substantially All Assets in Large Public Company Bankruptcies, as a Percentage of All Cases Disposed, by Year of Case Disposition*, available online at http://lopucki.law.ucla.edu/tables_and_graphs/363_sale_percentage.pdf.

Chapter Nineteen

Side Note 19-1 (Not referenced in the text): Non-debtor Releases in Chapter 11 Reorganizations

The Chapter 11 bankruptcy case filed in 2019 by Purdue Pharma (makers of OxyContin, one of the primary opioid-based pain relief drugs involved in the opioid addiction holocaust that has to date taken 500,000 lives in the U.S. via drug overdoses and is implicated in millions of cases of opioid use disorder) in the Southern District of New York, raised the contentious issue of the use of non-debtor releases in Chapter 11 plans. Purdue Pharma was owned by members of the Sackler family who collectively earned more than $10 billion for the distribution and sale of OxyContin. The OxyContin scandal has exposed Purdue Pharma and its affiliated companies, the Sacklers, and numerous other individuals to claims of civil liability as well as possible criminal culpability. The plan of reorganization proposed by debtor in the Chapter 11 case, offered for the Sackler family itself to pay about $3.4 billion to go toward the various claims and to forfeit its ownership interests in Purdue Pharma. But in exchange, the plan proposed that the Sacklers individually as well as hundreds of their associates and all their other corporations trusts and other entities the Sacklers' control receive releases from any further liability for non-derivative, direct or particularized claims, not derivative of the debtor's liability (e.g., claims against the Sacklers or their associates individually for their alleged misconduct rather than the misconduct of the debtor and for their alleged breach of duties owed to claimants other than the debtor itself). In September 2021, after two years of negotiations and over the outraged protests of opioid reform activists as well as the

opposition of the U.S. Department of Justice, the proposed plan was approved by the bankruptcy judge in the case. You can read about the issue at www.npr.org/2021/09/01/1031053251/sackler-family-immunity-purdue-pharma-oxcyontin-opioid-epidemic#:~:text=Television-,Sackler%20Family%20Wins%20Immunity%20From%20Opioid%20Lawsuits%20In%20Purdue%20Pharma,liability%20for%20the%20opioid%20crisis and the bankruptcy judge's decision at *In re Purdue Pharma L.P.*, __B.R. __, 2021 WL 4240974 (Bankr. S.D.N.Y. Sept. 17, 2021). Do you agree with the bankruptcy judge that this settlement is the best of imperfect options for Purdue Pharma and its creditors?

The Bankruptcy Court's approval of the Purdue Pharma plan including these non-debtor releases for the Sacklers family, their associates, and other entities, triggered a bill to be introduced in Congress to ban the use of non-debtor releases in bankruptcy reorganizations: *The Nondebtor Release Prohibition Act of 2021*. See the House Judiciary Committee press release at https://judiciary.house.gov/news/documentsingle.aspx?DocumentID=4776. Before Congress could act on that proposed legislation, the U.S. District Court in an order entered December 16, 2021, reversed the bankruptcy court's approval of the plan holding that federal bankruptcy law does not give the bankruptcy courts the authority to grant a release from liability for people who are not themselves bankruptcy debtors when creditors in the bankruptcy case object. See the article at www.npr.org/2021/12/16/1065047471/judge-rejects-purdue-pharmas-opioid-settlement-that-would-protect-the-sackler-fa and read the district court opinion at You can read the opinion of the district court at https://portal.ct.gov/-/media/AG/Press_Releases/2021/Judge-McMahon-Decision-121621.pdf.

The decision of the district judge will undoubtedly have been appealed by the time you read this. Check and see what the status of the case and the proposed plan are at this time. Also check and see what the status of the aforementioned legislation before Congress is as of now. Should non-debtor releases be prohibited across the board in bankruptcy reorganizations or merely subjected to strict conditions? When might a non-debtor release arguably be in the best interest of the creditors of a reorganizing debtor?

The bill before Congress also addresses the related problem of 'divisional mergers' that frequently allow corporations to shield their assets from victims. Essentially the corporate strategy involves transferring potentially troublesome claims or assets to a new entity to separate them from the cleansed entity, then causing the new entity burdened with the liability claims to file bankruptcy. Read a good summary of the various provisions of the bill including how it proposes to limit the divisional merger strategy at www.stevenslee.com/news/congress-advances-legislation-to-limit-nondebtor-bankruptcy-relief/. Do you agree with the bill's approach to limiting divisional mergers in bankruptcy cases?

END