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In This Issue

BEASTS OF BURDEN

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I've picked up certain tips and rules-of-thumb over the years that frequently help me in my practice. For example, one is to always "identify the property of the estate at issue." I can't think of a specific example, but remembering to simply identify the specific property of the estate at issue has often helped me clarify my thoughts about a seemingly complex case or issue. Another helpful tip I've received is to always know which party in a proceeding or matter carries the burden of proof.

As bankruptcy attorneys, we enjoy what is sometimes described as a comparably relaxed or informal atmosphere in the Bankruptcy Courts. I don't know exactly why that is, but I imagine it stems from the need to administer thousands (yes it's still *thousands*) of bankruptcy cases, each of which can span a number of years and involve many hearings, along with an acknowledgement that bankruptcy cases inherently involve a limited pool of assets that must be administered as efficiently as possible. Such considerations don't encourage too "lawyerly" an approach. But at some point, if a dispute cannot be resolved, Bankruptcy Courts, like other courts, will require the development of an evidentiary record to rely on in rendering a decision on any given issue.

Understanding which party carries the burden of proof not only helps avoid showing up at a hearing totally unprepared, but it also assists in analyzing and tailoring your approach to the hearing. To help me in this regard, I've kept a cheat sheet of certain burdens of proof that I've picked up over the years. There are more, but below I share with you the most common. I hope you find value in them.

Chapter 13 Confirmation.

- Debtor bears the burden of showing that the proposed plan satisfies the standards of confirmation by a preponderance of the evidence.

- *Domestic Support Obligations.* The non-debtor party has the burden of proving by a preponderance of the evidence that the debt is a domestic support obligation. *In re Cummings*, 523 B.R. 93 (Bankr. W.D. Mich., 2014).

Motion to lift or modify the automatic stay.

- Shifting burden: §362(d)(1) requires an initial showing of cause by the movant (a prima facie case); §362(d)(2) and 362(g) require an initial showing by movant of debtor's lack of equity in the property. *In re Holly's, Inc.*, 140 B.R. 643, 683 (Bankr. W.D. Mich. 1992).

- The party opposing relief carries the burden on all other issues. §362(g)(2).

Subject Matter Jurisdiction.

- Plaintiff has the burden of proving subject matter jurisdiction by a preponderance of the evidence. *Hedgepeth v. Tennessee*, 215 F.3d 608, 611 (6th Cir. 2000).

Objection to Exemptions.

- Exemptions to be liberally construed in favor of the Debtor and the burden of proof is on the objecting party. *Menninger v. Schramm (In re Schramm)*, 431 B.R. 397, 400 (B.A.P. 6th Cir. 2010; Fed. R. Bankr. P. 4003(c).

Approval of Professional Fees.

- A professional seeking approval of fees and expenses bears the burden of proof by a preponderance of the evidence. *In re Cripps*, 549 B.R. 836 (Bankr. W.D. Mich., 2016).

Dismissal.

- Party moving to dismiss bears the burden of proving by a preponderance of the evidence that cause for dismissal exists. *In re Cohara*, 324 B.R. 24, 27 (6th Cir. B.A.P. 2005).

Section 523 Dischargeability of Particular Debts.

- Creditor bears the burden of proving by a preponderance of the evidence that its claim falls within the exception to discharge. *Hart v. Molino (In re Molino)*, 225 B.R. 904, 907 (6th Cir. 1998).

- *Two Exceptions where non-dischargeability presumed*:

    - §523(a)(2)(C)(i)(I): consumer debts of more than $675 for luxury goods/services within 90 days before filing.

    - §523(a)(2)(C)(i)(II): cash advances totaling more than $950 within 70 days of filing.

Proof of Claim.

- Proof of claim filed in accordance with the rules is prima facie evidence of validity and amount of the claim. *See* Fed. R. Bankr. P. 3001(f). A party in interest who challenges such a proof of claim must produce evidence to rebut the presumption. Fed. R. Evid. 301; *In re Kemmer*, 315 B.R. 706, 713 (Bankr. E.D. Tenn. 2004).

    - If the objecting party rebuts the validity or amount of the claim, the burden reverts to the claimant to prove the claim by a preponderance of the evidence.

Use, Sale, or Lease of Property.

- Trustee has burden of proof on the issue of adequate protection of creditors. §363(p)(1).

- Entity asserting interest in property has the burden of proof on the issue of the validity, priority, or extent of such interest. §363(p)(2).

Preference Actions §547.

- Trustee has the burden of proof by a preponderance of the evidence on all elements of the claim.
- The debtor's insolvency is presumed if transfer occurred within 90 days of the petition date. §547(f).
- Defendant bears the burden of proving by a preponderance of the evidence on any affirmative defense.

Fraudulent Transfers §548.

- Trustee has the burden of proof by a preponderance of the evidence on all elements of the claim.
- Defendant bears the burden of proving by a preponderance of the evidence on any affirmative defense.

THE DISCHARGEABLILITY OF SINGLE ASSET MISREPRESENTATIONS AFTER THE SUPREME COURT'S RULING IN *LAMAR*

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I. Background

The Supreme Court's recent ruling in *Lamar, Archer & Cofrin, LLP v. Appling*, 138 S.Ct. 1752 (2018), clarified the distinction between section 11 U.S.C. § 523(a)(2)(A) and section 523(a)(2)(B). Specifically, the Supreme Court held that an oral misrepresentation about a single asset may qualify as a statement respecting a debtor's financial condition, which requires the heightened requirements of section 523 (a)(2)(B).

In *Lamar*, the law firm of Lamar, Archer & Cofrin, LLP ("LAC") objected to discharge of fees owed by one of LAC's former clients, Appling. In 2005, LAC threatened to withdraw from representation unless Appling paid his outstanding attorney's fees of more than $60,000.00. Appling told LAC that he expected a tax refund of over $100,000.00, and that he would use those funds for current and future fees. Based on Appling's representations, LAC continued litigating on Appling's behalf. However, when Appling received his tax refund, it was for substantially less than he originally anticipated and he decided to use the tax refund to support his business rather than paying LAC. A few months after their first meeting, LAC requested another meeting with Appling regarding his outstanding invoices. Rather than tell LAC that his refund was for less than he anticipated or that he used the funds for other expenses, Appling told LAC that his refund was delayed. Based on its continued belief that its fees would be paid from Appling's tax refund, LAC agreed to complete the pending litigation. Appling never paid his attorney's fees, and in 2011 LAC filed a lawsuit against Appling. LAC subsequently obtained a judgment against Appling for $104,179.60, and Appling filed for protection under Chapter 7 of the United States Bankruptcy Code.

LAC objected to Appling's discharge under 11 U.S.C. § 523(a)(2)(A) because LAC argued that the debt was incurred through "false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's….financial condition[1]." Appling moved to dismiss the adversary complaint by arguing that his alleged misrepresentations were statements respecting his financial condition, which are therefore governed by 523(a)(2)(B)[2]. Appling further argued that LAC could not object to discharge of the debt because the statements were not "in writing" as required for non-dischargeability under section 523(a)(2)(B).

The Bankruptcy Court held that "a statement regarding a single asset is not "a statement respecting the debtor's financial condition[3]" and the District Court affirmed the ruling after the trial. However, Appling appealed to the Court of Appeals for the Eleventh Circuit, which reversed. The Eleventh Circuit determined that "statement[s] respecting the debtor's . . . financial condition

[1] 11 U.S.C. § 523(a)(2)(A)
[2] See *Lamar, Archer & Cofrin v. Appling*, 138 S.Ct. 1752, 1758 (2018)
[3] *Id.*

may include a statement about a single asset[4]". Accordingly, because Appling's statements regarding the receipt and use of his tax refund were not in writing, his debt was not barred from discharge by 11 U.S.C. § 523(a)(2)(B).

The Supreme Court granted certiorari and affirmed the Eleventh Circuit's conclusion.

II. Supreme Court's Analysis

The Supreme Court's holding in Lamar is premised upon three principles:

1. Interpretation of the term "respecting."

The Court spent the majority of its opinion analyzing the term "respecting" as it applies to 11 U.S.C. § 523(a)(2)(B). LAC argued that the term "respecting" should be interpreted under its more limited definitions such as "about," "concerning," "with reference to" and "as regards."[5] Therefore, LAC argued that "respecting" includes "formal financial statement[s] providing a detailed accounting of one's assets and liabilities."[6] However, "a statement about a single asset would not"[7] be included.

The Court disagreed. The Court found that the definitions of the terms used to define "respecting" were "overlapping and circular with each one pointing to another in the group."[8] Furthermore, the Court found that the word "respecting" when used "in a legal context generally has a broadening effect, ensuring that the scope of the provision covers not only its subjects but also matters relating to that subject."[9] Conversely, LAC's limited definition would essentially read "respecting out of the statute."[10]

The Court found that "a statement is 'respecting' a debtor's financial condition if it has a direct relation to or impact on the debtor's overall financial status. A single asset has a direct relation to and impact on aggregate financial condition, so a statement about a single asset bears on a debtor's overall financial condition and can help indicate whether a debtor is solvent or insolvent, able to repay a given debt or not."[11] Therefore, "a statement about a single asset can be a statement respecting the debtor's financial condition."[12]

2. Incoherent Results

The Court also premised its decision on the incoherent results that would occur under LAC's interpretation. The Court reasoned that the heightened dischargeability requirements of 11 U.S.C. § 523(a)(2)(B) should not turn on the "superficial packaging of a statement rather than its

[4] *Id*.
[5] See Id. at 1759
[6] Id.
[7] Id.
[8] Id.
[9] Id. (internal citations omitted)
[10] Id. at 1761
[11] Id.
[12] Id.

substantive content."[13] For instance, under LAC's interpretation, a misrepresentation about a single asset that was made within the context of a formal written financial statement would require the heightened requirements of section 523(a)(2)(B); whereas, the same statement made individually or within a partial list of liabilities and assets would not require the same heightened scrutiny.

3. Historical Corroboration

Finally, the Court concluded that the statutory history of the phrase "statement respecting the debtor's financial condition" supported the Court's reading of the text[14]. The phrase was first included in the 1926 amendment to the Bankruptcy Act of 1898, which prohibited from discharge debts obtained through "… a materially false statement in writing respecting his financial condition." From 1926 through 1978 Courts of Appeals had ample opportunity to weigh in on the interpretation of the phrase. Congress was aware of those decisions when it enacted the Bankruptcy Code and chose to include it in section 523(a)(2)[15].

In addition to the three significant analytical points that the Court included in its analysis, the Court also found LAC's arguments regarding the undermining nature of the decision unpersuasive. LAC argued that the broad interpretation undermined section 523(a)(2)(A) and resulted in debtors being able to "swindle innocent victims for money, property or services by lying about their finances, then discharge the resulting debt in bankruptcy, as long as they did so orally."[16] However, the Court determined that 11 U.S.C. § 523(a)(2)(A) was still available to apply to specific forms of fraud, such as fraudulent conveyance schemes. Furthermore, it found that the heightened requirements of section 523(a)(2)(B) do not act as a shield for dishonest debtors. Rather, they reflect Congress' effort to balance the potential misuse of such statements by both debtors and creditors. The Court cited the House Report on the Bankruptcy Reform Act of of 1978, which indicated that Congress specifically included the heightened requirements of section 523(a)(2)(B) in order to reduce the burden on individuals and offset frequent abuses by lenders.[17] The House Report specifically identified and targeted lenders that designed their application process to induce the debtor to include information that could later be used by the lender to object to discharge.

III. <u>The effect on practitioners</u>

Occasionally, a debtor files for bankruptcy for non-contractual reasons such as negligence. However, the vast majority of filings include one or more contractual defaults. Accordingly, in almost every case, the result of a bankruptcy discharge is that at least one creditor will not receive their contractually due consideration. Not surprisingly, this means the most common adversary proceeding questions that bankruptcy practitioners answer are in regards to fraud. Many creditors who receive notice of a bankruptcy filing assume the only reason they weren't paid was because of fraudulent activity by the debtor. On the other hand, by the time many debtors consult

[13] Id.
[14] See Id. at 1762
[15] Id. at 1762
[16] Id. at 1763
[17] Id at 1763-64

with an attorney, they are terrified by the specter of fraud based on allegations that have been thrown at them by their creditors.

One of the most difficult questions for bankruptcy attorneys to address is the dischargeability of a debt that was incurred through an oral statement by the debtor regarding a single asset, and that was allegedly false. The Court's decision in *Lamar* helps provide guidance to both creditors and debtors regarding which representations require the heightened requirements of section 523(a)(2)(B). The Court has confirmed to creditors, debtors, and their respective counsel that even single asset representations regarding a debtor's financial condition must be made in writing and fulfill the other heightened requirements of 11 U.S.C. § 523(a)(2)(B) in order to be non-dischargeable.