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<u>Belated Amended Claims in Chapter 13 Bankruptcies</u>

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Perhaps at least in part due to the COVID pandemic these last two years, it seems as though bankruptcy courts have increasingly faced the challenge of dealing with amended claims that are filed several months, or even one or two years, after the timely-filed initial claims. Sometimes, the amended claim is filed at a time when the Chapter 13 trustee has already disbursed large amounts of money to that class of creditors, and allowance of such an amended claim could force the trustee to pursue overdisbursement from other creditors in that same class of claims. What tests or factors are courts applying in concluding whether an amended claim should be allowed in a Chapter 13 case? Is it relevant whether a confirmed Chapter 13 Plan provides for a deadline for which an amended claim shall be filed?

Because this issue pertains to a proof of claim, it seems only natural to start with the plain language of both 11 U.S.C. §502(a)(9) and Fed. R. Bankr. P. 3002(c). 11 U.S.C. § 502(b)(9) provides, in relevant part, that "if such an objection to the claim is made, the court, after notice and a hearing, shall determine the amount of such claim . . . and shall allow such claim in such amount, except to the extent . . . proof of such claim is not timely filed, except to the extent tardily filed as permitted under paragraph (1),(2), or (3) of section 726(a) of this title or under the Federal Rules of Bankruptcy Procedure. Fed. R. Bankr. P. 3002(c), in turn, provides for the timeline for determining whether a claim should be considered "not timely filed" by stating that "[i]n a voluntary chapter 7 case, chapter 12 case, or chapter 13 case, a proof of claim is timely filed if it is filed not later than 70 days after the order for relief under that chapter or the date of the order or conversion to a case under chapter 12 or chapter 13." The Sixth Circuit in *Tench,* 2016 WL 2822497 at *8 (B.A.P. 6th Cir. May 11, 2016) set a straight-forward, strict standard as to whether late-filed claims in a Chapter 13 case should be allowed and limited such an allowance to only the enumerated exceptions of 11 U.S.C. § 502(b). The Panel in *Tench* went even further and rejected the application of the equitable tolling doctrine in the instance when a creditor pleads "excusable neglect" in the delay with filing a timely claim. *In re Tench,* 2016 WL 2822497 at *7. While Fed. R. Bank. P. 3002(c) may seem like the natural starting point in a case dealing with an amended claim, it only pertains to the filing of the initial claim, and, in actuality, the Bankruptcy Code and Bankruptcy Rules are silent as to deadlines relating to amended claims. *See, In re Tesch,* Case No.

GK 19-01509 at *6 (Bankr. W.D. Mich. May 10, 2021). Thus, in the absence of direction from the Bankruptcy Code and Bankruptcy Rules, upon what does a court rely?

Because the Bankruptcy Code and Rules do not speak to the issue of amended claims, courts have traditionally fashioned at least two different approaches in discerning whether belated amendments should be allowed. Fed. R. Bankr. P. 7015, which renders Fed. R. Civ. P. 15 applicable in adversary proceedings, provides the foundation for some bankruptcy courts in allowing belated amended claims and in assessing whether the amended claims "relate back" to the original claim. *See, e.g., In re Spurling,* 391 B.R. 783, 786 (Bankr. E.D. Tenn. 2008) ("In the absence of any specific rules concerning the amendment of proofs of claim, the courts have often looked to Fed. R. Civ. P. 15(c) for guidance"); *but cf. In re Tesch,* Case No. GK 19-01509 at *7 (holding that Fed. R. Civ. P. 15 does not apply because a proof of claim is not a "pleading"). Several courts have engaged in a conjunctive two-step inquiry in determining whether a belated amended claim should be allowed, and the first step applies the "relation back" standard. An amended claim will meet the threshold of "relating back" to the initial claim if it "' 1) corrects a defect of form in the original claim; 2) describes the original claim with greater particularity; or 3) pleads a new theory of recovery on the facts set forth in the original claim.'" *In re Enron Corp,* 419 F.3d 115, 133 (2nd Cir. 2005)(citing *In re McLean Indus. Inc.* 121 B.R. 704, 708 (Bankr. S.D.N.Y. 1990 *citing in re G.L. Miller & Co.,* 45 F.2d 115, 116 (2d Cir. 1930)). A change in a claim's status from secured to unsecured for a debt under one note arises out of the same transaction, and thus an amendment would "relate back" or bear a "reasonable relationship" to the original claim. *See, e.g. In re Channakhon,* 465 B.R. 132, 142 (Bankr. S.D.Ohio 2012); *see also In re Spurling,* 391 B.R. 783, 788 (Bankr. E.D. Tenn. 2008). The Sixth Circuit Court of Appeals allowed a claimant to amend its original unsecured claim to a secured claim by showing its security. *Szatkowski v. Meade Tool & Die Co (in re Meade Tool & Die Co.),* 164 F.2d 228 (6th Cir. 1947).

If the "relation back" step of the two-step inquiry is satisfied, the courts then proceed to the second step which applies a standard of "equity" to the case at hand. In this second step, courts will "'examine each fact within the case and determine whether it would be equitable to allow the amendment.'" *In re Enron Corp.,* 419 F.3d at 133 (citing *In re Integrated Res, Inc.,* 157 B.R. 66, 70 (S.D.N.Y. 1993)). In this second step, numerous courts have applied the following balancing factors known as the *Miss Glamour Coats* test seemingly made infamous in the amended claim bankruptcy context by the leading case of *U.S. v. Int'l Horizons, Inc. (in re Int'l Horizons),* 751 F.2d 1213, 1218 (11th Cir. 1985): "(1) whether the debtors and creditors relied upon the Service's earlier proofs of claims or whether they had

reason to know that subsequent proofs of claims would be filed pending the completion of an audit; (2) whether other creditors would receive a windfall by the court's refusing to allow amendment; (3) whether the Service intentionally or negligently delayed in filing its proof of claim stating the amount of corporate tax due; (4) the justification for failure of the Service to file for a timely extension to the bar date; and (5) whether equity requires consideration of any other factors." *See also, Barton v. IRS (in re Burton),* 151 B.R. 110 (Bankr. W.D. Mich. 1993); *In re Jones,* 238 B.R. 338 (Bankr. W.D. Mich. 1999); *In re Dietz,* 136 B.R. 459 (Bankr. E.D. Mich. 1992); *In re Parsons,* 135 B.R. 283 (Bankr. S.D. Ohio 1991); *U.S. v. Kolstad (in re Kolstad),* 928 F.2d 171 (5th Cir. 1991); *In re Las Uvas Valley Daries,* 620 B.R. 367 (Bankr. N.M. 2020); *In re Martinez,* 513 B.R. 779 (Bankr. P.R. 2014). Other courts have adopted the following factors in the second "equitable" step of the two-step inquiry: "[u]ndue delay in filing, lack of notice to the opposing party, bad faith by the moving party, repeated failure to cure deficiencies by previous amendments, undue prejudice to the opposing party, and futility of the amendment." *Moross Ltd. P'ship v. Fleckenstein Cap., Inc.* 466 F.3d 508 (6th Cir. 2006); *see also In re Channakhon,* 465 B.R. at 143; *Matter of Stavriotis,* 977 F.2d 1202 (7th Cir. 1992).

In contrast to the numerous courts applying the afore-mentioned conjunctive two-step inquiry, there appears to be a smaller number of courts that weigh a combination of three factors fairly evenly in their determination of whether an amended claim should be allowed by a court. These courts apply the following three criteria: "First, the proposed amendment must not be a veiled attempt to assert a distinctively new right to payment as to which the debtor estate was not fairly alerted by the original proof of claim. Second, the amendment must not result in unfair prejudice to other holders of unsecured claims against the estate. Third, the need to amend must not be the product of bad faith or dilatory tactics on the part of the claimant." *Gens v. Resolution Trust Corp.,* 112 F.3d 569, 575 (1st Cir. 1997); *Unioil, Inc. v. H.E.Elledge; 270 Corp. (in re Unioil, Inc),* 962 F.2d 988, 993 (10th Cir. 1992); *In re Bozeman,* 616 B.R. 407, 415 (Bankr. M.D.Ala. 2020) (*in dicta*) (stating that "factors that courts consider in balancing the equities include: undue delay, bad faith or dilatory motive on the part of movant"). Since the Bankruptcy Code and Bankruptcy Rules are silent on the issue of amended claims, what if a debtor took it upon himself or herself to deal with the issue of amended claims in a Chapter 13 Plan? Would a provision in a confirmed Chapter 13 plan imposing a deadline for which a claimant should file its amended claim curb the difficulties that a court faces with regard to a belated amended claim?

What is the significance of a provision imposing a deadline for which a claimant should file its amended claim in a confirmed Chapter 13 on the ultimate outcome of whether a court allows this

belated amended claim? The court in *Tesch* squarely faced this issue when it was presented with a creditor who filed its amended deficiency claim relating to a surrendered vehicle almost three months after the 180-day deadline imposed by the confirmed Chapter 13 plan. *In re Tesch,* Case No. GK 19-01509 at *4. The *Tesch* court's analysis ultimately rested upon the authority of Fed. R. Bankr. P. 9006(b) which allows a party to seek an enlargement of time previously established by a court order. *Id.* at *11. In determining whether the creditor's failure to timely file its amended claim established pursuant to the confirmation order was the result of "excusable neglect" under Fed. R. Bankr. P. 9006(b)(1), the *Tesch* court applied the following well-renowned non-exclusive four factors set forth by the United States Supreme Court: "the danger of prejudice to the debtor, the length of the delay and its potential impact on judicial proceedings, the reason for the delay, including whether it was within the reasonable control of the movant, and whether the movant acted in good faith." *Pioneer Inv. Servs. Co. v. Brunswick Assocs. Ltd. P'ship,* 507 U.S. 380, 385 (1993). In applying the *Pioneer* factors to the case at hand, the *Tesch* court determined that while prejudice did not exist as to the debtor and the other general unsecured creditors and the court had no reason to believe the claimant did not act in good faith, claimant's almost three-month delay in the filing of its amended claim when some of the delay was attributable to its own actions or inactions did not constitute "excusable neglect," and the court disallowed claimant's amended deficiency claim. *In re Tesch,* Case No. GK 19-01509 at *12-14.

In the absence of direction provided by the Bankruptcy Code and Bankruptcy Rules, courts have grappled with allowance of amended claims for decades and are bound to face this issue on an increasing basis as the continued COVID pandemic arguably has presented obstacles for claimants to readily file their amended claims. The ultimate outcome of whether a court allows a belated amended claim may in fact differ based upon whether the deadline to file such an amended claim is imposed upon by a confirmed Chapter 13 plan.

Recap of Projected Disposable Income in Chapter 13 Cases – 6th Circuit

By: Rebecca L. Johnson-Ellis

Prior to enactment of the *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* ("BAPCPA") Chapter 13 plan payments were typically calculated by projecting the difference between the amounts provided on debtor's filed Schedules I and J which listed the debtors income and expenses respectively. With the passage of BAPCPA, Congress provided the bankruptcy code with a new sense and direction on how we analyze bankruptcy and determine a debtor's ability to pay on his or her debts. This guidance was further refined as to how to determine the Chapter 13 plan payments with the introduction of new terminology and definitions.

For a case to be confirmed over objection of the trustee or allowed unsecured creditor, the plan per BAPCPA must provide that "all of the debtor's projected disposable income to be received in the applicable commitment period beginning on the date the first payment is due under the plan will be applied to make payment to unsecured creditors under the plan."[i] With that provision, new terminology and definitions were presented in determining the debtor's projected disposable income. The terms "disposable income," "current monthly income," "applicable commitment period," and "median income" were introduced and are defined as follows:

Disposable income is defined as current monthly income received by the debtor, other than child support payments, foster care payments, or disability payments for a dependent child…, less amounts reasonably expended for the maintenance and support of the debtor or a dependent of the debtor.[ii]

Current monthly income ("**CMI**") is defined as the average monthly income from all sources that the debtor receives (or in a joint case the debtor and the debtor's spouse receive)… during the six month period… immediately preceding the commencement of the case and does not include any benefits under the Social Security Act.[iii]

Applicable commitment period ("**ACP**") is defined as three years or if the debtor's combined household income multiplied by twelve is greater than the median family income for that household size, then the ACP is not less than five years.[iv]

Median family income is defined as a number that is "both calculated and reported by the Bureau of the Census in the then most recent year."[v]

Amounts reasonably necessary to be expended is defined for a debtor under the median income as the amount needed for the maintenance and support of the debtor or the debtor's dependents.[vi]

For over median debtors it is the amounts specified in §§ 707(b)(2), 1325(b)(3)(A) or Official Form 122C-1, also referred to the "Means Test."

Once "disposable income" is calculated it is "projected" in a Chapter 13 case to determine the amounts to be paid to unsecured creditors. The challenges that followed were that "projected disposable income" was not specifically defined in the amendments. After BAPCPA, many courts considered what "projected disposable income" actually meant with mixed results. Specifically, courts struggled with how to deal with cases where a debtor's CMI and resulting disposable income resulted in a different number than what the calculations reflected on the debtor's Schedules I and J. The courts adopted two main approaches to determine projected disposable income: the "mechanical approach" and the "forward-looking approach."

The "mechanical approach" of determining projected disposable income took disposable income, as calculated on Form 122A-1, and multiplied that number by the number of months in the commitment period.[vii] The resulting number from that calculation was the amount to be paid to the debtor's unsecured creditors. This was true even if the resulting number on the debtor's Schedules I and J on the date of filing was a different number. This analysis was strictly reliant upon the historical calculation of the debtor's CMI and did not take into account any foreseeable changes in a debtor's income or expenses. This approach somewhat unfairly favored debtors whose historical income was less than what was stated on the date of filing and could greatly reduce what was required to be paid.

The "forward-looking approach" started with the debtor's disposable income as determined by the mechanical approach but was not as rigid and provided considerations for the debtor's actual income and expenses shown on the Schedules I and J on the date of filing. This was the holding in the Supreme Court case of *Hamilton v. Lanning,* 130 S. Ct. 2464, 2478 (2010) which stated that because Congress did not define the term "projected disposable income," that pre-BAPCPA practices still applied, and "that courts may take into account known or virtually certain changes to debtors' income or expenses when projecting disposable income."

The Supreme Court decision in *Lanning* thus held that projected disposable income was the debtor's CMI minus "amounts reasonably necessary to be expended" and the remaining funds left over multiplied by the ACP.[viii] However, if there are any substantial changes in the debtor's income and expenses that are reasonably foreseeable as of the effective date of the plan, those changes can be taken into consideration in determining that projected disposable income.[ix]

On February 16, 2022, the Labor Department released that the consumer price index, or inflation, climbed 7.5% from January 2021 to January 2022, which is the largest 12-month increase since February 1982 and a 39 year high.[x] Further, according to the U.S. Energy Department, gas prices are at their highest since October 2014 and have increased an average of 98 cents a gallon from a year ago, which is a 12-month increase of 46.5%.[xi] Since Chapter 13 projected disposable income is forward looking, and current news is that living expenses are increasing; we should expect to see these increases reflected on a debtor's Schedule J. By following the logic in *Lanning,* a debtor's projected Schedule J expenses showing an increase of 7.5% over the national and local standards should not be surprising and should be given deference as being reasonable.

Another issue presented to the bankruptcy courts after the *Lanning* decision, was whether the ACP was a temporal requirement, meaning the plan had to last three or five years, or if it was merely a multiplier of disposable income to determine the entire amount required to be paid into the plan. For Sixth Circuit cases this issue was decided in the case of *Baud v. Carol*, 634 F. 3d 327(6th Cir. 2011), cert. den., 132 S. Ct. 997 (U.S. Sup. Ct. 2012). In this important case the Sixth Circuit joined the Eighth, Ninth & Eleventh Circuits in determining the ACP, as provided by 11 U.S.C. §1325(b)(1)(B), to be a temporal requirement.[xii] The court clarified that the temporal requirement for under median income debtors who are proposing to pay less than 100% to unsecured claims must provide for a plan length not less than 36 months, and over median income debtors proposing to pay less than 100% to unsecured, plan length must not be less than 60 months.[xiii] The court found this is still true for over median debtors even if the means test shows the debtor has a negative or zero disposable income.[xiv]

The 6th Circuit Court not only recognized the Supreme Court's *Lanning's* forward-looking approach in determining projected disposable income but also recognized there were some provisions of the code that could not be ignored in determining disposable income. It went on to say that any discretion afforded in the *Lanning* case "does not permit bankruptcy court to alter BAPCPA's forms for calculating disposable income."[xv] Holding that the calculation of a debtor's projected disposable income "must exclude income- such as benefits received under the Social Security Act – that are excluded from the definition of current monthly income set forth in §101(10A) and must deduct 'amounts reasonably necessary to be expended' as defined in 1325(b)(3)..."[xvi] It reasoned that although in pre-BAPCPA projected disposable income calculations usually included Social Security benefits when calculating a debtor's disposable income, it recognized with BAPCPA a clear indication was made as to Congress's intent to discontinue that practice by specifically defining CMI.[xvii] BAPCPA's

provision to exclude Social Security benefits for payment on debt is further supported by another federal law, 42 U.S.C. § 407 (a) & (b) of the Social Security Act, which provides:

> (a) The right of any person to any future payment under this subchapter shall not be transferable or assignable, at law or in equity, and none of the moneys paid or payable or rights existing under this subchapter shall be subject to execution, levy, attachment, garnishment, or other legal process, or to the operation of any bankruptcy or insolvency law.
>
> (b) No other provision of law, enacted before, on, or after April 20,1983, may be construed to limit, supersede, or otherwise modify the provisions of this section except to the extent that it does so by express reference to this section.[xviii]

The Sixth Circuit did not specifically discuss whether excluding Social Security income would go astray of a good faith analysis, but by its discussion on the importance of the Code omitting specified income in the definition of CMI, it would seem excluding Social Security benefits would not. Other cases that have decided that omitting Social Security benefits cannot be considered in a good faith analysis are *Drummond v. Welsh* (*In re Welsh*), 711 F. 3d 1120 (9th Cir. 2013) *aff'g Drummond v. Welsh* (*In re Welsh*), 465 843 (B.A.P. 9th Cir. 2012), *Anderson v. Cranmer* (*In re Cranmer*), 697 F. 3d 1314, 1319 (10th Cir. 2011), *Beaulieu v. Ragos* (*In re Ragos*), 700 F. 3d 220, 227 (5th Cir 2012), *Fink v. Thompson,* 439 B.R. 140 (8th Cir. BAP 2010). Although the courts above have found that Social Security benefits are not required to be included in a Chapter 13 debtor's projected disposable income, it is widely accepted that a debtor is not precluded from voluntarily providing a portion or all for payment to show feasibility of the case. [xix]

After BAPCPA Congress has since passed another law to provide further guidance as to what income should not be included in CMI by enacting the Honoring American Veterans in Extreme Need Act of 2019, also known as the HAVEN Act. The passing of the law amended 11 U.S.C. § 101(10)(A) to exclude benefits received by the Department of Veteran's Affairs ("VA") in CMI to mirror the same protections already afforded Social Security benefits.[xx] Prior to the Act being signed into law, these benefits were included in debtor's CMI and debtor's projected disposable income. Although case law is somewhat limited due to the newness of the law, because the provisions of the HAVEN Act mirror that of Social Security benefits, it would seem the courts would follow the decisions already determined in regards to Social Security.

A case in point was recently decided in the Eastern District of Michigan, *In re Gresham*, 616 B.R. 505 (Bankr. E.D. Mich. 2020). In this case the debtor argued her VA disability benefits could be

excluded from her CMI and was not part of her projected disposable income for purposes of 11 U.S.C. §1325(b) and therefore did not need to be contributed to her Chapter 13 plan. The Court held that the debtor may rightfully exclude Veterans Disability Income from her projected disposable income and also found the HAVEN Act could be applied retroactively in Chapter 13 cases pending and already confirmed.[xxi]

Chapter 13 is a vehicle for debtors to be able to pay on their debts but still maintain a reasonable living. What we have learned from *Lanning* is that projecting a debtor's disposable income is done by calculating the debtor's CMI, as defined, subtracting the amounts reasonably necessary to be expended, multiplying the resulting figure by the ACP, and then taking into account all known or virtually certain changes at that time of confirmation. In *Baud* we learned that the ACP is a temporal requirement and if a debtor is under median income his plan shall run 36 months, and if a debtor is over median income his plan shall run 60 months. This is true even if his disposable income is zero or negative. Further, disposable income does not include Social Security benefits, and with the most recent passing of the HAVEN Act, does not include VA Disability and thus neither Social Security or VA benefits need to be included in a debtor's projected disposable income.

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[i] 11 U.S.C. §§ 1325 (b)(1)(A), (b)(1)(B)
[ii] 11 U.S.C. § 1325(b).
[iii] 11 U.S.C. §§101(10A).
[iv] 11 U.S.C. § 1325 (b)(4)
[v] 11 U.S.C. §101(39A)(A).
[vi] 11 U.S.C. 1325 (b)(2)(A)(i)
[vii] *See In re Barr*, 341 B.R.181 (Bankr. M.D.N.C. 2006); *In re Alexander*, 344 B.R. 742 (Bankr. E.D.N.C. 2006) *In re Guzman*, 341 B.R. 640 (Bankr. E.D. Wis. 2006)
[viii] *Hamilton v. Lanning*, 130 S. Ct. 2464, 2469
[ix] *Id.*,. at 2478.
[x] https://www.bls.gov/opub/ted/2022/consumer-prices-up-7-5-percent-over-year-ended-january-2022.htm
[xi] See https://www.eia.gov/outlooks/steo/marketreview/crude.php , https://www.eia.gov/petroleum/gasdiesel/ , and https://www.bls.gov/opub/ted/2022/consumer-prices-up-7-5-percent-over-year-ended-january-2022.htm
[xii] *Baud v. Carol*, 634 F. 3d 327(6th Cir. 2011), *cert. den*., 132 S. Ct. 997 (U.S. Sup. Ct. 2012)
[xiii] 11 U.S.C. §1325(b)(4)
[xiv] *Baud*, at 356.
[xv] *Baud,* at 345.
[xvi] *Id.,* at 357.
[xvii] *Id.,* at 347.
[xviii] 42 U.S.C.407
[xix] *See Mort Ranta v. Gorman*, 721 F. 3d. 241, 250-53 (4th Circuit)
[xx] *See H.R. 2938 Honoring American Veterans in Extreme Need Act of 2019* also known as the *HAVEN Act.*
[xxi] *In re Gresham*, 616 B.R. 505 (Bankr. E.D. Mich. 2020)