Bankruptcy

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I. INTRODUCTION

During 1996, the United States Court of Appeals for the Eleventh Circuit decided twenty-three cases in the area of bankruptcy law. These decisions covered a wide variety of issues arising under the Bankruptcy Code, as well as several issues concerning nonbankruptcy law. This Article is a survey of the bankruptcy decisions rendered by the Eleventh Circuit in 1996.

II. MUNFORD AND THE CONSEQUENCES OF A LEVERAGED BUYOUT

A. Settlement of Potential Claims

The Eleventh Circuit issued three significant decisions in the Munford bankruptcy case. There, the debtor operated convenience and specialty stores and filed for bankruptcy shortly after being purchased through a leveraged buyout ("LBO") transaction. The first Munford decision concerned a bankruptcy court's authority to enjoin contribution and indemnification claims among nondebtor parties. The debtor commenced an adversary proceeding against various shareholders, former officers and directors, and Valuation Research Corporation ("VRC") in an attempt to recover damages resulting from the failed LBO. VRC offered to settle the claim, but only if the bankruptcy court issued an order

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enjoining the other nonsettling defendants from asserting claims for contribution and indemnification against VRC. The debtor accepted the offer, and the bankruptcy court issued the order. The other defendants appealed, but the district court affirmed.

On further appeal to the Eleventh Circuit, defendants first argued that the bankruptcy court did not have subject matter jurisdiction over their state law contribution claims that had not been asserted in the adversary proceedings. However, the Eleventh Circuit found that without the order enjoining the contribution claims, the debtor would have lost its option to settle the claim with VRC. As a result, a sufficient nexus existed between the dispute and the bankruptcy case, thereby giving the bankruptcy court subject matter jurisdiction.

In their next argument, the nonsettling defendants contended that the bankruptcy court lacked the legal authority to enjoin their claim. However, the Eleventh Circuit found the necessary legal authority in section 105(a) of the Bankruptcy Code and rule 16 of the Federal Rules of Civil Procedure. Under section 105, a bankruptcy court “may issue any order . . . that is necessary or appropriate to carry out the provisions of this title.” Under rule 16, a bankruptcy court has the authority to take any appropriate action with respect to settlements. The combination of these two provisions provided the bankruptcy court with ample authority to enter an order barring the enforcement of the contribution claims.

B. Liability for the Failed LBO

The second Munford decision involved the liability of the debtor’s corporate directors under state law for the LBO that led to Munford’s demise. The bankruptcy and district courts concluded that Georgia’s

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3. 97 F.3d at 452; see In re Munford, 172 B.R. 404 (Bankr. N.D. Ga. 1993).
4. 97 F.3d at 452.
5. Id. at 453.
6. Id. at 453-54.
7. Id. (citing Miller v. Kemira, Inc. (In re Lemco Gypsum, Inc.), 910 F.2d 784, 787-88 (11th Cir. 1990)).
8. Id. at 452.
13. 97 F.3d at 455.
15. Id. at 458.
stock distribution and repurchase statutes applied to a leveraged acquisition of a corporation. At the time of the LBO, section 14-2-91 of the Official Code of Georgia Annotated ("O.C.G.A.") provided that corporate directors may distribute to shareholders surplus capital, but no such distribution is to be made if the corporation is insolvent or would be rendered so by the distribution. In addition, O.C.G.A. section 14-2-92 prohibited directors of a corporation from authorizing the corporation to repurchase its own shares if doing so would render the corporation insolvent. Finally, under O.C.G.A. section 14-2-154, directors who acted in violation of these statutes were jointly and severally liable for the amounts involved. The directors argued that the statutes were inapplicable to an LBO because in an LBO transaction the control of the corporation changes hands. This argument did not persuade the Eleventh Circuit. The court found instead that the LBO transaction was a "paper merger" of the debtor and a shell corporation with no assets. To allow the directors to escape state law liability under these circumstances "would frustrate the restrictions imposed upon directors who authorize a corporation to distribute its assets or to repurchase its shares from stockholders when such transactions would render the corporation insolvent." Thus, the court held that an LBO was subject to Georgia's stock distribution and repurchase statutes.

In the final Munford decision, the court discussed the liability of various other parties as a result of the LBO and resulting bankruptcy. The debtor sought to recover as fraudulent transfers the payments the two largest shareholders received for their shares in the LBO. Both the bankruptcy and district courts concluded that such payments were "settlement payments," and in accordance with section 546(e) of the Bankruptcy Code, not subject to recovery by the debt-

16. Id. at 460.
18. Id. § 14-2-92(e) (codified at O.C.G.A. § 14-2-640(c) (1994)).
19. Id. § 14-2-154(a)(1) (codified at O.C.G.A. § 14-2-832(a) (1994)).
20. 97 F.3d at 459.
21. Id. at 460.
22. Id.
23. Id. It is worth pointing out that in reaching this decision, the Eleventh Circuit declined to follow a decision of the Fourth Circuit which concluded otherwise. Id. at 459-60 (citing C-T of Virginia, Inc. v. Barrett, 958 F.2d 606, 611 (4th Cir. 1992)).
25. Id. at 608.
26. Id. at 607.
Section 546(e) provides that "the [debtor-in-possession] may not avoid a transfer that is . . . a settlement payment . . . made by or to a commodity broker, forward contract merchant, stockbroker, financial institution, or securities clearing agency." The term "settlement payment" refers to various types of payments "commonly used in securities trade." Disagreeing with the lower courts, the Eleventh Circuit concluded that the payments in question were not protected under section 546(e) because the shareholders received the payments from the debtor. In order for section 546(e) to shield a transfer, the payment must be made to the shareholder from one of the entities listed in that section. As a result, the shareholders could face liability on the debtor's fraudulent transfer claim.

The next issue discussed involved the debtor's tort claims against its officers and directors for breach of fiduciary duty, negligence, mismanagement, and waste of corporate assets. Looking to Georgia law, the Eleventh Circuit stated that under the "business judgment rule," officers and directors are protected from liability "when they make good faith business decisions in an informed and deliberate manner." The undisputed evidence was that the officers and directors of Munford consulted legal and financial experts throughout the LBO process and that by doing so, they satisfied their state law duty. Therefore, the officers and directors escaped liability on the debtor's tort claim. Likewise, the financial adviser, Shearson Lehman Brothers, escaped liability when the court refused to recognize a state law claim for "aiding and abetting" a breach of fiduciary duty.

In another claim, the debtor argued that severance contracts Munford entered into with three of its top officers were fraudulent transfers because the agreements lacked consideration. Under the agreement, the officers promised to continue in Munford's employment until the

28. 98 F.3d at 609.
31. 98 F.3d at 610.
32. Id.
33. Id.
34. Id.
36. 98 F.3d at 611 (citing Cottle v. Storer Communication, Inc., 849 F.2d 570, 575 (11th Cir. 1988)).
37. Id.
38. Id. at 612-13.
39. Id. at 608.
The Eleventh Circuit found that under Georgia law, continued employment in a terminable-at-will employment situation constituted consideration. Also, had the officers terminated their employment and frustrated Munford's plan to sell its stock, the severance contract would have provided Munford with recourse against the officers.

III. CONTEMPT POWER OVER THE INTERNAL REVENUE SERVICE

A. Violation of the Automatic Stay

The liability of the Internal Revenue Service ("I.R.S.") for violating the automatic stay was the heart of the issue in Jove Engineering, Inc. v. Internal Revenue Service. After the debtor, Jove Engineering, filed a Chapter 11 bankruptcy petition, the I.R.S. made repeated attempts to force payment of prepetition taxes in violation of the automatic stay. Eventually, Jove Engineering filed a motion with the bankruptcy court to hold the I.R.S. in civil contempt. The district court found that all the violations committed by the I.R.S. were merely inadvertent, as compared to intentional and malicious, and only awarded Jove Engineering five hundred dollars for attorney fees.

Jove Engineering appealed the decision to the Eleventh Circuit, contesting the limited recovery. Specifically, the debtor claimed that section 362(h) of the Bankruptcy Code provided a source for the relief it sought. However, the Eleventh Circuit concluded that section 362(h) did not authorize an award of damages in this case. Section 362(h) grants relief to "[a]n individual injured by any willful violation" of the automatic stay. Under the plain meaning of this provision,

40. Id. at 606.
41. Id. at 612 (citing Royal Crown Cos. v. McMahon, 183 Ga. App. 543, 545, 359 S.E.2d 379, 381 (1987)).
42. Id.
43. 92 F.3d 1539 (11th Cir. 1996).
44. Id. at 1543-44. The provisions of the automatic stay are found at 11 U.S.C. § 362 (1994).
45. 92 F.3d at 1544.
46. Id. at 1545.
47. Id.
49. 92 F.3d at 1549.
50. Id.
51. 11 U.S.C. § 362(h) (emphasis added).
Jove Engineering was not entitled to relief because it was a corporation, not an individual.\textsuperscript{52}

The Eleventh Circuit then considered Jove Engineering's alternative argument that section 105 of the Bankruptcy Code\textsuperscript{53} authorized finding the I.R.S. in contempt for violating the automatic stay.\textsuperscript{54} Under section 105, a court has broad powers to issue "any" type of order that is "necessary or appropriate" to carry out the provisions of the Bankruptcy Code.\textsuperscript{55} The use of the broad term "any" led the Eleventh Circuit to conclude that section 105 included orders awarding monetary relief.\textsuperscript{56} Furthermore, the court found that an award for monetary relief was "necessary or appropriate" for certain violations of the automatic stay.\textsuperscript{57} As a result, the Eleventh Circuit concluded that section 105 allowed Jove Engineering to seek an order granting monetary relief for the I.R.S.'s repeated violations of the automatic stay.\textsuperscript{58}

The Eleventh Circuit further found that the I.R.S.'s violations were willful.\textsuperscript{59} A violation is "willful" if the I.R.S. (1) knew that the automatic stay was in place and (2) intended the actions that violated the stay.\textsuperscript{60} Under the undisputed facts of the case, the I.R.S. was notified several times of the pending bankruptcy, but it nevertheless intentionally took actions that violated the automatic stay.\textsuperscript{61} In other words, the fact that the I.R.S. did not intend to violate the automatic stay did not

\textsuperscript{52} 92 F.3d at 1550. This conclusion is in accord with decisions by the Second and Ninth Circuits. See Johnston Envtl. Corp. v. Knight (\textit{In re} Goodman), 991 F.2d 613, 619 (9th Cir. 1993); Maritime Asbestosis Legal Clinic v. LTV Steel Co. (\textit{In re} Chateaugay Corp.), 920 F.2d 183 (2d Cir. 1990). The Third and Fourth Circuits have ruled to the contrary. See Cuffee v. Atlantic Business and Community Dev. Corp. (\textit{In re} Atlantic Business & Community Corp.), 901 F.2d 325, 329 (3d Cir. 1990); Budget Serv. Co. v. Better Homes of Va., Inc., 804 F.2d 289, 292 (4th Cir. 1986).

\textsuperscript{53} 11 U.S.C. § 105.

\textsuperscript{54} 92 F.3d at 1553.

\textsuperscript{55} 11 U.S.C. § 105(a).

\textsuperscript{56} 92 F.3d at 1554.

\textsuperscript{57} Id.

\textsuperscript{58} Id. This conclusion is interesting because, according to this view, any party, including a corporation, may be entitled to seek damages for a violation of the automatic stay under section 105. Thus, the intent of Congress, as the Eleventh Circuit found to exist in section 362(h), that only \textit{individuals} be entitled to such relief is rendered a virtual nullity. Perhaps the only distinction that remains is that the provisions authorizing damages under section 362(h) are mandatory while the provisions of section 105 are merely permissive.

\textsuperscript{59} 92 F.3d at 1555.

\textsuperscript{60} Id.

\textsuperscript{61} Id. at 1555-56.
relieve it of liability, because it intended to take the actions which resulted in a violation.\textsuperscript{63}

Finally, the Eleventh Circuit determined that, as a result of its violation of the automatic stay, the I.R.S. could be subject to civil contempt but that only coercive, not punitive, sanctions could be imposed.\textsuperscript{63} Sanctions are coercive "if they serve the complainant rather than vindicate some public interest."\textsuperscript{64} However, Jove Engineering sought "severe monetary damages in the form of a fixed non-compensatory fine," which the court found to be punitive in nature and thus not allowable.\textsuperscript{65} Nevertheless, the Eleventh Circuit concluded that Jove Engineering could be entitled to attorney fees and remanded the case to the district court for further consideration.\textsuperscript{66}

\textbf{B. Violation of the Discharge Injunction}

In \textit{Hardy v. United States (In re Hardy)},\textsuperscript{67} the Internal Revenue Service again found itself in hot water, this time for violating the discharge injunction of section 524 of the Bankruptcy Code.\textsuperscript{68} The debtor, Pierce Lamar Hardy, reopened his Chapter 13 bankruptcy case in 1993 and filed an adversary proceeding against the government, claiming that the I.R.S. violated the discharge injunction of section 524 by trying to collect discharged tax debts.\textsuperscript{69} The lower courts dismissed the proceeding for lack of subject matter jurisdiction after concluding that the doctrine of sovereign immunity barred the imposition of

\textsuperscript{62} Interestingly, the I.R.S. tried to excuse its repeated violations of the stay by blaming its computer system. The Eleventh Circuit was not persuaded by such an argument, stating that the I.R.S. could not shift the burden of a faulty or inadequate computer system to the debtor. \textit{Id.} at 1556. Furthermore, the Eleventh Circuit found inadequate a letter from the I.R.S. to Jove Engineering stating that it may "inadvertently" levy and seize property in violation of the automatic stay and that the debtor should report such actions to the I.R.S. instead of filing a motion for contempt in the bankruptcy court. \textit{Id.} at 1557. The court stated that such an "attempt to burden debtors with policing [the] I.R.S.'s misconduct is in complete derogation of the law" that each party is responsible for ensuring its compliance with a court order. \textit{Id.}

\textsuperscript{63} \textit{Id.} at 1557-60.
\textsuperscript{64} \textit{Id.} at 1558.
\textsuperscript{65} \textit{Id.} at 1559.
\textsuperscript{66} \textit{Id.} at 1559-60.
\textsuperscript{67} 97 F.3d 1384 (11th Cir. 1996).
\textsuperscript{68} 11 U.S.C. § 524. This provision states in pertinent part that a discharge in bankruptcy "operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover, or offset any such debt as a personal liability of the debtor." \textit{Id.}
\textsuperscript{69} 97 F.3d at 1387.
monetary damages against the government.\textsuperscript{70} Hardy appealed further to the Eleventh Circuit.\textsuperscript{71} During the pendency of the appeal, President Clinton signed into law the Bankruptcy Reform Act of 1994,\textsuperscript{72} which amended section 106 of the Bankruptcy Code, the provision discussing sovereign immunity in bankruptcy.\textsuperscript{73} Thereafter, section 106, as amended, specifically abrogated the government's sovereign immunity for claims arising under section 524 of the Bankruptcy Code.\textsuperscript{74}

When the Eleventh Circuit issued its decision, it concluded that by virtue of the 1994 amendments, sovereign immunity had been waived with respect to Hardy's claim, which gave the lower courts subject matter jurisdiction.\textsuperscript{75} However, Hardy had to demonstrate that a source outside of section 106 entitled him to the monetary relief sought.\textsuperscript{76} The Eleventh Circuit noted that the trend among courts was to find that bankruptcy courts had the inherent contempt power under section 524 to grant the necessary relief for violations of the discharge injunction.\textsuperscript{77} Nevertheless, instead of finding such inherent power, the Eleventh Circuit decided to exercise caution and rely on the statutory contempt powers of section 105.\textsuperscript{78} Relying on its recent decision in \textit{Jove Engineering, Inc. v. Internal Revenue Service},\textsuperscript{79} the court in \textit{Hardy} concluded that section 105 granted bankruptcy courts the power to award monetary damages for violations of the discharge injunction of section 524.\textsuperscript{80}

\section*{IV. CHAPTER 13 ELIGIBILITY}

The Eleventh Circuit issued a significant decision on the question of determining Chapter 13 eligibility in \textit{United States v. Verdunn}.\textsuperscript{81} The

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\bibitem{71} 97 F.3d at 1387.
\bibitem{73} \textit{Id.}
\bibitem{74} 97 F.3d at 1387-88. After the 1994 amendment, section 106 contained a subsection expressly abrogating sovereign immunity as to a governmental unit for sixty specific sections of the Bankruptcy Code, including sections 106 and 362. 11 U.S.C. § 106(a)(1) (1994).
\bibitem{75} 97 F.3d at 1388.
\bibitem{76} \textit{Id.}
\bibitem{77} \textit{Id.} at 1389.
\bibitem{78} \textit{Id.} (citing Chambers v. NASCO, Inc., 501 U.S. 32, 44-45 (1991) (warning that courts must exercise caution in invoking inherent powers)).
\bibitem{79} 92 F.3d 1539 (11th Cir. 1996). For further discussion of \textit{Jove}, see \textit{supra} notes 43-66 and accompanying text.
\bibitem{80} 97 F.3d at 1389-90.
\bibitem{81} 89 F.3d 799 (11th Cir. 1996).
\end{thebibliography}
I.R.S. issued Thomas Verdunn a notice of tax deficiency of $297,000 for the years from 1982 to 1986. The notice of deficiency specified the amount of the tax liability based on criteria established by the Internal Revenue Code. Verdunn challenged the deficiency determination in Tax Court, but he filed a Chapter 13 bankruptcy petition shortly before the Tax Court was to conduct a trial on the matter.

The I.R.S. filed a proof of claim in Verdunn's case for $297,000 in unsecured debt and then objected to confirmation of Verdunn's plan, contending that he was not entitled to Chapter 13 eligibility. Under section 109(e) of the Bankruptcy Code, "[o]nly an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than $100,000" is eligible for Chapter 13 relief. Because Verdunn disputed the character and nature of his tax liability, the bankruptcy court concluded that the I.R.S.'s claim was not "liquidated" for purposes of section 109(e). The district court affirmed, also holding that because Verdunn "vigorously disputed" his tax liability, the debt was not "readily ascertainable" and, as such, not liquidated.

The I.R.S. further appealed its case to the Eleventh Circuit, which focused its discussion on whether the tax claim was a liquidated one. The court defined a liquidated debt as one where it is certain what is due and how much is due. A liquidated debt is that which has been made certain as to amount due by agreement of the parties or by operation of law. Therefore, the concept of a liquidated debt relates to the amount of liability, not the existence of liability.

Verdunn argued that the amount of the debt was not readily ascertainable by the deficiency notice. He also contended that the fraud

82. Id. at 800.
83. Id. at 803. The deficiency determinations are based on criteria found at 26 U.S.C. § 6211(a).
84. 89 F.3d at 800.
85. Id.
87. 89 F.3d at 801.
88. Id. at 801-02; see also United States v. Verdunn, 187 B.R. 996 (M.D. Fla. 1995).
89. 89 F.3d at 802.
90. Id. (footnote and citations omitted) (citing BLACK'S LAW DICTIONARY 930 (6th ed. 1990) and In re McGovern, 122 B.R. 712, 715 (Bankr. N.D. Ind. 1989)).
91. Id. at 801.
allegations were disputed and that an extensive evidentiary hearing in the Tax Court was necessary to determine the liability. In contrast, the I.R.S. argued the debt was liquidated because the notice of deficiency provided the necessary information to compute the tax liability in accordance with tax law. In support of its argument, the I.R.S. cited the Seventh Circuit's decision in *In re Knight*. In that case, the debtor was a town court judge required under state law to report traffic convictions to the state bureau of motor vehicles. Under state law, the failure to report a conviction resulted in a fine of one hundred dollars. The debtor failed to report 915 convictions, resulting in a liability of $91,500. In bankruptcy, the debtor argued that this debt was not liquidated because he disputed his liability. The Seventh Circuit disagreed and found that the debt was liquidated because the amount was fixed in a demand letter sent by the state to the debtor and could be calculated under the relevant state statute.

The Eleventh Circuit found the I.R.S.'s argument persuasive, particularly its reliance on *Knight*; in fact, the court concluded that Verdunn was indistinguishable from *Knight*. Internal Revenue Code standards were used to calculate Verdunn's tax liability. The amount of the liability was evident from the statutory notice of deficiency. As in *Knight*, the debt was readily ascertainable and therefore liquidated for purposes of section 109(e). Also, the debtor's dispute of the claim did not render the debt unliquidated. Therefore, Verdunn was not eligible for Chapter 13 relief.

V. THE AUTOMATIC STAY

In *United States v. Ruff (In re Rush-Hampton Industries)*, the Eleventh Circuit essentially ruled "no harm, no foul" in finding that the

92. Id. at 802.
93. Id.
94. 55 F.3d 231 (7th Cir. 1995).
95. Id. at 232.
96. Id.
97. Id. at 233.
98. Id.
99. Id. at 235.
100. 89 F.3d at 803.
101. Id.
102. Id.
103. Id.
104. Id. at 802 n.9 (citing *In re Knight*, 55 F.3d 231, 234 (7th Cir. 1995); *In re Jordan*, 186 B.R. 201, 202 (Bankr. D. Me. 1994); *Vaughan v. Central Bank of the South (In re Vaughan)*, 36 B.R. 935, 938 (N.D. Ala.), aff'd, 741 F.2d 1383 (11th Cir. 1984)).
105. 98 F.3d 614 (11th Cir. 1996).
Internal Revenue Service was entitled to postpetition interest despite its violation of the automatic stay. The I.R.S. filed a claim in the debtor's bankruptcy case for unpaid 1978 taxes plus interest. Later, the I.R.S. determined that the debtor had overpaid its 1979 taxes, and it set off the claim for the 1978 taxes against the 1979 overpayment without seeking relief from the automatic stay. The bankruptcy court held that the I.R.S. violated the automatic stay, but nevertheless allowed the 1979 overpayment to cover the 1978 taxes. However, the bankruptcy court decided to penalize the I.R.S. for the violation by denying it the right to receive postpetition interest on its claim, and the district court affirmed.

The Eleventh Circuit agreed with the lower courts that the I.R.S. should have first obtained relief from the automatic stay before exercising its right of setoff. But even though a violation of the automatic stay would require damages if a debtor is injured, the Eleventh Circuit found no authority for the bankruptcy court to deny the I.R.S.'s right to postpetition interest in lieu of damages, particularly because the trustee in the case did not seek damages. In short, the Eleventh Circuit found that under the "narrow" circumstances of the case, the conduct of the I.R.S. was a mere "harmless violation of the automatic stay" that did not justify the sanction that the bankruptcy court imposed.

VI. REJECTION OF EXECUTORY CONTRACTS

A creditor challenged a debtor's ability to reject a homesite purchase contract in Sipes v. Atlantic Gulf Communities Corp. (In re General Development Corp.). Both the bankruptcy and district courts concluded that the contract was executory for the purpose of section 365(a) of the Bankruptcy Code, thus allowing the debtor to reject...
The creditor appealed further to the Eleventh Circuit, which affirmed by adopting the opinion of the district court.

The Sipes and General Development Corporation entered into an agreement for the sale of a homesite in Florida. In 1990, General Development entered Chapter 11 bankruptcy. Once in bankruptcy, General Development rejected its homesite purchase contract with the Sipes. The Sipes, however, argued that the homesite purchase agreement was not an executory contract that could be rejected in bankruptcy. Section 365(a) of the Bankruptcy Code allows a Chapter 11 debtor to “assume or reject any executory contract or unexpired lease of the debtor.” Unfortunately, the Bankruptcy Code does not provide a definition for the term “executory contract.” The Sipes argued that a contract was executory if “there remained mutual obligations due and owing from the parties.” Under this definition, the homesite purchase agreement would not be executory because the Sipes had fulfilled all their obligations.

The court, however, did not agree with the Sipes’ definition. Instead, it followed a “functional approach” by which a contract is executory if the rejection would ultimately benefit the bankruptcy estate and creditors. Under this view, the contract would be executory if only the debtor had outstanding obligations under it, and the obligations were a burden to the debtor. This was the case with General Development. The homesite purchase agreement obligated it to improve and deed developed homesites, and its ability to reject these obligations because it did not have the financial ability to perform them was critical to the reorganization. Therefore, General Development’s rejection of the homesite purchase agreement was proper, and the Sipes no longer had an enforceable interest under the agreement.

117. 84 F.3d at 1365, affg 177 B.R. 1000, 1002 (S.D. Fla. 1995).
118. 84 F.3d at 1365.
119. Id. at 1366.
121. 84 F.3d at 1374.
122. Id.
123. Id. at 1375 (citing Arrow Air v. Port Auth. (In re Arrow Air, Inc.), 60 B.R. 117, 121-22 (Bankr. S.D. Fla. 1986)).
124. Id. at 1374.
125. Id. at 1375.
VII. PRIORITY OF CLAIMS

In the Chapter 7 case of Internal Revenue Service v. Davis (In re Davis), the Eleventh Circuit decided that an I.R.S. claim for taxes under section 507(a)(7) of the Bankruptcy Code should be paid as a priority claim under section 726(a)(1) even though the I.R.S. did not file the claim within the time required under Bankruptcy Rule 3002-c. The bankruptcy court had held that the tax claim could only be paid as an unsecured claim under section 726(a)(3) because of its untimeliness. The district court held otherwise, concluding that timeliness provisions of Bankruptcy Rule 3002(c) do not apply to distributions under section 726(a)(1). Noting that the statutory language of section 726(a)(1) makes no distinction between late and timely claims, the Eleventh Circuit agreed with the district court's application of the law and affirmed.

VIII. EXEMPTIONS

A. Georgia Homestead Exemption

The Eleventh Circuit discussed a debtor's ability to avoid a lien on exempt property in Holloway v. John Hancock Mutual Life Insurance Co. (In re Holloway). When Linda and Eldridge Holloway filed for bankruptcy, they included with their petition a list of exempt property.
Included on that list was their residence, but the Holloways listed the value of the exemption as zero.135 Once in bankruptcy, the Holloways filed a motion to avoid a lien on their residence pursuant to section 522(f) of the Bankruptcy Code,136 the lien being the result of a judgment obtained by John Hancock Mutual Life Insurance Company.137 The specific issue before the Eleventh Circuit was whether a debtor needed to have equity in the property to claim an exemption and avoid the lien. As already noted, the Holloways listed the value of their exemption as zero, and they had no equity in the property because it was subject to two security deeds and a tax lien in addition to the judgment lien.138 Section 522(f) of the bankruptcy Code allows avoidance of a judgment lien “on an interest of the debtor in property to the extent that such lien impairs an exemption.”139 According to the Eleventh Circuit, the outcome of the case turned on the definition of the phrase “impairs an exemption.”140 The court noted divergent lines of cases. One line concludes that, under the plain language of the statute, section 522(f) allows avoidance of a judicial lien only to the extent it impairs the exemption.141 Thus, if the claimed exemption was invalid, the debtor could not avoid the judgment lien. The contrary line of cases concludes that liens are avoidable even if the debtor can claim no equity in the property.142 The court in Holloway noted, however, that it was bound to follow the decision of the Eleventh Circuit in the case of Wrenn v. American Cast Iron Pipe Co. (In re Wrenn),143 whereby the court held that under the plain language of section 522(f), a debtor can avoid a lien only to the extent it impairs the exemption, irrespective of the debtor’s equity interest in the property.144 In view of Wrenn, the court concluded that the Holloways could avoid John Hancock’s lien only to the extent it impaired their homestead exemption.145 Because the Holloways

135. 81 F.3d at 1064.

136. 11 U.S.C. § 522(f) (1994). This Code section provides in relevant part that “the debtor may avoid the fixing of a lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled under subsection (b) of this section, if such lien is ... a judicial lien.” 11 U.S.C. § 522(f)(1)(A).

137. 81 F.3d at 1065.

138. Id. at 1064.


140. 81 F.3d at 1068.

141. Id. at 1068 (citing Riddell v. N.C.R. Universal Credit Union (In re Riddell), 96 B.R. 816 (Bankr. S.D. Ohio 1989)).

142. Id. at 1068-69. See, e.g., In re Magosin, 75 B.R. 545 (Bankr. E.D. Pa. 1987).

143. 40 F.3d 1162 (11th Cir. 1994).


145. 81 F.3d at 1069.
valued their exemption at zero, John Hancock's lien could not be avoided.\textsuperscript{146}

\textbf{B. Florida Homestead Exemption}

Yet another homestead exemption claim was at issue when the Eleventh Circuit decided \textit{Englander v. Mills (In re Englander)}\textsuperscript{147}. Upon filing bankruptcy, the debtors claimed a homestead exemption in 1.05 acres of lakefront property within a municipality.\textsuperscript{148} Under the Florida constitution, however, a debtor is entitled to a homestead exemption only to one-half acre of land if located within a municipality.\textsuperscript{149} The trustee and creditors objected to the claimed exemption because it exceeded this size limitation.\textsuperscript{150} In response to the objection, the debtors clarified their exemption by designating a portion of their property as nonexempt and subject to sale for the benefit of creditors.\textsuperscript{151} However, this nonexempt portion had no access to roads, utilities, or lake frontage, and it was completely surrounded by property claimed as exempt.\textsuperscript{152} The bankruptcy court concluded that the debtors' "gerrymandering" of their homestead exemption was in bad faith and denied the exemption.\textsuperscript{153} As a result, the bankruptcy court ordered the whole property sold and allocated the proceeds to satisfy the debtors' right to a homestead exemption.\textsuperscript{154} The district court affirmed.\textsuperscript{155} Because the debtors' property was indivisible, thereby making a sale of the nonexempt portion impossible, the Eleventh Circuit found the equitable solution to be a sale of the property and to apportion the proceeds as an "appropriate recognition of the debtors' homestead exemption."\textsuperscript{156} Therefore, the Eleventh Circuit affirmed.\textsuperscript{157}

\textbf{C. Florida Annuities Exemption}

Whether a settlement agreement was an annuity contract for the purposes of an exemption under Florida law was the issue in \textit{Guardian

\begin{thebibliography}{99}
\bibitem{146} Id.
\bibitem{147} 95 F.3d 1028 (11th Cir. 1996).
\bibitem{148} Id. at 1029.
\bibitem{149} Fla. Const. art. X, § 4(a)(1).
\bibitem{150} 95 F.3d at 1029.
\bibitem{151} Id. at 1029-30.
\bibitem{152} Id. at 1030.
\bibitem{153} Id. (citing In re Englander, 156 B.R. 862, 864 (Bankr. M.D. Fla. 1992)).
\bibitem{154} 95 F.3d at 1030.
\bibitem{155} Id.
\bibitem{156} Id. at 1032.
\bibitem{157} Id.
\end{thebibliography}
Life Insurance Co. v. Solomon (In re Solomon). The debtor, Fred Solomon, settled a claim in 1985 against Union Mutual Life Insurance Company. Under the settlement agreement, Union Mutual was to pay Solomon $50,000, followed by monthly payments of $6,507.97 for ten years, and finally a lump-sum payment of $450,000. When Solomon filed a Chapter 7 bankruptcy petition in 1993, he listed the settlement proceeds as exempt property, claiming that the settlement agreement was an annuity contract. Under Florida law, proceeds of annuity contracts are exempt. Before the Eleventh Circuit, Guardian Life argued that the settlement agreement between Solomon and Union Mutual was not exempt because it was not an annuity contract and that neither party intended it to be one. In contrast, Solomon argued for a broad definition of "annuity contracts" that would encompass the settlement agreement in question.

The Eleventh Circuit, agreeing with Guardian Life, concluded that the settlement agreement was not an annuity contract under Florida law. Specifically, the court in Solomon read Florida case law "to require the existence of an actual annuity contract before a series of payments may be exempt." Solomon's receipt of a series of payments from Union Mutual did not in itself create an annuity contract. Instead, the court noted that "[t]o qualify for the exemption, the parties to the agreement must have intended to create an annuity contract." Nothing in the settlement agreement between Solomon and Union Mutual revealed that they intended the settlement to create an annuity contract. Thus, the Eleventh Circuit concluded that Solomon was not entitled to the exemption.

158. 95 F.3d 1076 (11th Cir. 1996).
159. Id. at 1077.
160. Id.
161. Id.
162. Id. See FLA. STAT. ANN. § 222.14 (West 1993).
163. 95 F.3d at 1078.
164. Id.
165. Id.
166. Id. (emphasis in original).
167. Id. at 1079.
169. 95 F.3d at 1079.
170. Id.
A. **Debts for Fraud**

A debtor who did not directly obtain the benefit of his fraudulent conduct nevertheless found his debt for fraud excepted from discharge in *HSSM #7 Ltd. Partnership v. Bilzerian (In re Bilzerian).*171 HSSM obtained a judgment in a federal district court in Texas against Paul Bilzerian and his corporation, Bicoastal Financial Corporation, after a jury found that Bilzerian fraudulently induced HSSM to invest monies in Bicoastal.172 After Bilzerian filed for bankruptcy, HSSM commenced an adversary proceeding, objecting under section 523(a)(2)(A) of the Bankruptcy Code173 to the discharge of this judgment debt.174 Under section 523(a)(2)(A), a bankruptcy discharge “does not discharge an individual debtor from any debt . . . for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by false pretenses, a false representation, or actual fraud.”175

On motions for summary judgment, the bankruptcy court ruled in favor of Bilzerian and found that Bicoastal Financial Corporation, not Bilzerian, directly received the benefit of the fraudulent conduct.176 However, the district court reversed, concluding that Bilzerian received some benefit, at least indirectly, from the fraud.177 The district court further concluded that under the principles of collateral estoppel, the Texas judgment established the necessary elements of fraud, thereby resulting in the debt in question being excepted from discharge pursuant to section 523(a)(2)(A).178

On Bilzerian’s appeal, the Eleventh Circuit considered the issue of whether a debtor must receive a benefit from fraud in order for a debt to be subject to the discharge exception of section 523(a)(2)(A).179 As to this question, three views have emerged. The first view, and the one adopted by the bankruptcy court, is that the debtor must personally
receive the money that was obtained by fraud.\textsuperscript{180} The second view, called the “receipt of benefits theory” and adopted by the district court, is that the debtor need only derive some benefit from the fraud.\textsuperscript{181} The third and most liberal view is that the debtor need only obtain money by fraudulent means, but the debtor need not personally receive the money or any benefit therefrom.\textsuperscript{182}

Although lower court opinions on this issue were varied, the Eleventh Circuit noted that the Fifth, Sixth, and Ninth Circuits had adopted the receipt of benefits theory.\textsuperscript{183} Most analogous was the Ninth Circuit case of \textit{In re Ashley}, which involved a debtor who fraudulently induced a creditor to loan money to his corporation.\textsuperscript{184} The Ninth Circuit found that the debtor was in a position to benefit from the infusion of capital to his corporation, resulting in the debt being excepted from discharge.\textsuperscript{185}

The Eleventh Circuit found the reasoning of Ashley persuasive and concluded that Bilzerian, by fraudulently inducing HSSM to invest in his corporation, was in a position to receive a benefit from his fraud.\textsuperscript{186} As a result of the benefit he received, Bilzerian’s debt to HSSM was excepted from discharge even though he did not personally receive the money from HSSM.\textsuperscript{187} The Eleventh Circuit then concluded that Bilzerian was precluded from contesting the fraud finding of the Texas court under principles of collateral estoppel.\textsuperscript{188} Thus, the debt to HSSM was excepted from Bilzerian’s bankruptcy discharge.\textsuperscript{189}

The issue before the Eleventh Circuit in \textit{Fuller v. Johannessen (In re Johannessen)} was whether the allegations in the complaint were sufficient to state a claim for fraud, thereby excepting the fraudulently acquired debt from discharge.\textsuperscript{190} The creditors in that case settled a claim against the debtor arising from the construction of a house.\textsuperscript{191} After reaching the settlement, however, the debtor filed for Chapter 7

\textsuperscript{180} \textit{Id.} at 890.
\textsuperscript{181} \textit{Id.}
\textsuperscript{182} \textit{Id.}
\textsuperscript{183} \textit{Id.} See BancBoston Mortgage Corp. v. Ledford (\textit{In re Ledford}), 970 F.2d 1556 (6th Cir. 1992), \textit{cert. denied}, 507 U.S. 916 (1993); Luce v. First Equip. Leasing Corp. (\textit{In re Luce}), 960 F.2d 1277 (5th Cir. 1992); Ashley v. Church (\textit{In re Ashley}), 903 F.2d 599 (9th Cir. 1990).
\textsuperscript{184} Ashley, 903 F.2d at 602.
\textsuperscript{185} \textit{Id.} at 604.
\textsuperscript{186} 100 F.3d at 891.
\textsuperscript{187} \textit{Id.}
\textsuperscript{188} \textit{Id.} at 892.
\textsuperscript{189} \textit{Id.}
\textsuperscript{190} 76 F.3d 347 (11th Cir. 1996).
\textsuperscript{191} \textit{Id.} at 348.
bankruptcy. The creditors filed a complaint to determine the dischargeability of the debt, claiming that the debt arising from the settlement was excepted from discharge for fraud under section 523(a)(2)(A). On the debtor's motion to dismiss, the bankruptcy court dismissed the complaint with prejudice, and the district court affirmed.

On further appeal, the Eleventh Circuit stated the rule that "a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." Also, under the Federal Rules, a plaintiff need only set forth a short and plain statement of his claim to give the defendant fair notice of what the claim is. Additionally, on a motion to dismiss, a court is required to accept as true the allegations contained in the complaint.

The court in Johannessen found a statement in the creditors' complaint alleging that the debtor made misrepresentations about the monies that were being delivered to him. Next, the creditors alleged that they relied on the misrepresentations and that their reliance was justified under the circumstances. Finally, the creditors claimed monetary damages as a result of the misrepresentations. These allegations were sufficient to state a claim for fraud under section 523(a)(2)(A). Thus, the Eleventh Circuit reversed the lower courts and remanded the case to proceed on the merits.

192. Id.
193. Id. at 349. Under section 523(a)(2)(A), a bankruptcy discharge does not discharge a debtor from any debt to the extent obtained by "false pretenses, a false representation, or actual fraud." 11 U.S.C. § 523(a)(2)(A).
194. See FED. R. CIV. P. 12(b)(6) (applicable to bankruptcy under FED. R. BANKR. P. 7012).
195. 76 F.3d at 348. See also Fuller v. Johannessen, 180 B.R. 682 (M.D. Fla. 1995).
196. 76 F.3d at 349 (quoting Conley v. Gibson, 355 U.S. 41, 45-46 (1957)).
197. Id. at 349-50. See Conley, 355 U.S. at 47.
198. Id. at 350.
199. Id.
200. Id.
201. Id.
202. Id.
203. Id. Perhaps anticipating a defense to be asserted by the debtor, the Eleventh Circuit further noted that the fact that the debt in question was the result of a settlement agreement did not prevent it from being a debt for fraud. Id. See Greenberg v. Schools, 711 F.2d 152, 156 (11th Cir. 1983).
B. Debts for Alimony, Maintenance, or Support

The Eleventh Circuit considered the dischargeability of attorney fees in a child support dispute in Strickland v. Shannon (In re Strickland). Kenneth Strickland petitioned a Florida court to modify a child support order. The state court denied the petition and ordered Kenneth to pay $9430.50 in attorney fees and costs to his former wife, Lauren. After filing a Chapter 7 bankruptcy petition, Kenneth commenced an adversary proceeding to determine whether the debt for attorney fees and costs were excepted from his discharge under section 523(a)(5) of the Bankruptcy Code. The bankruptcy court ruled as a matter of law that a debt for attorney fees in a postdivorce child custody dispute is discharged in bankruptcy. The district court reversed, however, and Kenneth appealed further.

The Eleventh Circuit stated that the issue of whether a debt was in the nature of alimony, maintenance, or support was a matter of federal law and not state law. Nevertheless, state law can provide guidance in making the determination. Under Florida law, a former spouse's relative need and ability to pay serves as the basis for awarding attorney fees in a modification action. Therefore, in this case, the state court necessarily determined that the award of attorney fees was necessary for Lauren's support. Kenneth argued that the decision of whether the award was actually support should be made by the bankruptcy court and that the bankruptcy court should consider the former spouse's financial status in making that decision. The Eleventh Circuit disagreed, stating that expanding the discharge provision of section 523(a)(5) "into an assessment of the ongoing financial circumstances" of a former spouse "would of necessity embroil federal courts in domestic relations

204. 90 F.3d 444 (11th Cir. 1996).
205. 90 F.3d at 446.
206. Id.
207. Id. (citing 11 U.S.C. § 523(a)(5) (1994) (debt to a former spouse is not discharged in bankruptcy to the extent that "such debt . . . is actually in the nature of alimony, maintenance, or support").
209. 90 F.3d at 446.
210. Id. (citing Harrell v. Sharp (In re Harrell), 754 F.2d 902, 904-05 (11th Cir. 1985)).
211. Id. (citing Jones v. Jones (In re Jones), 9 F.3d 878, 880 (10th Cir. 1993)).
212. Id. at 446-47 (citing FLA. STAT. ANN. § 61.16(1) (1993)).
213. Id. at 447.
214. Id. (citing Adams v. Zentz, 963 F.2d 197, 200 (8th Cir. 1992)). The court in Strickland refused to follow this reasoning, noting that section 523(a)(5) "requires noting more than 'a simple inquiry as to whether the obligation can legitimately be characterized as support.'" 90 F.3d at 447 (quoting Harrell, 754 F.2d at 906).
matters which should properly be reserved to the state courts.\textsuperscript{19} For these reasons, the court in \textit{Strickland} concluded that the debt was excepted from the debtor's discharge.\textsuperscript{20}

X. SECURITY INTEREST IN POSTPETITION HOTEL REVENUE

The debtor in \textit{Financial Security Assurance, Inc. v. Tollman-Hundley Dalton, L.P.}\textsuperscript{21} owned a hotel. The case involved a security agreement by which the debtor, Tollman-Hundley, granted the creditor, Financial Security, a security interest in its hotel and all rents and profits associated therewith. After default, Financial Security accelerated the payments due under the loan, and Tollman-Hundley filed a Chapter 11 bankruptcy petition. Tollman-Hundley operated the hotel postpetition for thirteen months until Financial Security obtained relief from the automatic stay to foreclose. During that time, the hotel generated more than $4,000,000 in revenues, but after paying postpetition operating expenses, only $400,000 remained. Financial Security attempted to gain access to the funds, arguing that they were covered by the parties' security agreement. Tollman-Hundley sought an order authorizing it to use the excess money to fund a liquidation plan,\textsuperscript{22} thus setting up the dispute to be settled by the courts.

According to section 552(a) of the Bankruptcy Code, property generally acquired postpetition by the debtor is not subject to a prepetition security interest.\textsuperscript{23} Nevertheless, exceptions exist in section 552(b): A security interest will remain in postpetition "proceeds, product, offspring, rents, or profits"\textsuperscript{24} derived from prepetition property "to the extent provided by such security agreement and by applicable nonbankruptcy law."\textsuperscript{25} In addressing the contentions of the parties, the bankruptcy court looked to the Supreme Court's decision in \textit{Butner v. United States}\textsuperscript{26} and concluded that state law defined the terms "proceeds, products, offspring, rents, or profits."\textsuperscript{27} The bankruptcy court then reviewed Georgia law and determined that hotel revenues did not fall within these definitions.\textsuperscript{28} Accordingly, the bankruptcy court

\textsuperscript{19} 90 F.3d at 447 (quoting \textit{Harrell}, 754 F.2d at 907).
\textsuperscript{20} Id.
\textsuperscript{21} 74 F.3d 1120 (11th Cir. 1996) (per curiam).
\textsuperscript{22} Id. at 1121-22.
\textsuperscript{23} Id. at 1122 (citing 11 U.S.C. § 552(a) (1994)).
\textsuperscript{24} Id. (citing 11 U.S.C. § 552(b)(1)).
\textsuperscript{25} 11 U.S.C. § 552(b)(1).
\textsuperscript{26} 440 U.S. 48 (1979).
\textsuperscript{27} Id. at 54.
concluded that the excess $400,000 was not covered by section 552(b), and the district court affirmed.\textsuperscript{225}

Undeterred, Financial Security appealed to the Eleventh Circuit and succeeded in obtaining a reversal.\textsuperscript{226} The Eleventh Circuit first concluded that the lower courts had erred in using state law to define the terms “proceeds, products, offspring, rents, or profits.”\textsuperscript{227} The court found that the lower courts’ reliance on \textit{Butner} was misplaced in that \textit{Butner} authorized reference to state law to determine only whether Financial Security’s security interest extended to hotel revenues.\textsuperscript{228} However, the question presented by the case was not whether the hotel revenues were covered by the security interest because the parties already had agreed that they were.\textsuperscript{229} Instead, the question was whether hotel revenues fell within the meaning of section 552(b).\textsuperscript{230}

According to the Eleventh Circuit, this issue was simply a matter of interpreting the meaning of a federal statute.\textsuperscript{231} Quite interestingly, the ultimate source for interpreting federal law in this case was \textit{Black’s Law Dictionary}, which defines the term “rent” as “consideration paid for use or occupation of property” and “in a broader sense, . . . the compensation or fee paid, usually periodically, for the use of any rental property, land, buildings, equipment, etc.”\textsuperscript{232} Virtually adopting \textit{Black’s Law Dictionary} as defining rent as used in section 552(b), the Eleventh Circuit concluded that the hotel revenues at issue came within the scope of that section.\textsuperscript{233} Thus, Financial Security retained its security interest in the postpetition hotel revenues generated by Tollman-Hundley.

The Eleventh Circuit sought to bolster its ruling by pointing out that the 1994 amendments to the Bankruptcy Code changed section 552(b) to explicitly include hotel revenues within its scope.\textsuperscript{234} Nevertheless, it is interesting to note that the Eleventh Circuit’s decision was contrary to the decisions of other circuits that had held that state law was

\begin{flushright}
\textsuperscript{225} Id. (citing \textit{Financial Sec. Assurance}, 165 B.R. at 702).
\textsuperscript{226} Id. at 1125.
\textsuperscript{227} Id. at 1123.
\textsuperscript{228} Id.
\textsuperscript{229} Id.
\textsuperscript{230} Id. at 1123-24.
\textsuperscript{231} Id. at 1124.
\textsuperscript{232} Id. (quoting \textit{BLACK’S LAW DICTIONARY} 1297 (6th ed. 1990)).
\textsuperscript{233} Id.
\end{flushright}
determinative of the meaning of pre-1994 section 552(b).\textsuperscript{235} Because section 552(b) has been amended, however, such a conflict should not be significant for future cases.

XI. TRUSTEE AND PROFESSIONAL COMPENSATION

The Eleventh Circuit in United States Trustee v. Fishback (In re Glados, Inc.)\textsuperscript{236} limited the rights of trustees and professionals to obtain interest on their fee awards.\textsuperscript{237} Lawrence Kleinfeld was appointed Chapter 7 trustee for the debtor, Glados, Inc., in 1985. The only assets available in the case were two causes of action, and the trustee employed the law firm of Kleinfeld & Fishback as trustee's counsel to assist him in pursuing these claims. After several years of litigation, the trustee succeeded in obtaining proceeds for the bankruptcy estate sufficient to pay in full all creditors with a surplus remaining.\textsuperscript{238} When the trustee and trustee's counsel filed their fee applications, they requested interest on their fee claims under section 726(a)(5) of the Bankruptcy Code, which authorizes interest on claims when a surplus exists.\textsuperscript{239} Over the objection of the United States Trustee, the bankruptcy court awarded interest on the fees.\textsuperscript{240}

The Eleventh Circuit framed the issues as (1) whether, under section 726(a)(5), the trustee may receive interest from the date of his appointment and (2) whether a professional, such as counsel for the trustee, may receive interest from the date of the fee application.\textsuperscript{241} The statutory provisions involved, however, created a dilemma. Specifically, section 726(a)(5) provides that interest on the claim is to be paid "at the legal rate from the date of the filing of the petition."\textsuperscript{242} Although professional fees are paid in accordance with section 726, these fees are awarded under section 330 during the bankruptcy case.\textsuperscript{243} In other words, even though interest is to accrue on a claim from the date of the petition, a claim for fees does not exist until the fee award, which is

\begin{footnotesize}
235. Id. at 1124 n.9 (citing Financial Sec. Assurance, Inc. v. Days Cal. Riverside Ltd. Partnership, 27 F.3d 374, 376 (9th Cir. 1994); T-H New Orleans Ltd. Partnership v. Financial Sec. Assurance, Inc., 10 F.3d 1099, 1114 (5th Cir. 1993), cert. denied, 114 S. Ct. 1833 (1994)).

236. 83 F.3d 1360 (11th Cir. 1996).

237. See id. at 1366.

238. Id. at 1361.

239. Id. at 1362; see also 11 U.S.C. § 726(a)(5) (1994).

240. 83 F.3d at 1362.

241. Id.

242. Id. at 1363 (quoting 11 U.S.C. § 726(a)(5)).

243. Id. (citing 11 U.S.C. § 330 (1994) (setting forth the standard and procedure for compensating officers of the estate)).
\end{footnotesize}
normally at or near the end of the case. Noting that under the statutory provisions on compensation a trustee or professional does not have a claim until the fee is awarded, the Eleventh Circuit concluded that the time for the interest to begin accruing was the date of the actual fee award.

XII. MORTGAGE FORECLOSURES AND CHAPTER 13 CASES

A debtor's attempt to cure a mortgage default through a Chapter 13 plan after foreclosure was the issue before the Eleventh Circuit in Commercial Federal Mortgage Corp. v. Smith (In re Smith). Commercial Federal, the mortgage holder on the debtor's residence, conducted a valid foreclosure sale and purchased the property after Smith defaulted on the mortgage. Less than three months later, Smith filed a Chapter 13 bankruptcy petition. In his Chapter 13 plan, Smith proposed to reinstate the mortgage by paying prepetition arrearage through the plan and remaining current on the monthly mortgage payments to Commercial Federal. He argued that under Alabama law, he had the right to redeem the mortgage for one year after foreclosure by paying a one-time lump sum for the full amount due and that this right could be modified by allowing him to cure the default through his plan.

The Eleventh Circuit framed the issue as "whether 11 U.S.C. § 1322(b) permits a debtor to exercise his state statutory right of redemption in a Chapter 13 plan by 'curing' a default and 'reinstating' a mortgage after a valid foreclosure sale of his property." Under section 1322(b) of the Bankruptcy Code, a debtor may not modify the rights of a mortgage holder through a Chapter 13 plan. Smith argued that this provision did not prevent him from modifying his statutory right of redemption. The Eleventh Circuit, however, disagreed and concluded that even though this redemption right became property of the bankruptcy estate, Smith could only exercise that right by making the one-time

244. Id. at 1363-64. It appears that by awarding the interest from the date of appointment or the date of the fee application, the bankruptcy and district courts were trying to reach a compromise solution. Id. at 1364 n.3.
245. Id. at 1365-66; see also Boldt v. Crake (In re Riverside-Linden Inv. Co.), 945 F.2d 320 (9th Cir. 1991); In re Brown, 190 B.R. 689 (Bankr. M.D. Fla. 1996).
246. 85 F.3d 1555 (11th Cir. 1996).
247. Id. at 1555.
248. Id. (citing Ala. Code § 6-5-251 (1993)).
249. Id. (quoting 11 U.S.C. § 1332(b) (1994)).
251. 85 F.3d at 1558.
252. Id.
payment as required by the statute. 253 Significantly, Smith filed for bankruptcy protection after the valid foreclosure by Commercial Federal, and the event "drew a bright-line termination date of the right to cure a default through a Chapter 13 plan." 254 Thus, Smith's statutory right of redemption could not be modified by his Chapter 13 plan to allow him to cure the default on his mortgage. 255

XIII. RULES OF Procedure

A. Failure to State a Claim

In Brandt v. First Union Corp. (In re Southeast Banking Corp.), 256 the Eleventh Circuit dismissed a Chapter 7 trustee's complaint for failure to state a claim in accordance with rule 12(b)(6) of the Federal Rules of Civil Procedure. 257 The debtor in this case was a holding company that owned all the shares of Southeast Bank in Florida. Prior to bankruptcy, the debtor and First Union entered into an agreement to discuss the possibility of a merger. Under the agreement, First Union had access to confidential information regarding the debtor's financial condition. Sometime thereafter, state and federal regulators closed the debtor's bank, and First Union bought its assets through an auction. The trustee then commenced a civil action against First Union, claiming that First Union leaked its financial information to the regulators, thus resulting in the bank's closure. The trustee also claimed that at that time the bank actually was solvent and otherwise financially sound. 258 The district court dismissed the trustee's complaint for failure to state a claim, and the Eleventh Circuit affirmed. 259

In affirming, the Eleventh Circuit noted that the basic claim of the trustee was that the bank "was liquid and should not have been closed." 260 The decision to close the bank was made by federal regulators, but the regulators were not subject to suit for taking such a discretionary action. 261 The Eleventh Circuit stated that the trustee's claim against First Union was merely an attempt to "do what it

253. Id. at 1560-61.
254. Id. at 1560 (citing Federal Land Bank v. Glenn (In re Glenn), 760 F.2d 1428, 1435 (6th Cir.), cert. denied, 474 U.S. 849 (1985)).
255. Id. at 1561.
256. 93 F.3d 750 (11th Cir. 1996) (per curiam).
257. FED. R. CIV. P. 12(b)(6).
258. 93 F.3d at 751.
259. Id. at 751-52.
260. Id. at 751.
261. Id.
otherwise could not do, sue for its damages as a result of the government's alleged improper closure of Southeast Bank. Because the trustee's complaint was based on a discretionary act of federal regulators, it failed to state a claim for relief.

B. Timely Appeal

A Chapter 7 trustee found himself the victim of his own procedural error in Florida v. Brandt (In re Southeast Bank Corp.). The trustee sought a determination that certain taxes on the debtor's art collection were invalid. The bankruptcy court ruled that the taxes were valid and entered an order in favor of the taxing authority on October 1, 1993. Three days later, on October 4, the bankruptcy court entered a memorandum opinion explaining the reasons for the order. The trustee filed a motion for reconsideration on October 13, which was nine days after the memorandum opinion but twelve days after the entry of the actual order. The bankruptcy court subsequently granted the motion and entered a judgment concluding that the taxes were invalid, and the district court affirmed.

On further appeal, the Eleventh Circuit reversed. According to rule 59(e) of the Federal Rules of Civil Procedure, the trustee had ten days from the date of the bankruptcy court's order to file his motion for reconsideration. The Eleventh Circuit noted that the original bankruptcy court order was entered on October 1, 1993 and that the trustee's motion was filed on October 13, twelve days later. Because the motion was filed outside the ten day period required under rule

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262. Id. at 751-52.
263. Id. at 752.
264. 97 F.3d 476 (11th Cir. 1996).
265. Id. at 477.
266. Id. at 477-78.
267. Id. at 478.
268. Id.
269. Id.
270. Id. at 479.
271. Id. at 478 (citing FED. R. CIV. P. 59(e) which provides that "[a]ny motion to alter or amend a judgment shall be filed no later than 10 days after entry of the judgment." Id. (made applicable to bankruptcy proceedings under FED. R. BANKR. P. 9023)).
272. Id. at 478. The Eleventh Circuit pointed out that under FED. R. CIV. P. 58, applicable to bankruptcy proceedings under FED. R. BANKR. P. 9021, the "brightline definition" for the entry of a judgment is the entry of a document separate from a memorandum opinion that sets forth the judgment. Id. Thus, the applicable date was the date of the entry of the order and not the date of the entry of the memorandum opinion.
59(e), the motion was untimely, and the bankruptcy court lacked jurisdiction to consider it.\textsuperscript{273}

XIV. NON\textsuperscript{2}BANKRUPTCY LAW

A. Rate Undercharge Claims

The trustee's ability to bring certain rate undercharge claims was presented to the Eleventh Circuit in Whitaker v. Frito-Lay, Inc. (\textit{In re Olympia Holding Corp.}).\textsuperscript{274} The trustee for a bankrupt motor common carrier brought an undercharge claim against Frito-Lay, a shipper, claiming that the debtor's tariffs on file with the Interstate Commerce Commission ("I.C.C." ) were invalid because they identified the shipper by code instead of by name.\textsuperscript{275} The trustee sought to have the coded rates declared void ab initio\textsuperscript{276} and collect from the shipper the difference between the discounted rate actually charged and the official class rate on file with the I.C.C.\textsuperscript{277} The Eleventh Circuit noted, however, that under the Negotiated Rates Act of 1993,\textsuperscript{278} Congress specifically validated the use of coded rates.\textsuperscript{279} Thus, contrary to the trustee's contention, the coded tariffs were legal.\textsuperscript{280} The court then concluded that it did not have the authority to retroactively reject a tariff because Congress only delegated such authority to the I.C.C.\textsuperscript{281} The trustee's claim was therefore dismissed.\textsuperscript{282}

B. State Law Issues

The res judicata effect of a foreclosure proceeding under Florida law on the value of collateral was at issue in \textit{Ob/Gyn Solutions, L.C. v. Six

\textsuperscript{273} Id.
\textsuperscript{274} 88 F.3d 952 (11th Cir. 1996).
\textsuperscript{275} 88 F.3d at 954-55.
\textsuperscript{276} Id. at 958.
\textsuperscript{277} Id. at 954.
\textsuperscript{279} 88 F.3d at 959-60.
\textsuperscript{280} Id. at 962.
\textsuperscript{281} Id. (citing I.C.C. v. American Trucking Ass'n, 467 U.S. 354, 367 (1984)). The court further noted that the I.C.C.'s ability to reject a tariff was extremely limited and could not be done in this case in view of Congress's clear expression of support for the coded tariffs. Id.
\textsuperscript{282} Id.
In this case, the debtor guaranteed a note secured by a mortgage. After default, the creditor obtained a final judgment of foreclosure determining the lien to be in the amount of $1,838,196.02 and then bid on the property for $1,200,000 at the judicial sale. The creditor later obtained a money judgment against the debtor in the full amount of the lien. The judgment, which the debtor did not challenge, failed to reflect the offset for the judicial sale or fair market value of the property. After the debtor filed for bankruptcy, the creditor filed a proof of claim reflecting the amount of the money judgment with an offset for the amount bid at the judicial sale. The debtor objected to the proof of claim.

After the bankruptcy and district courts sustained the debtor’s objection, the creditor appealed to the Eleventh Circuit. The issue on appeal was whether the principle of res judicata under Florida law prevented the debtor from challenging the claim that was based on a final state court judgment. The Eleventh Circuit, affirming the lower courts, noted that because the creditor included a “previously unadjudicated offset” in its claim, the creditor put in issue before the bankruptcy court the amount of the claim and the valuation of the property that was the basis for the claim. In other words, the creditor’s proof of claim admitted that the state court judgment did not reflect the actual value of the claim. Furthermore, the Eleventh Circuit noted that under Florida law a rebuttable presumption is created that the foreclosure bid price is equal to the property’s fair market value. The lower courts had found that the property that the creditor obtained through foreclosure was worth approximately $1,900,000. Because this value exceeded the amount of the state court judgment, the debtor’s debt was extinguished by the foreclosure, resulting in the creditor's claim being disallowed.

In Dayton Securities Associates v. Securities Group 1980 (In re Securities Group 1980), limited partners of the debtor found themselves obligated under New York law to make significant capital

283. 80 F.3d 452 (11th Cir. 1996).
284. Id. at 454.
285. Id. at 454-54.
286. Id. at 455.
287. Id. at 456.
288. Id. at 457.
289. Id. at 456.
290. Id.
291. Id. at 454.
292. Id. at 457.
293. 74 F.3d 1103 (11th Cir. 1996).
contributions to the trustee in bankruptcy even though they were no longer limited partners at the time of the bankruptcy. When the parties became limited partners, they agreed to make additional capital contributions to the limited partnership, an obligation which, if necessary, required them to personally and severally contribute an amount up to three times their initial capital contribution. At some point, the limited partners were bought out, and a few years later, the limited partnership filed for bankruptcy. Thereafter, the trustee demanded that all former limited partners make the additional capital contribution so that the debtor could pay off all creditors, but the former limited partners objected.

The certificates of the limited partners were part of the public record in New York, and the certificates noted the obligation of the limited partners to make the additional capital contribution, if necessary.

The Eleventh Circuit noted that under New York law, a limited partner is liable to the partnership for any unpaid contributions he has agreed on the certificate to make. Furthermore, New York law has a strong policy favoring the protection of creditors who extend credit to partnerships in view of a limited partner's promise of capital contributions. Therefore, the limited partners were liable for the capital contribution, at least with respect to the creditors who extended credit or whose claims arose before the limited partners left.

In *Lummus Corp. v. Unsecured Creditor's Committee of Lummus Industries, Inc. (In re Lummus Development Corp.)*, two creditors filed proofs of claim contending that they were entitled to the notes receivable of the debtor. The crux of the dispute was whether an asset purchase agreement between the two creditors conveyed the notes receivable from the one creditor, Lummus Industries, to the other creditor, Lummus Corporation. The Eleventh Circuit found that the unambiguous language of the asset purchase agreement did not indicate

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294. *Id.* at 1108.

295. *Id.* at 1105-06.

296. *Id.* at 1107-08.

297. *Id.* at 1108 (citing N.Y. PARTNERSHIP LAW § 106(1)(b) (McKinney 1988)).

298. *Id.* (citing N.Y. PARTNERSHIP LAW § 106(3)).

299. *Id.* This liability extended to two lease claims that arose after the limited partners withdrew from the partnership. The basis for their liability was the fact that the leases were entered into prior to their withdrawal. As such, the landlords relied on the publicly recorded certificates when they extended credit to the partnership. *Id.* at 1109-12.

300. 85 F.3d 575 (11th Cir. 1996).

301. *Id.* at 576.

302. *Id.* Lummus Industries was the debtor's parent corporation. *Id.*

303. *Id.*
that the notes receivable were being conveyed to Lummus Corporation. 304 Lummus Corporation, on the other hand, contended that the omission of the notes receivable was a mutual mistake. 306 Nevertheless, the Eleventh Circuit noted that under Georgia law, "if the agreement contains unambiguous language, the court gives the language its plain meaning." 308 Thus, in view of the agreement's plain language, the Eleventh Circuit affirmed the decisions of the lower courts that Lummus Industries, not Lummus Corporation, was entitled to the notes receivable. 307

304. Id. at 577. The value of this asset amounted to over $4.6 million. Id.
305. Id. at 576.
306. Id. at 577 (citing Georgia-Pacific Corp. v. Lieberam, 959 F.2d 901, 905 (11th Cir. 1992) (citing Hunsinger v. Lockheed Corp., 192 Ga. App. 781, 386 S.E.2d 537 (1989))).
307. Id.